

**CITY OF HARRISBURG, PENNSYLVANIA**

**SEWER REVENUE TRUST FUND**

**FINANCIAL STATEMENTS AND SUPPLEMENTARY  
INFORMATION**

**YEARS ENDED DECEMBER 31, 2006 AND 2005**

**WITH  
INDEPENDENT AUDITOR'S REPORT**

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**MAHER DUESSEL**

CERTIFIED PUBLIC ACCOUNTANTS

# CITY OF HARRISBURG, PENNSYLVANIA

## SEWER REVENUE TRUST FUND

YEARS ENDED DECEMBER 31, 2006 AND 2005

### TABLE OF CONTENTS

#### **Independent Auditor's Report**

#### **Financial Statements:**

Statements of Net Assets	1
Statements of Revenues, Expenses, and Changes in Net Assets	2
Statements of Cash Flows	3
Notes to Financial Statements	5

#### **Supplementary Schedules:**

Second Supplemental Agreement of Lease, Third Supplemental Agreement of Lease, and Collection System Lease:	
Reserve Requirement Calculation	23
Bond Covenant Requirement Calculation	24

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CERTIFIED PUBLIC ACCOUNTANTS

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## Independent Auditor's Report

The Honorable Stephen R. Reed, Mayor  
Members of City Council  
City of Harrisburg, Pennsylvania

We have audited the accompanying financial statements of the Sewer Revenue Trust Fund (an enterprise fund) of the City of Harrisburg, Pennsylvania (City) as of and for the years ended December 31, 2006 and 2005, as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these financial statements based on our audits. The prior year financial statements were audited by other auditors whose report, dated June 12, 2006, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Sewer Revenue Trust Fund of the City and do not purport to, and do not present fairly the financial position of the City, as of December 31, 2006 and 2005, and the changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Sewer Revenue Trust Fund of the City of Harrisburg, Pennsylvania as of December 31, 2006, and the changes in financial position and the cash flows thereof for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The Second Supplemental Agreement of Lease, Third Supplemental Agreement of Lease and Collection System Lease Reserve Requirement Calculation and Bond Covenant Requirement Calculation presented on pages 23 and 24 are presented for purposes of additional analysis and are not a required part of these basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

*Maher Duessel*

Harrisburg, Pennsylvania  
October 1, 2007

**City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund**

(an enterprise fund of the City of Harrisburg, Pennsylvania)

Statements of Net Assets

as of December 31, 2006 and 2005

	2006	2005
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents	\$ 2,163,692	\$ 1,763,958
Investments	720,503	934,053
Accounts receivable, net of allowance for uncollectible accounts of \$394,093 in 2006 and \$488,585 in 2005	2,895,283	2,831,622
Due from the City of Harrisburg General Fund	1,165,000	1,165,000
Other assets	542,382	607,577
Total current assets	<u>7,486,860</u>	<u>7,302,210</u>
Other assets		
Direct financing lease proceeds receivable from the City of Harrisburg	161,966	594,565
Total other assets	<u>161,966</u>	<u>594,565</u>
Capital assets, not being depreciated	751,605	374,526
Capital assets, net of accumulated depreciation of \$47,562,900 in 2006 and \$45,748,753 in 2005	40,073,546	41,374,727
	<u>40,825,151</u>	<u>41,749,253</u>
Total assets	<u>48,473,977</u>	<u>49,646,028</u>
<b>LIABILITIES</b>		
Current liabilities		
Accounts payable	353,815	280,554
Accrued expenses	36,066	31,777
Due to other funds	28,881	28,566
Due to other component units	2,269,418	2,413,253
Current portion of vested compensated absences	19,961	20,334
Current portion of workers' compensation	86,543	73,193
Current portion of future lease rentals payable	1,724,537	1,855,222
Current portion of bonds payable	45,483	45,073
Total current liabilities	<u>4,564,704</u>	<u>4,747,972</u>
Long-term liabilities		
Vested compensated absences	377,277	357,673
Workers' compensation	256,472	225,553
Future lease rentals payable	5,784,319	6,853,374
Bonds payable	123,674	158,288
Total long-term liabilities	<u>6,541,742</u>	<u>7,594,888</u>
Total liabilities	<u>11,106,446</u>	<u>12,342,860</u>
<b>NET ASSETS</b>		
Invested in capital assets, net of related debt	33,478,261	33,635,222
Unrestricted	3,889,270	3,667,946
Total net assets	<u>\$ 37,367,531</u>	<u>\$ 37,303,168</u>

The accompanying notes are an integral part of these financial statements.

**City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund**

(an enterprise fund of the City of Harrisburg, Pennsylvania)

Statements of Revenues, Expenses, and Changes in Net Assets

for the years ended December 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Operating revenues		
Charges for services	\$ 13,151,051	\$ 12,995,888
Operating expenses		
Salaries and wages	1,829,075	1,757,319
Fringe benefits	618,030	305,546
Communications	23,024	21,611
Professional fees	340,845	521,697
Utilities	1,861,527	1,827,661
Insurance	316,125	310,948
Maintenance and repairs	249,862	324,507
Contracted services	5,260,728	5,824,093
Supplies	624,691	488,279
Depreciation	1,829,405	2,081,842
Total operating expenses	<u>12,953,312</u>	<u>13,463,503</u>
Operating income (loss)	<u>197,739</u>	<u>(467,615)</u>
Nonoperating revenue (expenses)		
Grant subsidy	657,537	-
Investment income	91,134	32,986
Interest expense	(880,352)	(936,714)
Loss on disposal of assets	(1,695)	-
Total nonoperating revenue (expenses)	<u>(133,376)</u>	<u>(903,728)</u>
Change in net assets	64,363	(1,371,343)
Net assets - beginning of year	<u>37,303,168</u>	<u>38,674,511</u>
Net assets - end of year	<u>\$ 37,367,531</u>	<u>\$ 37,303,168</u>

The accompanying notes are an integral part of these financial statements.

**City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund**

(an enterprise fund of the City of Harrisburg, Pennsylvania)

## Statements of Cash Flows

for the years ended December 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Cash flows from operating activities		
Received from user charges	\$ 13,087,390	\$ 12,876,475
Payments to employees for services	(1,809,844)	(1,742,305)
Payments for fringe benefits	(618,030)	(305,546)
Payments to suppliers for goods and services	<u>(8,212,026)</u>	<u>(9,138,001)</u>
Net cash provided by operating activities	<u>2,447,490</u>	<u>1,690,623</u>
Cash flows from noncapital financing activities		
(Increase) decrease in advances to City of Harrisburg General Fund	<u>315</u>	<u>12,924</u>
Net cash provided by (used in) noncapital financing activities	<u>315</u>	<u>12,924</u>
Cash flows from capital and related financing activities		
Acquisition and construction of capital assets	(45,967)	-
Lease and bond payments	<u>(2,258,131)</u>	<u>(2,237,214)</u>
Net cash used in capital and related financing activities	<u>(2,304,098)</u>	<u>(2,237,214)</u>
Cash flows from investing activities		
Sales (purchases) of investments	213,550	(427,719)
Interest on investments	<u>42,477</u>	<u>32,986</u>
Net cash provided by (used in) investing activities	<u>256,027</u>	<u>(394,733)</u>
Net increase (decrease) in cash and cash equivalents	399,734	(928,400)
Cash and cash equivalents - beginning of year	<u>1,763,958</u>	<u>2,692,358</u>
Cash and cash equivalents - end of year	<u>\$ 2,163,692</u>	<u>\$ 1,763,958</u>

(Continued)

**City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund**

(an enterprise fund of the City of Harrisburg, Pennsylvania)

Statements of Cash Flows (continued)

for the years ended December 31, 2006 and 2005

	<u>2006</u>	<u>2005</u>
Reconciliation of operating income (loss) to net cash cash provided by operating activities		
Operating income (loss)	\$ 197,739	\$ (467,615)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities		
Depreciation	1,829,405	2,081,842
Provision for uncollectible accounts	(94,492)	(208,789)
Changes in assets and liabilities		
Accounts receivable	30,831	89,376
Other assets	65,195	(37,670)
Direct financing lease	277,762	486,500
Vested compensated absences	19,231	15,014
Workers' compensation	44,269	(239,708)
Accounts payable and accrued expenses	77,550	(28,327)
Net cash provided by operating activities	<u>\$ 2,447,490</u>	<u>\$ 1,690,623</u>
Other cash flow information		
Cash payments for interest	<u>\$ 880,352</u>	<u>\$ 936,714</u>
Noncash investing, capital and financing activities		
Capital assets purchased by The Harrisburg Authority on behalf of the Sewer Revenue Trust Fund	<u>\$ 861,031</u>	<u>\$ 232,161</u>

(Concluded)

The accompanying notes are an integral part of these financial statements.

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**A. *Reporting Entity***

The City of Harrisburg, Pennsylvania (City) Sewer Revenue Trust Fund is used to account for the operating assets and liabilities of the sewage collection system and sewage conveyance and treatment system subleased and leased, respectively, by The Harrisburg Authority (Authority) to the City.

Long-term debt issued to finance capital additions relating to the sewage conveyance and treatment system and to the collection system, related debt sinking funds, and unexpended bond proceeds held in restricted trust accounts are reflected in the accounts of the Authority.

**B. *Basis of Accounting***

The accounting records of the Sewer Revenue Trust Fund are maintained on the accrual basis and are accounted for as an enterprise fund.

Enterprise funds are used to account for operations that are financed and operated in a manner similar to private business where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

The Sewer Revenue Trust Fund follows GASB Statement No. 20 *“Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting”* (Statement No. 20) for reporting and disclosure purposes. As permitted by Statement No. 20, the Sewer Revenue Trust Fund has elected not to apply Financial Accounting Standards Board pronouncements issued after November 30, 1989 unless the GASB specifically adopts the FASB Statement or Interpretation.

Enterprise funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with an enterprise fund’s principal ongoing operations. The principal operating revenues of the Sewer Revenue Trust Fund are charges to customers for sales and services. Operating expenses for the Sewer Revenue Trust Fund include the cost of sales and services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the Sewer Revenue Trust Fund’s policy to use restricted resources first, then unrestricted resources as they are needed.

The City maintains the accounts of the Sewer Revenue Trust Fund in sufficient detail to identify accounts receivable, and revenue and expenses of the collection system separately from those of the conveyance and treatment system, as required by the terms of the respective lease agreements with the Authority. Such amounts have been combined for presentation in the Sewer Revenue Trust Fund’s financial statements.

**City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund**  
(an enterprise fund of the City of Harrisburg, Pennsylvania)  
Notes to Financial Statements  
December 31, 2006 and 2005

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**C. *Cash and Cash Equivalents***

For the purposes of the statement of cash flows, highly liquid investments (including designated assets) with a maturity of three months or less when purchased are considered to be cash equivalents.

**D. *Investments***

The Sewer Revenue Trust Fund carries its investments at fair value. The fair value of the investments is based upon values provided by external investment managers and quoted market prices.

**E. *Allowance for Uncollectible Accounts***

The allowance for uncollectible accounts is based upon historic ratios developed from experience and other such factors which, in the judgment of City officials, deserve recognition in estimating possible losses. Management believes that they have adequately provided for future probable losses.

**F. *Capital Assets***

Capital assets are carried at cost. Capital assets are defined by the government as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of one year. Depreciation is computed using the straight-line method. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is recognized in income for the period. The cost of maintenance and repairs is charged to expense as incurred and significant renewals and betterments are capitalized.

**G. *Vested Compensated Absences***

Vested compensated absences represent vested portions of accumulated unpaid vacation, sick pay and other employee benefit amounts. It is the Sewer Revenue Trust Fund's policy to permit employees to accumulate a limited amount of earned but unused vacation, sick pay and other employee benefit amounts, which will be paid to employees upon separation from City service.

**H. *Net Assets***

Net assets are classified in the following categories:

***Invested in Capital Assets, Net of Related Debt*** – This category groups all capital assets, including infrastructure, into one component of net assets. Accumulated depreciation and the outstanding balances of debt that are attributable to the acquisition, construction or improvement of these assets reduce this category.

***Unrestricted Net Assets*** – This category represents the net assets of the Sewer Revenue Trust Fund, which are not restricted for any project or other purpose.

## City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund

(an enterprise fund of the City of Harrisburg, Pennsylvania)

Notes to Financial Statements

December 31, 2006 and 2005

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### 2. DEPOSITS AND INVESTMENTS

The deposit and investment policy of the Sewer Revenue Trust Fund is restricted by the terms of the Second Supplemental Agreement of Lease, the Third Supplemental Agreement of Lease and the Collection System Lease between the City and the Authority. Allowable deposits and investments are limited to direct obligations of the United States of America, shares in portfolios of the Pennsylvania Local Government Investment Trust Program and/or in savings or time deposits or certificates of deposit fully insured by the Federal Deposit Insurance Corporation, or certificates of deposit fully secured by direct obligations of the United States of America in one or more banks, savings and loan associations or mutual savings banks (inclusive of the Trustee); such deposits shall be subject to withdrawal upon not more than 6 months notice or prior to the date upon which such money will be required to be expended, whichever is earlier, and, to the extent not insured, shall be secured continuously by the depository in the manner required by laws of the Commonwealth of Pennsylvania.

The policy is further restricted with respect to the reserve fund, which is comprised of amounts accumulated in the Sewer Revenue accounts, after withdrawals for operating expense obligations, until the balance is such that the reserve shall equal the sum of (1) one-half of the lease rental due under the next lease year, and (2) one-half of the annual operating expenses as estimated by the consulting engineers, for the next succeeding lease year. With respect to the reserve fund, investments in direct obligations of the United States of America are limited to those having a maturity date or being subject to redemption at the option of the holder either within one year from the date of such investment or prior to the date upon which such money will be required to be expended, whichever is earlier. All cash, cash equivalents and investments except cash with fiscal agents are restricted pursuant to the reserve requirements.

The Sewer Revenue Trust Fund's deposit and investment policy is in compliance with the terms of the Second Supplemental Agreement of Lease, the Third Supplemental Agreement of Lease and the Collection System Lease.

#### A. *Deposits*

*Custodial Credit Risk.* Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. As of December 31, 2006 and 2005, the Sewer Revenue Trust Fund's book balance was \$2,163,692 and \$1,763,958 and the bank balance was \$2,078,850 and \$1,763,813. Of the bank balance for December 31, 2006 and 2005, \$100,000 and \$100,000 was covered by federal depository insurance and \$1,978,850 and \$1,663,813 was collateralized under Act No. 72 of the 1971 Session of the Pennsylvania General Assembly, in which financial institutions were granted the authority to secure deposits of public bodies by pledging a pool of assets, as defined in the Act, to cover all public funds deposited in excess of Federal Depository Insurance limits.

#### B. *Investments*

The City of Harrisburg uses an external investment pool to ensure safety and maximize efficiency, liquidity, and yield for City funds. These funds are invested in the Pennsylvania Treasurer's INVEST Program for Local Governments and Nonprofits (INVEST) which

## City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund

(an enterprise fund of the City of Harrisburg, Pennsylvania)

Notes to Financial Statements

December 31, 2006 and 2005

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separately issues audited financial statements which are available to the public. The fair value of the City's position in the external investment pool is equivalent to the value of the pool shares. The Commonwealth of Pennsylvania provides external regulatory oversight of the pool.

The Sewer Revenue Trust Fund pools certain of its investments with the City of Harrisburg. The Sewer Revenue Trust Fund's position in the pooled funds at December 31, 2006 and 2005 was \$467,791 and \$459,954.

At December 31, 2006 and 2005, the fair value of the investments of the pooled and non-pooled funds of the City of Harrisburg was as follows:

	<u>Fair Value</u>
<u>December 31, 2006</u>	
Investments:	
Money market fund	\$ 1,092,264
External investment pool	<u>2,712</u>
Total	<u>\$ 1,094,976</u>
Reconciliation to total investments	
Non-pooled funds	\$ 2,712
Pooled funds	<u>1,092,264</u>
Total	<u>\$ 1,094,976</u>
	<u>Fair Value</u>
<u>December 31, 2005</u>	
Investments:	
Money market funds	\$ 16,019
External investment pool	474,099
U.S. Government agency obligations	243,266
U.S Government obligations	<u>1,048,752</u>
Total	<u>\$ 1,782,136</u>
Reconciliation to total investments	
Non-pooled funds	\$ 474,099
Pooled funds	<u>1,308,037</u>
Total	<u>\$ 1,782,136</u>

**City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund**

(an enterprise fund of the City of Harrisburg, Pennsylvania)

Notes to Financial Statements

December 31, 2006 and 2005

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**Custodial credit risk.** Custodial credit risk is the risk that the counterparty to an investment transaction will fail and the government will not recover the value of the investment or collateral securities that are in possession of an outside party. All investments of the City of Harrisburg are held by the counter party's trust department or agent but not in the City's name.

**Concentration of credit risk.** The City of Harrisburg places no limit on the amount it may invest in any one issuer. More than 5 percent of the City of Harrisburg's investments were held with the following issuers:

	<u>Fair Value</u>	<u>% of Total Investments</u>
<u>December 31, 2006</u>		
Wachovia money market fund	\$ 1,092,264	99.75%
<u>December 21, 2005</u>		
PA Treasury – Invest	\$ 474,099	26.60%
Federal Home Loan Bank	\$ 145,922	8.19%
Federal National Mortgage Association	\$ 97,344	5.46%

**Credit risk.** The City of Harrisburg's fixed income investments had the following level of exposure to credit risk:

	<u>Fair Value</u>	<u>Rating</u>
<u>December 31, 2006</u>		
Money market funds	\$ 1,092,264	Unrated
External investment pool	\$ 2,712	AAA
	<u>Fair Value</u>	<u>Rating</u>
<u>December 31, 2005</u>		
Money market funds	\$ 16,019	AAA
External investment pool	\$ 474,099	AAA
U.S. Government agency obligations	\$ 243,266	AAA

## City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund

(an enterprise fund of the City of Harrisburg, Pennsylvania)

Notes to Financial Statements

December 31, 2006 and 2005

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**Interest rate risk.** The Sewer Revenue Trust Fund's policy is to limit investments to those having a maturity date or being subject to redemption at the option of the holder either within one year from the date of such investment or prior to the date upon which such money will be required to be expended, whichever is earlier. The City of Harrisburg's investments mature as follows:

Investment Type	Fair Value	Investment maturity (in years)	
		Less than 1	1-5
<u>December 31, 2006</u>			
Money market funds	\$ 1,092,264	\$ 1,092,264	\$ -
External investment pool	<u>2,712</u>	<u>2,712</u>	<u>-</u>
Total	<u>\$ 1,094,976</u>	<u>\$ 1,094,976</u>	<u>\$ -</u>
<u>December 31, 2005</u>			
Money market funds	\$ 16,019	\$ 16,019	\$ -
External investment pool	474,099	474,099	-
U.S. Government agency obligations	<u>243,266</u>	<u>-</u>	<u>243,266</u>
Total	<u>\$ 733,384</u>	<u>\$ 490,118</u>	<u>\$ 243,266</u>

### 3. WORKERS' COMPENSATION DEPOSIT

In accordance with the provisions of the Pennsylvania Workers' Compensation Act, the City has secured an exemption from the necessity of insuring its workers' compensation liability and has elected to maintain a separate fund to provide a reserve for claimants entitled to benefits. Since inception, a total of \$600,000 has been deposited in a bank trust account through December 31, 2006. Interest of \$1,442,264 has been earned on deposits and claims of \$700,000 have been paid from the trust account from inception through December 31, 2006. During 2006, the City withdrew \$1.3 million to fund operating deficits of the general fund. At December 31, 2006, the City had deposited \$1,050,000 back into the fund, giving the City total assets held as reserves of \$1,092,264 at December 31, 2006. The amount of the deposit relating to the Sewer Revenue Trust Fund included in investments totaled \$717,791 and \$459,954 at December 31, 2006 and 2005.

**City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund**  
 (an enterprise fund of the City of Harrisburg, Pennsylvania)  
 Notes to Financial Statements  
 December 31, 2006 and 2005

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**4. CAPITAL ASSETS**

Capital asset activity for the year ended December 31, 2006, is as follows:

	Beginning of Year	Additions	Retirements and Dispositions	End of Year
Capital assets, not being depreciated:				
Land	\$ 361,421	\$ -	\$ -	\$ 361,421
Construction in progress	13,105	390,184	(13,105)	390,184
 Total capital assets, not being depreciated	 374,526	 390,184	 (13,105)	 751,605
Capital assets, being depreciated:				
Buildings	33,919,800	445,202	-	34,365,002
Improvements	2,666,415	19,547	-	2,685,962
Equipment and furniture	36,746,817	65,170	(16,953)	36,795,034
Infrastructure	13,790,448	-	-	13,790,448
 Total capital assets, being depreciated	 87,123,480	 529,919	 (16,953)	 87,636,446
Less accumulated depreciation for:				
Buildings	(15,838,393)	(697,406)	-	(16,535,799)
Improvements	(667,112)	(27,879)	-	(694,991)
Equipment and furniture	(23,449,760)	(969,569)	15,258	(24,404,071)
Infrastructure	(5,793,488)	(134,551)	-	(5,928,039)
 Total accumulated depreciation	 (45,748,753)	 (1,829,405)	 15,258	 (47,562,900)
 Total capital assets, being depreciated, net	 41,374,727	 (1,299,485)	 (1,695)	 40,073,546
 Capital assets, net	 \$ 41,749,253	 \$ (909,302)	 \$ (14,800)	 \$ 40,825,151

**City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund**  
(an enterprise fund of the City of Harrisburg, Pennsylvania)  
Notes to Financial Statements  
December 31, 2006 and 2005

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Capital asset activity for the year ended December 31, 2005, is as follows:

	Beginning of Year	Additions	Retirements and Dispositions	End of Year
Capital assets, not being depreciated:				
Land	\$ 361,421	\$ -	\$ -	\$ 361,421
Construction in progress	772,666	-	(759,561)	13,105
Total capital assets, not being depreciated	1,134,087	-	(759,561)	374,526
Capital assets, being depreciated:				
Buildings	33,687,639	232,161	-	33,919,800
Improvements	2,666,415	-	-	2,666,415
Equipment and furniture	35,987,256	759,561	-	36,746,817
Infrastructure	13,790,448	-	-	13,790,448
Total capital assets, being depreciated	86,131,758	991,722	-	87,123,480
Less accumulated depreciation for:				
Buildings	(15,116,070)	(722,323)	-	(15,838,393)
Improvements	(639,315)	(27,797)	-	(667,112)
Equipment and furniture	(22,252,612)	(1,197,148)	-	(23,449,760)
Infrastructure	(5,658,914)	(134,574)	-	(5,793,488)
Total accumulated depreciation	(43,666,911)	(2,081,842)	-	(45,748,753)
Total capital assets, being depreciated, net	42,464,847	(1,090,120)	-	41,374,727
Capital assets, net	<u>\$ 43,598,934</u>	<u>\$(1,090,120)</u>	<u>\$ (759,561)</u>	<u>\$ 41,749,253</u>

Capital assets at December 31, 2006 and 2005, with estimated lives, are as follows:

	Estimated Life
Buildings	50 – 100 years
Improvements	40 years
Equipment and furniture	5 – 25 years
Infrastructure	50 – 100 years

Depreciation is taken on a straight-line basis over the estimated useful life of the asset and amounted to \$1,829,405 and \$2,081,842 in 2006 and 2005, respectively.

**City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund**  
 (an enterprise fund of the City of Harrisburg, Pennsylvania)  
 Notes to Financial Statements  
 December 31, 2006 and 2005

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**5. RISK MANAGEMENT**

The Sewer Revenue Trust Fund is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City purchases commercial insurance for all risks of loss except those related to injuries of employees. Settled claims have not exceeded this commercial coverage in any of the past three fiscal years.

The Sewer Revenue Trust Fund is self insured for workers' compensation. As a self-insurer, the Sewer Revenue Trust Fund is required to fund an already established trust fund, dollar for dollar, once the City has passed total liability threshold of \$3,471,552 as established by the Commonwealth of Pennsylvania. Accordingly, the City has established a trust fund for workers' compensation claims, but has not had to fund it as the City's current outstanding liability for claims incurred at December 31, 2006 does not exceed the established threshold. The Sewer Revenue Trust Fund provides coverage for up to a maximum of \$500,000 for each workers' compensation claim, and has purchased commercial coverage for claims in excess of coverage provided by the Sewer Revenue Trust Fund.

The Sewer Revenue Trust Fund has recorded a liability for outstanding workers' compensation claims, included with accrued expenses, in the amount of \$343,015 and \$298,746 at December 31, 2006 and 2005, respectively. This claims liability is discounted to present value at a discount rate of 5% and is based on the requirements of Governmental Accounting Standards Board Statement No. 10, which requires that a liability for claims be reported if information prior to the issuance of the financial statements indicates that it is probable that a liability has been incurred at the date of the financial statements and the amount of the loss can be reasonably estimated.

Changes in the claims liability amounts in fiscal years 2006 and 2005 were as follows:

	<u>2006</u>	<u>2005</u>
Balance – January 1	\$ 298,746	\$ 538,454
Current year claims and changes in estimates	155,510	(190,506)
Claim payments	<u>(111,241)</u>	<u>(49,202)</u>
Balance – December 31	343,015	298,746
Current portion	<u>86,543</u>	<u>73,193</u>
Long-term portion	<u>\$ 256,472</u>	<u>\$ 225,553</u>

**6. COMMITMENTS AND CONTINGENCIES**

*Future Lease Rentals Payable*

On October 1, 1984, the City entered into a supplemental lease agreement pursuant to the refunding of the Authority's Guaranteed Sewer Revenue Bonds, Series of 1978. The 1984 Second Supplemental Agreement of Lease provides for rental payments in the amount sufficient to retire bonds issued to finance the cost of major construction improvements to the sewage conveyance and treatment system. Also included are interest and administrative costs of the Authority.

On January 15, 1988, the City entered into a Third Supplemental Agreement of Lease and a Collection System Lease pursuant to the issuance of the Authority's Sewer Revenue Bonds, Series A and B of 1988, respectively. The Third Supplemental Agreement of Lease was entered into providing for rental payments in an amount sufficient to retire bonds issued to finance the Series A Project relating to the sewage conveyance and treatment system. The Collection System Lease was entered into providing for rental payments in an amount sufficient to retire bonds issued to finance the Series B Project relating to the sewage collection system.

In accordance with the lease agreements, the City is required to make the following minimum annual lease rental payments:

Lease Year Ending December 31,	Basic Lease Rental	Authority Administrative Expense	Total
2007	\$ 1,854,341	\$ 100,000	\$ 1,954,341
2008	1,857,422	60,000	1,917,422
2009	1,858,081	60,000	1,918,081
2010	1,861,382	60,000	1,921,382
2011	1,855,497	60,000	1,915,497
Total minimum lease payments	9,286,723	<u>\$ 340,000</u>	<u>\$ 9,626,723</u>
Less amount representing interest	<u>(1,777,867)</u>		
Present value of net minimum lease payments	7,508,856		
Current portion	<u>1,724,537</u>		
Long-term portion	<u>\$ 5,784,319</u>		

## City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund

(an enterprise fund of the City of Harrisburg, Pennsylvania)

Notes to Financial Statements

December 31, 2006 and 2005

The net book value of equipment held under capital leases included in capital assets was \$14,088,171 and \$14,262,765 at December 31, 2006 and 2005, respectively. In addition, the Fund has direct financing lease proceeds receivable totaling \$161,966 and \$594,565 at December 31, 2006 and 2005, respectively, which represent funds available for future construction of improvements to the sewage conveyance, treatment and collection systems under the lease agreements. Construction of improvements to these systems under the lease agreements was \$861,031 and \$232,160 during 2006 and 2005, respectively. Capital assets under the lease agreement have been treated as noncash transactions in the Statements of Cash Flows.

The City is required under the terms of the Second Supplemental Agreement of Lease, the Third Supplemental Agreement of Lease and Collection System Lease to make additional rental payments within 190 days after the end of each year, equal to excess funds in the Sewer Revenue Trust Fund as defined in the respective lease agreements. There were no excess funds at December 31, 2006 and 2005, accordingly, no additional payment was due.

### 7. LONG-TERM LIABILITIES

Long-term liability activity for the year ended December 31, 2006, is as follows:

	Beginning of year	Additions	Accretion/ Amortization	Retirements	End of Year	Current Portion
Vested compensated absences	\$ 378,007	\$ 312,692	\$ -	\$ (293,461)	\$ 397,238	\$ 19,961
Workers' compensation	298,746	155,510	-	(111,241)	343,015	86,543
Future lease rentals payable (note 6)	8,708,596	-	-	(1,199,740)	7,508,856	1,724,537
Bonds payable	203,361	-	12,232	(46,436)	169,157	45,483
Total long-term liabilities	<u>\$ 9,588,710</u>	<u>\$ 468,202</u>	<u>\$ 12,232</u>	<u>\$ (1,650,878)</u>	<u>\$ 8,418,266</u>	<u>\$ 1,876,524</u>

Long-term liability activity for the year ended December 31, 2005, is as follows:

	Beginning of year	Additions	Accretion/ Amortization	Retirements	End of Year	Current Portion
Vested compensated absences	\$ 362,993	\$ 273,531	\$ -	\$ (258,517)	\$ 378,007	\$ 20,334
Workers' compensation	538,454	(190,506)	-	(49,202)	298,746	73,193
Future lease rentals payable (note 6)	9,827,270	-	-	(1,118,674)	8,708,596	1,855,222
Bonds payable	234,472	-	14,077	(45,188)	203,361	45,073
Total long-term liabilities	<u>\$ 10,963,189</u>	<u>\$ 83,025</u>	<u>\$ 14,077</u>	<u>\$ (1,471,581)</u>	<u>\$ 9,588,710</u>	<u>\$ 1,993,822</u>

On December 28, 1995, the City issued Federally Taxable General Obligation Bonds, Series A of 1995 and Federally Taxable General Obligation Bonds, Series B of 1995 in the aggregate principal amount of \$35,734,416 (plus accrued interest of \$16,495, less original issue and

## City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund

(an enterprise fund of the City of Harrisburg, Pennsylvania)

Notes to Financial Statements

December 31, 2006 and 2005

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underwriters' discounts of \$543,380) with interest rates ranging from 5.60% to 6.84% to fund the City's unfunded actuarial accrued pension liability and a reserve for the payment of the principal amortization component of the City's 1996 Minimum Municipal Obligation (MMO) payment required under Act 205. The net proceeds of \$33,892,502 (after payment of \$735,452 in issuance costs and a deposit of \$579,577 to the MMO escrow fund) were paid to the Pennsylvania Municipal Retirement System to fund the actuarial accrued pension liability. On December 30, 1997, the City issued \$12,840,000 of Federally Taxable General Obligation Bonds, Series E of 1997, with interest rates ranging from 6.35% to 6.42% to advance refund \$10,760,249 (\$9,402,812 in principal and \$1,357,437 of accumulated interest) of General Obligation, Series A and B of 1995, with interest rates ranging from 5.65% to 7.24%. The net proceeds of \$12,661,384 (after payment of \$178,616 in underwriting fees, insurance and other issuance costs) were deposited in escrow to defease the Series A and B of 1995 bonds maturing on April 1, 1998 as well as those maturing on April 1, 2011 through April 1, 2019.

These bonds are payable in annual installments of \$3,092,157 to \$3,638,650 through April 1, 2010 and will be serviced through general revenues of the City and through sewer operating revenues. The bonds were allocated proportionately between the City's governmental activities and the Sewer Revenue Trust Fund based upon the related unfunded actuarial accrued pension liability. The amount outstanding at December 31, 2006 and 2005 in the Sewer Revenue Trust Fund was \$169,157 and \$203,361, respectively.

The annual requirements to amortize these bonds outstanding as of December 31, 2006 are as follows:

	City of Harrisburg		Sewer Revenue Trust Fund		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
2007	\$ 3,593,167	\$ 119,833	\$ 45,483	\$ 1,517	\$ 3,638,650	\$ 121,350
2008	3,411,226	356,087	43,180	4,507	3,454,406	360,594
2009	3,288,392	597,421	41,625	7,562	3,330,017	604,983
2010	3,053,288	815,044	38,869	10,318	3,092,157	825,362
Total	<u>\$ 13,346,073</u>	<u>\$ 1,888,385</u>	<u>\$ 169,157</u>	<u>\$ 23,904</u>	<u>\$ 13,515,230</u>	<u>\$ 1,912,289</u>

## **8. PENSION PLANS**

### **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

#### *Basis of Accounting*

The plan's financial statements are prepared using the accrual basis of accounting. Plan members' contributions are recognized in the period in which the contributions are due. Employer contributions are recognized in the period in which the contributions are due, in accordance with Act 205 - 1984, as amended. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

#### *Method Used to Value Investments*

Investments are reported at fair value. The plan's assets with PMRS are pooled for investment purposes and, therefore, do not represent specific identifiable investment securities.

#### *Plan Description*

The Sewer Revenue Trust Fund contributes to the City's Non-uniformed Employees' pension plans with the Pennsylvania Municipal Retirement System (PMRS), an agent multiple-employer public retirement system (PERS). On January 2, 2002, the assets of Plans A and B were combined, but the requirements for eligibility and benefits remain the same. Employees become eligible for participation in a plan immediately upon employment and become fully vested after 20 years of service for City A plans and 10 years for City B plans. The plans have been established by City ordinance in accordance with the authority for municipal contributions required by Act 205-1984 of the Pennsylvania legislature, as amended by Act 189-1990. The plans require covered employees to contribute a percentage of total compensation.

PMRS issues publicly available financial reports that include financial statements and required supplementary information for PERS. That report may be obtained by writing to the Pennsylvania Municipal Retirement System, P.O. Box 1165, Harrisburg, PA 17108-1165 or by calling 1-800-622-7968.

The benefits provided by the plans differ by employment group and are based upon average compensation and length of service. Normal benefits are calculated at 2.5% per year of credited service multiplied by the final average annual salary for the Non-uniformed Employees' A plan. In no case may the benefit exceed 50% of the final average annual salary. The benefits provided by the Non-uniformed Employees' B plan are calculated at 2.0% per year of credited service multiplied by the final average annual salary. In no case may the benefit exceed 75% of the final average annual salary.

The plans provide retirement, disability and death benefits to plan members and their beneficiaries. Cost-of-living allowances are provided at the discretion of the plan.

In addition, Non-uniformed Employees' A plan is closed to new entrants.

## City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund

(an enterprise fund of the City of Harrisburg, Pennsylvania)

Notes to Financial Statements

December 31, 2006 and 2005

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### *Funding Policy*

Act 205 requires that annual contributions be based upon the plan's minimum municipal obligation (MMO). The MMO is based upon the plan's bi-annual actuarial valuation.

Contributions by the City are determined under the entry age normal method. Unfunded past service liability is amortized over the average future service of active participants.

Employee contributions to the plan are based on a percentage of compensation. Non-uniformed employees contribute 4.0-6.0% and 5.0% of annual compensation for Plan A and B, respectively. An interest rate of 6.0% is applied to the employees' account. Employees' accumulated contributions plus interest will be returned upon termination or death if no other benefits are payable under the plan. The plans are also eligible to receive an allocation of state aid from the General Municipal Pension System State Aid Program which must be used for pension funding. Any funding requirements established by the MMO in excess of employee contributions and state aid must be paid by the municipality in accordance with Act 205.

The Commonwealth of Pennsylvania allocates foreign fire and casualty insurance premium collections to aid individual municipalities. The monies received must be contributed to the pension plans or used to pay debt service on unfunded pension liability bonds. Significant actuarial assumptions used to compute the actuarially determined contribution requirements are the same as those used to compute the pension benefit obligation. Since 1996, the State's allocation exceeded the City's statutory funding requirements. Therefore, the City reflects no employer contributions to its pension plans during 2006 or 2005. State aid received in excess of City statutory funding requirements was not deposited to the pension plans but was utilized to fund debt service on the City's unfunded pension liability general obligation bonds issued in 1995 in accordance with Act 205 as amended.

The City had been participating in Level III of the State Act 205 Pension Plan Recovery Program, utilizing the 15-year delayed implementation of funding standard provision and amortizing the unfunded actuarial accrual liabilities under its pension plans established at January 1, 1985, over 40 years on the basis of level percentage of future payroll amortization. Prior to 1996, the allocation of general municipal pension system state aid the City received under Act 205 was based upon the City's costs of its pension plans since this amount was less than the amount determined under the unit value calculation.

In an effort to increase the amount of general municipal pension system state aid received by the City for its pension plans, the City passed a resolution in December 1995, to rescind its prior election to amortize the unfunded actuarial accrued liabilities of its plans established at January 1, 1985, over 40 years using level percentage of payroll amortization and began amortizing these amounts over 30 years using level dollar amortization. The January 1, 1996, actuarial valuation of the pension plan was prepared on the basis of 30-year level dollar amortization. The 1996 State aid received by the City was based upon the January 1, 1995, actuarial valuation reports which reflect 40-year level percentage of payroll amortization. The 1997 state aid received by the City will be based upon the January 1, 1996, actuarial valuation reports using 30-year level dollar amortization.

**City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund**

(an enterprise fund of the City of Harrisburg, Pennsylvania)

Notes to Financial Statements

December 31, 2006 and 2005

Also, the City contributed \$60,626 in 1995 in addition to its statutory funding requirement, or minimum municipal obligation (MMO) payments, in order to satisfy the full MMO for each plan in 1995 without regard to the 15-year phase-in provision. This allowed the City to determine the MMO's for its plans for 1996 without utilizing the delayed implementation of funding standard provision which required that the City make a contribution in 1996 to each plan which is at least equal to the contribution made by the City to each plan during 1995. This reduced the total MMO for each of the City's "A" plans beginning in 1996.

Administrative costs, including the investment manager, custodial trustee and actuarial services, are charged to the plan and funded through investment earnings.

***Annual Pension Cost and Net Pension Obligation***

The City's annual non-uniformed employees' pension cost and net pension obligation to the Plans at January 1, 2006 and 2005 are as follows:

	2006		2005	
	Plan A	Plan B	Plan A	Plan B
Annual required contribution	\$ -	\$ -	\$ -	\$ -
Contributions made	-	-	-	-
Change in net pension obligation	-	-	-	-
Net pension obligation – beginning of year	-	-	-	-
Net pension obligation – end of year	\$ -	\$ -	\$ -	\$ -

***Three-Year Trend Information***

Non-uniformed employees' – Plan A:

Calendar Year Ending	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
January 1, 2004	\$ -	- %	\$ -
January 1, 2005	\$ -	-	\$ -
January 1, 2006	\$ -	-	\$ -

**City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund**  
 (an enterprise fund of the City of Harrisburg, Pennsylvania)  
 Notes to Financial Statements  
 December 31, 2006 and 2005

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Non-uniformed employees' – Plan B:

Calendar Year Ending	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
January 1, 2004	\$ -	- %	\$ -
January 1, 2005	\$ -	-	\$ -
January 1, 2006	\$ -	-	\$ -

The annual required contribution for the current year was determined as part of the January 1, 2004 actuarial valuation using the entry age normal actuarial cost method. The actuarial assumptions include (a) a 6.00% investment rate of return (net of administrative expenses) and (b) projected salary increases of 4.70% per year. The assumptions do not include postretirement benefit increases, which are funded by State appropriation when granted. The actuarial value of assets is determined using market values determined by the trustee.

**9. RELATED PARTY TRANSACTION**

The City of Harrisburg General Fund provides certain administrative and operational services to the Sewer Revenue Trust Fund. Charges to the Sewer Revenue Trust Fund for administrative services and other expenses incurred were \$5,233,735 and \$5,798,954 for the years ended December 31, 2006 and 2005, respectively.

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**SUPPLEMENTARY SCHEDULES**

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**SECOND SUPPLEMENTAL AGREEMENT OF LEASE,  
THIRD SUPPLEMENTAL AGREEMENT OF LEASE, AND  
COLLECTION SYSTEM LEASE:**

**RESERVE REQUIREMENT CALCULATION AND  
BOND COVENANT REQUIREMENT CALCULATION**

**City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund**  
 (an enterprise fund of the City of Harrisburg, Pennsylvania)  
 Second Supplemental Agreement of Lease, Third Supplemental  
 Agreement of Lease, and Collection System Lease  
 December 31, 2006

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In accordance with the respective Articles 5 of the Second Supplemental Agreement of Lease as amended by the Third Supplemental Agreement of Lease and the Collection System Lease between The Harrisburg Authority and the City of Harrisburg, Pennsylvania, the Sewer Revenue Trust Fund is, at the end of each lease year, required to accumulate amounts in the Sewer Revenue accounts, after withdrawals for operating expense obligations, until the balance is such that the reserve shall equal the sum of (1) one-half of the lease rental due under the next lease year, and (2) one-half of the annual operating expenses as estimated by the consulting engineers, for the next succeeding lease year. Following is a computation of the reserve as of December 31, 2006, which the City is required to accumulate and maintain. Additionally, after the required reserve balance is attained, the City is required to pay any excess funds to The Harrisburg Authority within 190 days after the end of the year. The City may withdraw funds from the reserve account to satisfy lease payments as required by the Collection System Lease agreement.

Cash and investments – December 31, 2006	(1)	\$ 2,166,404
Amount due from the City of Harrisburg – December 31, 2006		1,165,000
Amounts pledged by the City for full satisfaction of obligations related to operations in Accordance with the lease Sections 5.02 and 5.03		
Accounts payable		(353,815)
Accrued expenses and other current obligations		(142,570)
Current receivables pledged to satisfy current liabilities		<u>496,385</u>
Total funds available		<u>\$ 3,331,404</u>
Required reserves		
Operation and maintenance expense reserve:		
Consulting engineers estimated operating costs - \$11,924,125 x 50%		\$ 5,962,063
2007 lease rental payment reserve:		
\$1,854,341 x 50%		<u>927,171</u>
Total reserve requirement		<u>\$ 6,889,234</u>
Required reserves in excess of funds available at December 31, 2006		<u>\$ (3,557,830)</u>

(1) Excludes workers' compensation investments of \$717,791

**City of Harrisburg, Pennsylvania Sewer Revenue Trust Fund**  
 (an enterprise fund of the City of Harrisburg, Pennsylvania)  
 Second Supplemental Agreement of Lease, Third Supplemental  
 Agreement of Lease, and Collection System Lease  
 December 31, 2006

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In accordance with the respective Sections 4.04 of the Second Supplemental Agreement of Lease as amended by the Third Supplemental Agreement of Lease and the Collection System Lease between The Harrisburg Authority and the City of Harrisburg, Pennsylvania, the following computation is provided to verify if a sewer rate change is required by the agreement:

Total operating expense (2006 cash basis), as defined in the agreement of lease	\$ 10,938,057
Minimum net rentals due – 2007	1,854,341
Established margin of safety (5% of minimum net rental – 2006)	<u>92,761</u>
Total covenant requirement	12,929,959
Total revenue (2006 cash basis)	13,100,370
Cash and investments – December 31, 2005      (1)	<u>2,238,057</u>
Excess revenue, cash, and investments over covenant requirement (2006 cash basis)	<u><u>\$ 2,408,468</u></u>

(1) Excludes workers' compensation investments of \$459,954