

CITY OF SALEM, VIRGINIA



COMPREHENSIVE ANNUAL FINANCIAL REPORT YEAR ENDED JUNE 30, 2012

DEPARTMENT OF FINANCE

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INTRODUCTORY SECTION



The introductory section of the City of Salem, Virginia's Comprehensive Annual Financial Report contains the Letter of Transmittal, which presents an overview of the profile of the City of Salem government, the local economic condition and outlook, major initiatives and accomplishments, and financial policies and financial planning. Also included in this section are an organizational chart and the Certificate of Achievement for Excellence in Financial Reporting awarded by the Government Financial Officers Association of the United States and Canada (GFOA) for the Comprehensive Annual Financial Report for the fiscal year ended June 30, 2011. It is the highest form of recognition in governmental financial reporting.

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November 20, 2012

**The Honorable Mayor, Members of City Council
and Citizens of Salem, Virginia**

In accordance with Section 8.9 of the Salem City Charter, we are pleased to present the City of Salem (the City) Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2012. The charter requires the City to issue an annual report on its financial position and activities and that the report be audited by an independent firm of certified public accountants. This report was prepared by the Department of Finance in conformity with generally accepted accounting principles (GAAP) as promulgated by the Government Accounting Standards Board (GASB).

Responsibility for both the accuracy of the data and the completeness and fairness of the presentation, including all disclosures, rests with the City. The data as presented is accurate in all material respects and is reported in a manner designed to present fairly the financial position and results of operations of the City as measured by the financial activity of various funds and component units. All disclosures necessary to enable the reader to gain the maximum understanding of the City's financial activity have been included.

The City has established a comprehensive internal control framework designed to both safeguard the government's assets against loss from unauthorized use or theft and to properly record and adequately document transactions in order to compile information for the presentation of the City's financial statements in conformity with GAAP. Because the cost of internal controls should not outweigh their benefits, the City's comprehensive framework of internal controls has been designed to provide reasonable rather than absolute assurance that the financial statements will be free from material misstatement.

Management's discussion and analysis (MD&A) on page 21 provides a narrative introduction, overview and analysis to assist users in interpreting the basic financial statements as required by GAAP. This letter is meant to complement the MD&A and should be read in conjunction with it.

Profile of the Government

Salem is located at the southern end of the Shenandoah Valley, approximately 190 miles west of Richmond and 250 miles southwest of Washington, DC. Its position in the southeastern United States gives the City ready access, within a 500-mile radius, to nearly two-thirds of the total population of the United States. In addition, the City lies at the region's crossroads of major rail and highway systems, making it a part of the principal trade, industrial, transportation, medical and cultural center of western Virginia.

Chartered by the Commonwealth of Virginia as a town in 1806 and as a city in 1968, Salem encompasses a land area of 14.4 square miles. The City's 2012 estimated population, 25,145 accounts for approximately 8.1% of the population in its metropolitan statistical area (MSA), which includes the neighboring City of Roanoke and Counties of Botetourt, Craig, Franklin and Roanoke.

The City of Salem operates under a council-manager form of government. The primary government provides a full range of services including general government administration, judicial administration, public safety, public works, health and welfare, parks and recreation, community development activities and support for education. The City also owns and operates an electric distribution system, water and sewage facilities and a civic center.

The financial reporting entity reflected in the CAFR, which is more fully described in Note 1 to the basic financial statements, conforms to the requirements of the Governmental Accounting Standards Board (GASB) Statement No. 14, as amended by GASB Statement No. 39. The accounting and reporting principles of the GASB are based on the fundamental concept that publicly elected officials are accountable to their constituents, and the financial statements should emphasize the primary government and permit financial statement users to distinguish between the primary government and its component units. There are several commissions and authorities where the City's accountability is limited to appointments to, or seats on, the respective boards. The City does not exercise financial or administrative control over these entities, so they are excluded from this report.

The City's reporting entity includes one discretely presented component unit, the City of Salem School Division. A component unit is a legally separate entity, which meets one of three conditions: the governing board is appointed by the primary government, the entity is fiscally dependent on the primary government, or excluding the entity could potentially result in misleading financial reporting. A five-member School Board appointed by City Council supervises operations of the School Division. The School Division receives significant financial support from the City. Given these conditions, the School Division is presented in a separate column in the government-wide financial statements to emphasize that it is legally separate from the primary government and to differentiate its financial position and results of operations from that of the primary government.

Local Economic Condition and Outlook

Salem has a large and diverse economic base that has enabled the City to fare better than other localities during the past several years of national recession. This base consists of industrial manufacturing, medical facilities, wholesale/retail trade, agriculture, accommodation and food services, higher education, rail transportation, banking services and regional utility services. Included in the manufacturing process are hi-tech electronics, medical equipment, tires, furniture, steel, tool and die and railroad equipment, just to name a few. Based on 4th quarter 2011 data from US Census Bureau, Salem experienced the largest number of new hires in health care, accommodation and food services, manufacturing, and retail trade industries.

Jobs in the medical field tend to be more recession proof than other industries and Salem is home to two of the largest medical facilities in the area, Lewis Gale Medical Center and the Salem Veterans Administration Medical Center. These hospitals are the two largest employers located in Salem, employing approximately 3,400 people.

Given current economic conditions, Salem is pleased to have growth continuing in the business community. General Electric and Yokohama Industries are Salem's largest manufacturing employers employing approximately 1,740 people. Yokohama, Salem's largest manufacturer, completed a \$13 million expansion in fiscal year 2011 and added approximately 80 new jobs in the current fiscal year. General Electric expanded the product line manufactured at its Salem location and hired approximately 80 people in the past year.

Graham-White Manufacturing Company supplies an assortment of new and remanufactured severe-duty pneumatic/electro-pneumatic valves and accessories to heavy rail, rail transit, military, truck and bus, and industrial clients worldwide. The company was purchased by Faiveley Transport, with the commitment to channel additional business and jobs to this area. Faiveley Transport is a 90-year-old publicly traded company with 5,000 employees in 24 countries on five continents.

QualiChem, which manufactures water based cutting and grinding fluids and water treatment chemicals, continued to experience growth. The company has undertaken an 11,000 foot expansion of its Salem facility and added approximately 15 jobs in the past year.

Salem became home to one of only 19 new Chick-Fil-A restaurants constructed in the last year in the United States. Chick-Fil-A, which previously had no presence in Salem, opened a new restaurant in June 2012. Chick-Fil-A is the second largest quick-service chicken restaurant chain in the United States, with over 1,615 locations in 39 states and Washington, D.C.

Salem Montessori School constructed a second facility on a parcel at the Salem Commerce Park. The building is approximately 10,000 square feet with six classrooms. The school was built to accommodate up to 182 students from three years of age through sixth grade.

A number of new businesses opened in Salem during the past year including Med Express, an urgent care facility, Aaron's Rentals, Newfangled Bride, Generations Medical Supply Store and Hidden Treasures, a consignment store. Frontline Eurosports, a new motorcycle shop specializing in BMW and Triumph brands, completed building renovations and opened during fiscal year 2012. The Salem location is one of only three locations in Virginia that sells BMW motorcycles. The 12,000 square foot business features a showroom and service shop. First Bank opened their first location in Salem and Hometown Bank purchased property with plans to build its first branch office in Salem.

Construction of new homes increased compared to prior years. Thirty-four new homes and townhouses with an assessed value of \$7.1 million were constructed in the City during fiscal year 2012. Construction continued in several different subdivisions in the City. Foreclosures were also down slightly from the previous year.

Despite continuing financial challenges, Salem was proud to provide an atmosphere and quality of life conducive to families and businesses. Over the years, Salem has been able to maintain stable property tax rates. Salem's unemployment rate of 6.5% is slightly above the state unemployment rate of 6%, but well below the national unemployment rate of 9.3%. A strong educational system providing a well-educated and skilled workforce along with generally lower operating costs is a key reason why employers have chosen to relocate in Salem and the rest of the Valley. The City's effort to retain existing business and industry is an integral part of its economic development efforts.

The City continued to face financial challenges intensified by unfunded State mandates and slow revenue growth. While general fund revenues increased \$1.5 million or 2.2%, expenditures increased \$1.6 million or 2.6%. Property taxes comprised approximately 48.9% of general fund revenues and showed growth from the prior year. Salem's real estate assessments rose a modest 1.3% in fiscal year 2012, resulting in tax revenue growth of \$175,000. Personal property tax revenue increased \$143,000 or 2.5%. New equipment purchases contributed to the \$288,000 or 11.1% increase in machinery and tools tax revenue.

Other local tax revenue increased \$860,000 or 5.1%. The meals tax rate was increased from 4% to 6% effective February 1, 2012 with the additional 2% committed to School Division capital needs. Meals tax revenue increased \$690,000 or 27.1% with approximately \$520,000 committed to the School Division as of June 30, 2012. Sales tax revenue showed encouraging growth of \$184,000 or 3.2%. Business license taxes, which are based on gross receipts, were up \$187,000 or 4.1% from fiscal year 2011.

Charges for services revenue increased \$237,000 or 5.3% largely due to higher charges for waste collection and disposal, offset by a corresponding increase in transportation and disposal costs. Income from the revenue recovery program was also higher than the previous year. Intergovernmental revenues remained fairly level with the prior year. An increase in highway maintenance funding was offset by declines in revenue from the state for Comprehensive Services for At Risk Youth and Families. Funding received under HB599 for public safety also declined.

Maintaining the high service levels to which our citizens are accustomed continued to be a challenge in fiscal year 2012. While it appears the economy is starting to improve and some revenue growth was experienced, the City continued to closely monitor spending. Limited hiring and capital equipment purchases were made. General fund expenditures increased \$1.6 million or 2.6% from the prior year. General government costs were up \$892,000 or 18.2%. Fiscal year 2012 was the first year of operation for the employee health clinic, which incurred expenditures of \$406,000. The purchase of software licenses also contributed to the increase. Public safety costs were up \$561,000 or 3.8% largely due to increased jail costs. Per diem rates and average daily prisoner population increased from the previous year. A new ambulance was purchased in fiscal year 2012 at a cost of \$168,000 with grant funding of \$92,000 covering a portion of the cost. Highway maintenance spending was \$300,000 higher than the previous year in the public works area.

Net assets of business-type activities declined \$2.4 million. Electric Fund net assets decreased \$1.6 million. Purchased power costs rose \$633,000 or 2.2%. To cover Electric Fund's share of the new ERP project, \$252,000 was transferred to capital projects fund. Transfers to the general fund were \$2,150,000 and represent a payment in lieu of taxes of \$1.5 million and \$650,000 in funding assistance for capital purchases.

Net assets of the Water and Sewage Fund decreased \$77,239 in fiscal year 2012. Effective July 1, 2010, a new rate structure and fee schedule for water and sewer services was instituted. Rates were increased January 1, 2011 and January 1, 2012 with an additional increase effective January 1, 2013. As such, charges for services increased \$1.1 million or 11.3% in fiscal year 2012. As part of the City's normal process of reviewing planned capital improvements, the City determined that certain projects would not proceed due to costs and other factors. Approximately \$300,000 in costs incurred for these projects were expensed in fiscal year 2012. In addition, \$252,000 was transferred to capital projects to cover the Water and Sewage fund share of the new ERP system. These one-time expenses contributed to the decrease in net assets.

Major Initiatives and Accomplishments

Salem City Council and Management are committed to making Salem a great place to live, work and raise a family. To that end, the City and School Board work diligently to provide one of the finest

school systems, not only in the region, but throughout the Commonwealth. All six Salem schools were fully accredited by the Virginia Department of Education and the Southern Association of Colleges and Schools (SACS). Each of Salem's six schools and the division as a whole have met or exceeded the Annual Measurable Objectives (AMO) under the *No Child Left Behind Act* for the 2011-2012 school year. The Virginia Board of Education recognized South Salem Elementary, West Salem Elementary and East Salem Elementary and the division overall with its Board of Education Excellence Award. G. W. Carver Elementary received the Governor's Award for Educational Excellence and Salem High and Andrew Lewis received the Competence to Excellence Award. G. W. Carver Elementary and East Salem Elementary were again recognized as "Distinguished Title I Schools" for the eighth consecutive year for exceeding ESEA achievement objectives. Dr. H. Alan Seibert, Superintendent, was named Region VI Superintendent of the Year. The region includes 15 area school divisions.

On April 24, 2012, the School Board awarded a \$14.9 million construction contract to Salem-based G&H Contracting to build a new South Salem Elementary School. The new school, which will be approximately 88,000 square feet, is scheduled to open in September 2013 in time for the start of the 2013-2014 school year. The new school will replace the current South Salem School that was built in the early 1960s. The circular design of the original building was cutting edge at the time, but over the years has proven to be a largely unforgiving design concept that has been unsuitable for expansion or renovation.

Salem continues to be active in tourism development as a means of economic development. The City participates with the Roanoke Valley Convention and Visitors Bureau to promote conventions and events in the region. The annual Salem Fair held at the Salem Civic Center is the largest fair in the state. Attendance at the Fair held in July 2011 was up 5% with nearly 315,000 in attendance. The Salem Red Sox played their fourth season at Salem Memorial Stadium with approximately 218,000 fans in attendance. Events such as Stagg Bowl, Roanoke Valley Horse Show, Olde Salem Days, NCAA Championships and many other events bring hundreds of thousands of participants, spectators and tourists to Salem and the surrounding area.

The NCAA awarded Salem and the Old Dominion Athletic Conference approval to serve as co-hosts for the Amos Alonzo Stagg Bowl and the Men's Division III Basketball championship through 2013. Besides football and basketball, the City was awarded women's softball through 2014. In 2012, Division III returned, while Division II softball comes back to town in 2013 and 2014. In addition, the City was awarded the NCAA Division II Women's Lacrosse Championship for 2014 with the games to be played at Kerr Stadium at Roanoke College. In 2012, nearly 8,500 people traveled to Salem to attend NCAA events held in the City, which included the Stagg Bowl, Division III Men's Basketball Championship and Division II and III Softball.

The James I. Moyer Complex hosted nearly 1,600 softball teams this year in tournaments that filled 12,667 hotel rooms in the area. Major tournaments included the ASA Men's Class C Fast Pitch National Tournament, ASA Girls 14U & 18U Eastern Fast Pitch Nationals, ISF Senior World Cup and the NCAA Division III National Softball Championship. The largest event at the Complex was the annual Chance Crawford Benefit Tournament with 132 teams participating.

In fiscal year 2012, the City and School Division began the implementation process for three new software projects to replace legacy financials, human resources, payroll, timekeeping, cashiering and billing systems. The need to streamline process and provide timely information has been the driving force for implementing new software.

New World Systems was selected for financials. They have provided solutions, including application, software, hardware, training and support for Local Government and Public Safety agencies since 1981 and service more than 1,000 public sector organizations nationwide. The first phase went live October 1, 2012 and included general ledger, purchase orders and accounts payable. Additional modules will be implemented in fiscal years 2013 and 2014.

Kronos, Inc. was selected for human resources, payroll and timekeeping. The company has provided workforce management solutions since 1977 and is widely recognized by industry analysts as a global leader in the workforce management market, servicing more than 30 million people around the world. The implementation process has begun and a planned first phase launch of human resources and timekeeping is schedule for early 2013.

PCI, LLC was selected for cashiering, billing and collection of real estate, personal property taxes and business taxes. The company has provided governmental cash receipting and revenue collection software since 1992. The City has utilized the company's cashiering software since August of 2000. An upgrade of the software to their full suite was completed and cashiering went live in July 2012. Real estate bills were processed in October 2012 utilizing the new system with personal property taxes and business taxes scheduled for late 2013.

In July 2011, an addition to the Police Department was completed. The Police Department building was expanded by 3,600 square feet to provide office space for a judge presiding on the U. S. Court of Appeals for the Fourth Circuit and his five member staff. In addition to the new offices, existing locker rooms were expanded. General Services Administration leased the office space from the City for a period of fifteen years with an optional five year renewal period.

A new records management/computer aided dispatch/mobile system was installed at the Police Department and became operational in fiscal year 2012. The new system allows officers to access the records management system real-time from their vehicles and is equipped with automatic vehicle locator

technology so dispatchers are able to see the exact location of each vehicle at all times. The new technology also offers the ability for officers to print summons from their vehicles, eliminating duplicate data entry.

The Civic Center's steam-based HVAC system was replaced with a hot water system that should reduce maintenance costs and result in a decline in energy consumption. The project included new boilers, temperature controls, air handlers and piping. New ceilings, floors and mixed use lighting were installed in the community room. Exterior and interior lighting, including offices, was also being replaced at the Civic Center. Motion sensors have been installed in offices to help reduce energy consumption. The total cost of the project was \$4.3 million.

The City completed a \$3.4 million sewer rehabilitation project, which substantially upgraded older areas of the sewer system. The project included lining of existing sewer lines, replacement of sewer lines, replacement of manholes and lids and manhole repair. This project is the second of a five-phase approach in improving the City's sewer system.

The City continued work on the very popular greenway trails. Construction began on Phase IIIA of the Roanoke River Greenway in fiscal year 2012. Phase IIIA extended the greenway approximately 1.3 miles from Eddy Street to Mill Lane. Funds from the American Recovery and Reinvestment Act were awarded to the City to pay for a portion of construction costs. Construction was also completed to connect two sections of the greenway trail at the Colorado Street Bridge.

Thanks to generous donations from businesses and individuals in the community, construction of a new dog park, Salem Rotary Dog Park, was completed in the fall of 2011. The park was constructed on a vacant lot owned by the City located beside the Animal Shelter.

City of Salem Street Department designed and constructed a new grill cover at Lewis Gale Field at the Ted Williams grilling area along the first base line. A 97-foot long picnic pavilion was also constructed along the left field line, providing a space for corporate and family events. These improvements will enhance the experience for families and large groups attending Salem Red Sox games.

The City and School Division are self-insured for health insurance with Anthem Blue Cross/Blue Shield managing the plan. In an effort to reduce costs of the City's health insurance plan and moderate future premium increases, the City opened an employee health clinic in the summer of 2011. The clinic is managed by Healthstat, the leading independent provider of on-site primary care, health risk intervention and disease management services. The clinic is available to all employees and their family members who have insurance through the City or School Division.

Financial Policies and Financial Planning

The City's annual budget is based upon the financial policies of the City and reflects the balance between anticipated revenues and proposed expenditures. As required by City Code, the City Manager submits a recommended budget to City Council thirty days prior to the last Council meeting in May of each year for the fiscal year beginning July 1st. After an extensive study process and a public hearing to receive citizen input, the City Council adopts the budget on or before June 30th.

The budget function is used as a management tool, including performance objectives, goals and long-range planning, as well as maintaining budgetary controls. The objective of these budgetary controls is to ensure compliance with legal provisions embodied in the annual appropriated budget approved by City Council. Activities of the General Fund, which incorporates debt service, are included in the annual budgetary control established at the fund level (that is, the level at which expenditures cannot legally exceed the appropriated amount.) The government also maintains an encumbrance accounting system as one technique of accomplishing budgetary control. Encumbered amounts lapse at year-end. However, encumbrances generally are re-appropriated as part of the following year's budget.

The City prepares a five-year capital improvement plan, which identifies and prioritizes major City projects and includes cost estimates and potential funding sources. The City closely monitors available funding and proceeds with capital purchases only as funds become available.

Independent Audit

Virginia law and the Charter of the City of Salem require that the financial statements of the City be audited by a certified public accountant selected by City Council. Brown, Edwards & Company, L.L.P., has performed an annual audit of the Comprehensive Annual Financial Report. Their audit was conducted in accordance with generally accepted auditing standards; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and *Specifications for Audits of Counties, Cities and Towns* issued by the Auditor of Public Accounts of the Commonwealth of Virginia. The auditor's report, which includes their opinion on the financial statements of the City, is contained in the Financial Section of this report. Other auditor's reports are included in the Compliance Section.

Certificate of Achievement for Excellence in Financial Reporting

The Government Finance Officers Association of the United States and Canada (GFOA) has awarded a Certificate of Achievement for Excellence in Financial Reporting to the City of Salem, Virginia, for its Comprehensive Annual Financial Report for 2011. This represents the twenty-fourth year Salem has earned this distinction. In order to be awarded a Certificate of Achievement, a government must

publish an easily readable and efficiently organized Comprehensive Annual Financial Report, whose contents conform to program standards. Such reports must satisfy both generally accepted accounting principles and applicable legal requirements. We believe this report conforms to the Certificate of Achievement Program requirements and standards and are submitting it to the GFOA to determine its eligibility for another certificate.

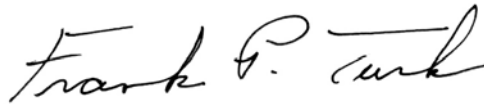
Acknowledgments

We would like to express our appreciation to the staff of the Department of Finance for the dedication and professionalism demonstrated daily assuring the financial integrity of the City and the preparation of this report. We would also like to express our appreciation to you, City Council, for the continued insight you bring to this City and the strong commitment you have made to its fiscal integrity and financial leadership. Lastly, we would like to express our appreciation to our independent auditing firm, Brown, Edwards & Company, L.L.P., for their cooperation and input in our efforts.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'KS Boggess', followed by a long horizontal flourish.

Kevin S. Boggess
City Manager

A handwritten signature in black ink that reads 'Frank P. Turk' in a cursive style.

Frank P. Turk
Director of Finance

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**CITY OF SALEM, VIRGINIA
DIRECTORY OF PRINCIPAL OFFICIALS
JUNE 30, 2012**

MEMBERS OF CITY COUNCIL

Byron R. Foley Mayor
John C. Givens..... Vice-Mayor
Lisa D. Garst Member
Jane W. Johnson Member
William D. Jones Member

ELECTED OFFICERS

Bonnie C. McCormack Treasurer
Linda M. Carroll Commissioner of the Revenue
Thomas E. Bowers Commonwealth's Attorney
Gary Chance Crawford Clerk of Circuit Court
Eric A. Atkins City Sheriff

GENERAL CITY GOVERNMENT

Kevin S. Boggess City Manager
James E. Taliaferro, II Assistant City Manager and Clerk of Council
Frank P. Turk Director of Finance
Stephen M. Yost City Attorney
Beth M. Austin Director of Human Resources
Mark R. Waldron Director of Management Information Systems
Angela A. Sellers Director of Technology Systems
Jeff A. Dudley Police Chief
Chester G. Counts Fire Chief
Charles E. Van Allman, Jr. City Engineer
Norman M. Tyler, Jr. Director of Streets and General Maintenance
John P. Shaner Director of Parks and Recreation
Janis C. Augustine Library Director
Dana M. Oliver Registrar
A. K. Briele, III Director of Electric Department
Caleb M. Taylor Director of Water and Sewer Department
S. Thomas Lander Real Estate Assessor
Todd W. Sutphin Building Official and Zoning Administrator
James M. Fender, Jr. Director of Solid Waste Disposal and Transfer Station
Melinda J. Payne Director of Planning and Economic Development
R. Carey Harveycutter, Jr. Director of Civic Facilities
Mike Stevens Director of Communications

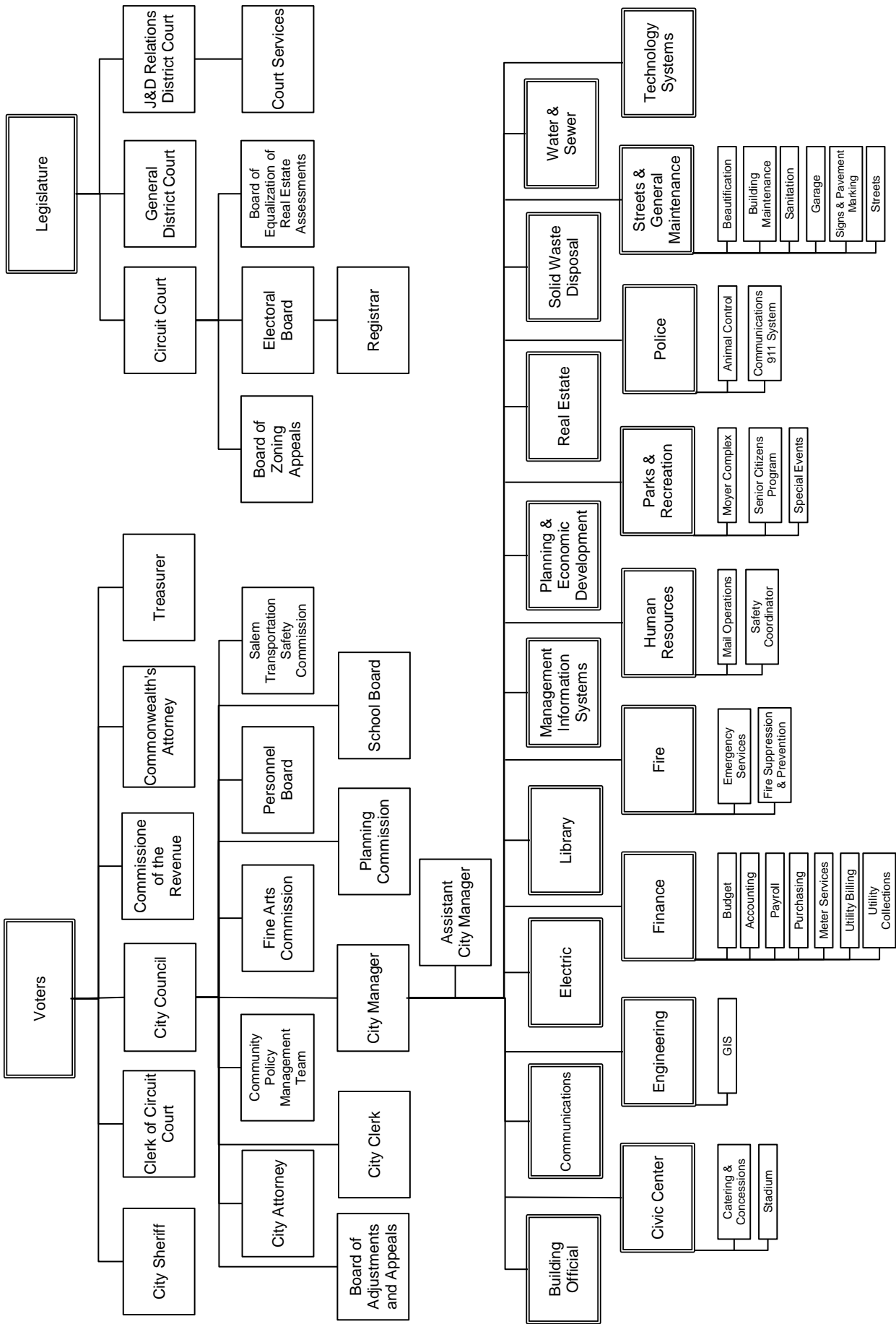
MEMBERS OF SCHOOL BOARD

Sarah W. Southard Chairman
David H. Preston Vice Chairman
Cindy W. Neathawk Member
Artice Ledbetter Member
Dr. Michael A. Chiglinsky Member

SCHOOL ADMINISTRATION

Dr. H. Alan Seibert Superintendent of Schools
Michael A. Bryant Assistant Superintendent
Frank P. Turk Director of Finance
Michael R. Crew Director of Business
Dr. Joseph T. Coleman Director of Assessment and School Principal
Dr. Darryl D. Helems Supervisor of Student Services
Curtis N. Hicks Director of Secondary Instruction
Russell L. Holladay Director of Personnel
Dr. Randy L. Jennings Supervisor of Special Education
Diane D. Washenberger Director of Elementary Instruction

CITY OF SALEM, VIRGINIA
ORGANIZATIONAL CHART
JUNE 30, 2012



Certificate of Achievement for Excellence in Financial Reporting

Presented to

City of Salem
Virginia

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2011

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



Linda C. Danison

President

Jeffrey R. Enen

Executive Director

FINANCIAL SECTION



The financial section of the City of Salem's Comprehensive Annual Financial Report includes the independent auditor's report, management's discussion and analysis, basic financial statements, including accompanying notes, required supplementary information, and other supplementary information.

INDEPENDENT AUDITOR'S REPORT

Honorable Members of City Council
City of Salem, Virginia
Salem, Virginia

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Salem, Virginia ("City"), as of and for the year ended June 30, 2012, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and *Specifications for Audits of Counties, Cities, and Towns*, issued by the Auditor of Public Accounts of the Commonwealth of Virginia. 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 opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City as of June 30, 2012, and the respective changes in financial position, and where applicable, cash flows thereof and the budgetary comparison statement for the general fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 20, 2012 on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, the Analysis of Funding Progress for Defined Benefit Pension Plan and the Analysis of Funding Progress for Other Postemployment Benefits as listed in the table of contents be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's financial statements as a whole. The introductory section, combining nonmajor fund financial statements, and statistical section are presented for purposes of additional analysis and are not a required part of the financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the financial statements. The combining nonmajor fund financial statements and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements as a whole. The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

Brown, Edwards & Company, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

Roanoke, Virginia
November 20, 2012

**CITY OF SALEM, VIRGINIA
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEAR ENDED JUNE 30, 2012**

The following discussion and analysis of the City of Salem, Virginia's (the City's) financial performance provides an overview of the City's financial activities for the fiscal year ended June 30, 2012. It should be read in conjunction with the transmittal letter and the City's basic financial statements.

FINANCIAL HIGHLIGHTS

- As of June 30, 2012, the City of Salem's primary government had \$140.5 million in total net assets, a decrease of \$1.8 million from prior year. Unrestricted net assets available to fund future expenses were \$7.8 million or 5.6% of total net assets and increased \$1.5 million.
- As of June 30, 2012, the governmental activities had \$77.8 million in total net assets, which increased \$0.6 million from prior year. Unrestricted net assets available to fund future expenses were \$(10.6) million or (13.6)% of total net assets and increased by \$2.0 million from prior year.
- As of June 30, 2012, the business-type activities had \$62.7 million in total net assets, a decrease of \$2.3 million from prior year. Unrestricted net assets available to fund future expenses were \$18.5 million or 29.4% of total net assets and decreased \$442,683 from prior year.
- As of June 30, 2012, the general fund had \$7 million in total fund balance, which increased by \$205,160 from prior year. Unassigned fund balance was \$3.5 million or 49.7% of total fund balance.

OVERVIEW OF THE FINANCIAL STATEMENTS

Our discussion and analysis is intended to serve as an introduction to the City's basic financial statements. The City's financial statements present two types of statements, each with a different focus on the City's finances. The government-wide financial statements focus on the City as a whole and provide both short-term and long-term information about the City's overall financial status. The fund financials focus on the individual parts of City government, reporting the City's operations in more detail than the government-wide statements. Presentation of both perspectives provides the user a broader overview, enhances the basis for comparisons and better reflects the City's accountability.

Government-Wide Financial Statements

The government-wide financial statements begin on page 35 and include the Statement of Net Assets and the Statement of Activities. These statements provide information about the City as a whole using the accrual basis of accounting, which is the method used by most private-sector enterprises. All current year revenues and expenses are reported in the Statement of Activities regardless of when cash is received or paid. These statements allow readers to answer the question "Is the City's financial position, as a whole, better or worse as a result of the year's activities?"

One of the main goals of these two statements is to report the City's net assets and changes that affected net assets during the fiscal year. The change in the City's net assets, which is the difference between assets and liabilities, is one way to measure the City's financial health or financial position. Increases or decreases in net assets are indicators of whether the City's financial health is improving or declining. Other non-financial factors, such as changes in the City's property tax base and the condition of the City's infrastructure should also be considered in assessing the overall financial health of the City.

In the Statement of Net Assets and the Statement of Activities, the City's fund-based activity is classified as follows:

Governmental activities – Most of the City's basic services are reported here including general government, judicial administration, public safety, public works, health and welfare, education, parks and recreation and community development. Property taxes, other local taxes and federal and state grants finance most of these activities.

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

Business-type activities – The City's electric distribution system, water and sewage systems, Civic Center and catering and concessions are reported here as the City charges a fee to customers designed to cover all or most of the cost of services it provides.

Component unit – The City includes a discretely presented component unit in this report, the City of Salem School Division (School Division). The City of Salem is financially accountable for the School Division, although it is a legally separate entity.

Fund Financial Statements

The fund financial statements begin on page 37 and provide detailed information about the most significant funds, rather than the City as a whole. The City has three types of funds.

Governmental funds – Most of the City's basic services are included in governmental funds. Fund based statements for these funds focus on how resources flow into and out of the funds and the balances left at year-end that are available for future spending. In particular, unassigned fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year. These funds are reported on the modified accrual basis of accounting, which measures cash and other liquid assets that can readily be converted to cash. The governmental fund statements provide a detailed short-term overview that helps the reader determine the financial resources that can be spent in the near future to finance the City's programs. The City's governmental funds include the general fund, debt service fund and capital projects fund. The differences between governmental activities as reported in the government-wide and fund financial statements are reconciled in Exhibits 4 and 6.

Proprietary funds – When the City charges customers for the services it provides, whether to outside customers or to other units of the City, these services are generally reported in proprietary funds. Proprietary funds, like the government-wide statements, utilize the accrual basis of accounting and their statements provide both short-term and long-term financial information.

The City's enterprise funds, one type of proprietary fund, are accounted for in the same manner as the government-wide business-type activities; however, the fund financial statements provide more detail and additional information, such as cash flows. The City's enterprise funds include the electric fund, water and sewage fund, Civic Center and catering and concessions.

Fiduciary funds – Resources held for other governments or agencies not part of the City are reported as fiduciary funds. These activities are excluded from the government-wide financial statements because the City cannot use these assets to finance its operations. The accounting used for fiduciary funds is much like that used for proprietary funds. The City reports assets for other postemployment benefits (OPEB) related to its healthcare plan for retirees in an OPEB trust fund and accounts for assets held on behalf of the Cardinal Criminal Justice Academy and the Court-Community Corrections Program as agency funds. Agency funds are custodial in nature and do not involve measurement of results of operations.

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

A comparative analysis of government-wide information is as follows:

Summary of Net Assets

The following table presents a condensed summary of net assets.

Summary of Net Assets (In Millions)								
	Governmental Activities		Business-type Activities		Total Primary Government		Component Unit	
	2012	2011	2012	2011	2012	2011	2012	2011
Current and other assets	\$ 11.9	\$12.1	\$23.7	\$30.8	\$ 35.6	\$ 42.9	\$ 8.3	\$ 9.2
Capital assets, net	97.5	99.7	98.9	101.0	196.4	200.7	37.8	37.9
Total assets	109.4	111.8	122.6	131.8	232.0	243.6	46.1	47.1
Current and other liabilities	3.5	4.0	5.4	10.5	8.9	14.5	4.7	4.3
Long-term liabilities	28.1	30.6	54.5	56.2	82.6	86.8	0.9	0.9
Total liabilities	31.6	34.6	59.9	66.7	91.5	101.3	5.6	5.2
Invested in capital assets, net of related debt	87.1	88.4	44.3	44.2	131.4	132.6	37.8	37.9
Restricted	1.3	1.4	-	2.0	1.3	3.4	-	-
Unrestricted	(10.6)	(12.6)	18.4	18.9	7.8	6.3	2.7	4.0
Total net assets	\$ 77.8	\$77.2	\$62.7	\$65.1	\$140.5	\$142.3	\$40.5	\$41.9

The primary government net assets decreased from \$142.3 million to \$140.5 million. Net assets of governmental activities increased \$0.6 million offset by a decrease of \$2.4 million in business-type activities. A detailed description of the changes in revenues and expenses that create the differences in net assets is discussed in the next section.

Net assets invested in capital assets, net of related debt, represents the amount of capital assets owned by the City, including infrastructure, net of accumulated depreciation and any outstanding debt issued to fund the asset purchase or construction.

The primary government's unrestricted net assets, the portion of net assets that can be used to finance the daily operations of the City was \$7.8 million, an increase of \$1.5 million from prior year. Debt totaling \$4.2 million issued for Civic Center improvements is being repaid by governmental activities while the related asset is recorded in business-type activities. The City also assumed \$11.1 million of debt issued for school improvements while the School Division recorded the related asset. As such, \$15.3 million is included in governmental activities long-term liabilities, which directly reduced unrestricted net assets.

Net assets are reported as restricted when constraints on asset use are externally imposed by creditors, grantors, contributors, regulators, or are imposed by law through constitutional provisions or enabling legislation. The City had restricted net assets totaling \$1.3 million as of June 30, 2012 for governmental activities. Approximately \$880,000 in state funding was received, but not yet spent, for highway maintenance. Approximately \$360,000 in federal and state public safety grant funding was received, but not yet spent, for fire programs, asset forfeiture and hazardous materials grants. Local funding of \$54,680 was restricted for the new ERP and greenway projects.

As of June 30, 2012, the component unit had \$40.5 million in total net assets, which decreased \$1.4 million from prior year. Unrestricted net assets available to fund future expenses were \$2.7 million or 6.8% of total net assets and decreased by \$1.3 million from prior year.

MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

Summary of Changes in Net Assets

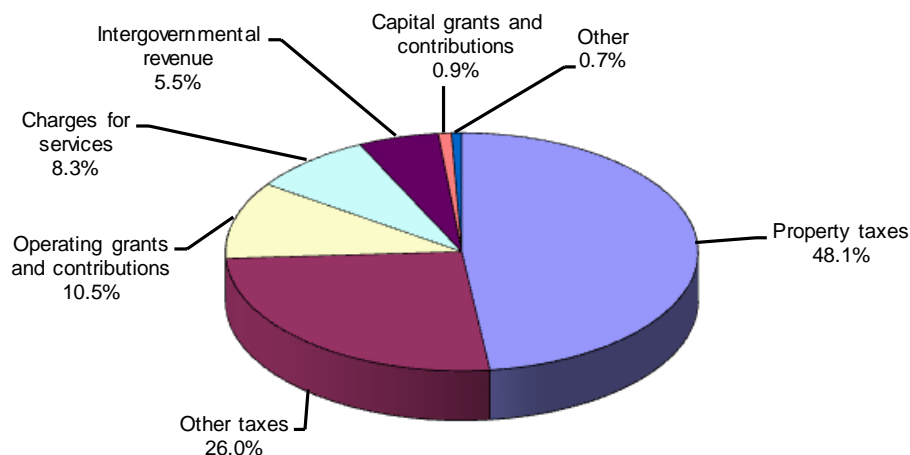
The following table presents a condensed summary of changes in net assets.

Summary of Changes in Net Assets (In Millions)								
	Governmental Activities		Business-type Activities		Total Primary Government		Component Unit	
	2012	2011	2012	2011	2012	2011	2012	2011
Revenues								
<i>Program Revenues:</i>								
Charges for services	\$ 5.6	\$ 5.1	\$49.7	\$47.5	\$ 55.3	\$ 52.6	\$ 1.6	\$ 1.6
Operating grants and contributions	7.1	7.1	-	-	7.1	7.1	7.8	7.2
Capital grants and contributions	0.6	1.5	-	-	0.6	1.5	-	-
<i>General Revenues:</i>								
Property taxes	32.5	32.1	-	-	32.5	32.1	-	-
Local sales and use tax	5.9	5.7	-	-	5.9	5.7	-	-
Business license tax	4.8	4.6	-	-	4.8	4.6	-	-
Meals tax	3.2	2.6	-	-	3.2	2.6	-	-
Utility taxes	1.1	1.1	-	-	1.1	1.1	-	-
Other taxes	2.6	2.8	-	-	2.6	2.8	-	-
Intergovernmental revenue	3.7	3.7	-	-	3.7	3.7	-	-
Investment earnings	0.1	0.1	-	-	0.1	0.1	-	-
Payments from City of Salem	-	-	-	-	-	-	18.5	18.4
State aid	-	-	-	-	-	-	13.2	12.8
Other	0.4	0.6	-	-	0.4	0.6	0.6	0.5
Total revenues	67.6	67.0	49.7	47.5	117.3	114.5	41.7	40.5
Expenses								
General government	\$ 6.5	\$ 6.2	\$ -	\$ -	\$ 6.5	\$ 6.2	\$ -	\$ -
Judicial administration	1.9	1.9	-	-	1.9	1.9	-	-
Public safety	16.5	15.8	-	-	16.5	15.8	-	-
Public works	14.4	13.9	-	-	14.4	13.9	-	-
Health and welfare	2.4	2.7	-	-	2.4	2.7	-	-
Education	18.5	18.4	-	-	18.5	18.4	43.1	41.2
Parks, recreation and cultural	5.3	5.5	-	-	5.3	5.5	-	-
Community development	2.1	1.8	-	-	2.1	1.8	-	-
Interest on long-term debt	1.1	1.2	-	-	1.1	1.2	-	-
Electric	-	-	36.0	35.1	36.0	35.1	-	-
Water and sewage	-	-	11.0	11.0	11.0	11.0	-	-
Civic center	-	-	2.5	2.3	2.5	2.3	-	-
Catering and concessions	-	-	0.9	0.9	0.9	0.9	-	-
Total expenses	68.7	67.4	50.4	49.3	119.1	116.7	43.1	41.2
Deficiency before transfers	(1.1)	(0.4)	(0.7)	(1.8)	(1.8)	(2.2)	(1.4)	(0.7)
Transfers	1.7	(3.3)	(1.7)	3.3	-	-	-	-
Increase (decrease) in net assets	0.6	(3.7)	(2.4)	1.5	(1.8)	(2.2)	(1.4)	(0.7)
Net assets, beginning	77.2	80.9	65.1	63.6	142.3	144.5	41.9	42.6
Net assets, ending	\$ 77.8	\$ 77.2	\$ 62.7	\$ 65.1	\$ 140.5	\$ 142.3	\$ 40.5	\$ 41.9

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

Governmental Activities – Revenues

The following graph presents revenues generated for governmental activities by category:



Property taxes, which were 48.1% of total governmental activities revenue, include real estate tax, the local portion of personal property tax, machinery and tools tax and public service corporation taxes. These revenues reflected growth of \$411,000 from prior year. New equipment purchases resulted in an \$288,000 or 11.1% increase in machinery and tools tax revenue. Real estate and personal property tax revenue showed moderate growth.

Sales and use tax and business and professional occupational license tax, which is based on gross receipts, increased \$184,000 or 3.2% and \$187,000 or 4.1%, respectively compared to the previous year. The meals tax rate was raised from 4% to 6% effective February 1, resulting in an additional \$690,652 in revenue. The additional 2% is committed to school capital needs. Other taxes which included bank stock tax, motor vehicle tax, recordation tax, admissions tax, lodging tax, cigarette tax and other miscellaneous tax decreased \$201,000 or 7.2%.

Charges for services, which were 8.3% of total governmental activities revenues, include fines, court fees, inspection fees, garbage collection fees, recreation fees and other program-based fees. These revenues increased \$445,000 from prior year. Fiscal year 2012 was the first year of the lease of the Police Department space by the federal government. Lease payments received from the federal government totaled \$123,000. Higher solid waste disposal fees were collected. Fees charged for ambulance transports under the revenue recovery program also increased.

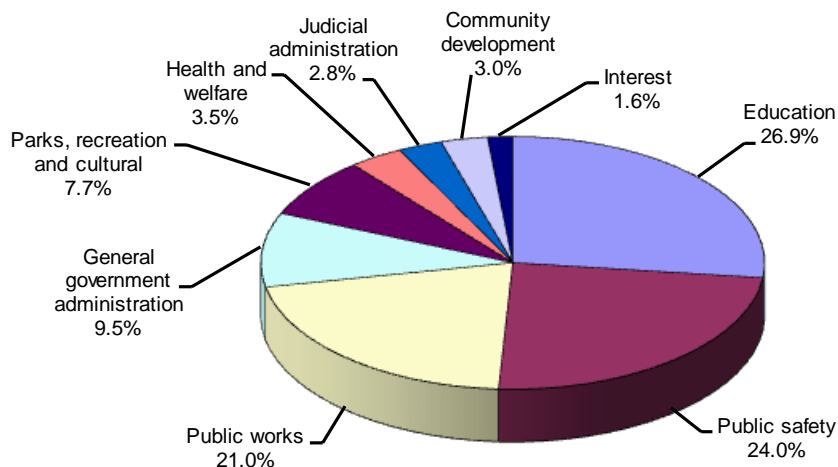
Operating grants and contributions, which were 10.5% of total governmental activities revenues, remained level with prior year. This category includes social service programs, street maintenance funds, reimbursement for constitutional officers, funding received under House Bill 599 for law enforcement and other grants and contributions. In the health and welfare function, revenue received under the Comprehensive Services Act for At Risk Youth and Families was lower due to fewer children requiring costly long term therapeutic care. Public safety operating grants declined \$127,000 which included cuts in funding received under house bill 599. In the public works function, highway maintenance funding from the state increased \$129,000 or 3.8% from the previous year, offsetting decreases in other areas.

Capital grants and contributions, which were 0.9% of total governmental activities revenue, include grants received from federal and state agencies to fund capital purchases. These revenues decreased \$922,000 from the previous year. The Colorado Street bridge project was completed in the previous fiscal year with final reimbursements received in fiscal year 2011. Federal funding of \$466,000 was received in fiscal year 2011 for interior finishing and office furnishings for the judge's chambers at the Police Department. In fiscal year 2012, \$300,000 was contributed by the School Division for the new ERP project. Grant funding received for the greenway projects remained level.

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

Governmental Activities – Expenses

Expenses of the governmental activities are shown below by functional area:



Education expenses totaling \$18.5 million or 26.9% of governmental activities, represents the largest allocation of resources. These expenses increased slightly from the prior year.

Public safety expenses, which were 24% of total governmental activities expenses, include operations of the labor-intensive police and fire departments, along with expense of emergency medical services, communications (E-911 call center) and the cost of juvenile justice programs. Public safety expenses were \$674,000 higher than prior year largely due to jail costs. Jail per diems and inmate populations rose from the prior year. Depreciation expense increased approximately \$89,000 as the new police department addition was completed in July 2011. Personnel costs of the Police and Fire departments were higher in fiscal year 2012.

Public works expenses were 21% of total governmental activities expenses and included engineering, solid waste management, building maintenance, street paving, traffic engineering and street maintenance. Expenses increased \$507,000 or 3.6% due to higher highway maintenance spending and waste disposal costs. Higher waste volume along with increased disposal rates resulted in increased costs.

General government expenses, which were 9.5% of total governmental activities expenses, include charges for administrative departments and increased \$473,000 or 7.8%. Fiscal year 2012 was the first year of operations for the employee health clinic and expenses of \$406,000 were incurred. Vehicle maintenance costs of the Fleet Management department were higher as vehicles and equipment are used longer before replacing. The purchase of software licenses also contributed to the increase.

Parks, recreation and cultural expenses were 7.7% of total governmental activities expenses and decreased \$211,000 from the prior year. Maintenance of city parks and greenways, library costs and expenses for citywide recreational and athletic programs and events were included in this category. In fiscal year 2011, certain amounts included in prior year construction in progress balances were expensed, increasing prior year costs.

Community development expenses were 3% of total governmental activities expense and increased \$242,000 or 13.2% due to higher economic development incentive payments partially offset by decreased spending of FEMA grant money. In fiscal year 2011, the City received FEMA funding to purchase homes located in the flood plain.

MANAGEMENT'S DISCUSSION AND ANALYSIS **(Continued)**

Business-type Activities

The proprietary funds provide the same type of information reported in the government-wide financial statements for business-type activities, but in more detail. Please refer to the MD&A's section on Financial Analysis of the City's Funds - Proprietary Funds for detailed analysis of the business-type activities major funds.

Component Unit – School Division Activities

General revenues of the School Division increased \$606,000 or 1.9%. State aid was higher in fiscal year 2012 due to one-time funding provided by the state for school operational support. Operating grants and contributions increased \$650,000 or 9.1%. In August 2010, Congress passed additional Jobs Bill stimulus legislation that provided one-time funding to be used by school divisions to rehire former employees, retain existing employees or hire new employees. Allocations must be spent by September 30, 2012. Amounts totaling \$800,000 were provided in fiscal year 2012, which offset the loss of other stimulus funding which had ended. The Salem City School Division was also one of only two school divisions in Virginia and seventy-six school systems nationwide to receive the Carol M. White PEP (Physical Education Program) grant. The primary focus of the multi-year grant is to implement a health and physical education curriculum that includes total body fitness, nutrition education, and healthy eating, while increasing student physical activities. In fiscal year 2012, \$192,000 was received.

The School Division incurred expenses of \$43.1 million for the year ended June 30, 2012 an increase of \$1.9 million or 4.6% from prior year. Salary costs were higher and two additional special education positions were added based on need. Fringe benefit costs increase due to the VRS pension contribution rate for the professional group increasing from 9.53% to 11.93%. Additional state funding was received that partially offset this increase. Health insurance and utility costs also contributed to higher expenditures in fiscal year 2012.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

Governmental Funds

As of June 30, 2012, the governmental funds had \$7 million in total fund balance, an increase of \$130,154 from prior year. Unassigned fund balances available to fund future expenditures were \$3.5 million or 49.3% of total fund balance. Unassigned fund balance, which includes all amounts not included in other classifications, is available to pay for future years' capital projects expenditures and provide for unforeseen circumstances. Restricted fund balance includes amounts that can be spent only for specific purposes stipulated by grantors and totaled \$1.3 million. Assigned fund balance totaled \$1.3 million and represents amounts set aside to cover health insurance costs and liquidate encumbrances. Committed fund balance totaled \$559,253 and includes \$39,436 for capital projects and \$519,817 dedicated to school capital improvements. City Council voted to increase the tax rate for meals from 4% to 6% effective February 2012 with the additional revenue dedicated to school capital needs.

General Fund

The general fund is the chief operating fund of the City. As of June 30, 2012, the general fund had \$7 million in total fund balance, which increased by \$205,160 from prior year. Unassigned fund balances available to fund future expenditures were \$3.5 million or 49.7% of total fund balance. As a measure of the general fund's liquidity, it may be useful to compare both total fund balance and unassigned fund balance to total fund expenditures. Total fund balance to total fund expenditures remained at 10.9%. Unassigned fund balance to total fund expenditures remains 5.4%.

City Council has stated its intent to increase the unassigned general fund balance to a level more reflective of the best practices recommended by the Government Financial Officers Association of the United States and Canada (GFOA). The slow recovery from the recession has adversely affected progress towards this goal. Unassigned fund balance to total fund revenues is 5.2%, short of City Council's goal. As the economy improves, the City should be better positioned to meet the objective.

MANAGEMENT'S DISCUSSION AND ANALYSIS

(Continued)

Property taxes, which were 49% of total general fund revenue, increased \$627,156 or 2% from the prior year. Real estate and personal property assessments reflect moderate increases. Investment in new equipment by businesses fueled a \$288,000 or 11.1% increase in machinery and tools tax.

Other local taxes, which comprised 26.4% of total general fund revenue, increased \$862,000 or 5.1% from the prior year. This category of revenue was reflective of local economic conditions with modest growth indicating recovery from the recession is underway. Sales tax revenue rose \$184,000 or 3.2% from the prior year. A 2% increase in the meals tax rate effective February 2012, contributed to an increase in meals tax of \$690,652 or 27.1%. As of June 30, 2012, \$519,817 is committed to school capital projects. Business license taxes, which are based on gross receipts, were up \$187,000 or 4.1%.

Intergovernmental revenue, which was 15.9% of total general fund revenue, decreased \$32,000 or 0.3% from the prior year. Highway maintenance funding was higher than the previous year but offset by decreased funding received under the Comprehensive Services Act. Grant funding in the public safety area remained level with the prior year.

Charges for services, which were 7% of total general fund revenue, increased \$237,000 or 5.3% from the prior year largely due to higher waste collection and disposal charges. Higher costs for waste disposal offset this increase. Fees charged for ambulance transports under the revenue recovery program increased approximately \$38,000. A \$1 ticket surcharge was implemented July 1, 2011 on certain tickets sold at the Salem Civic Center. Approximately \$24,000 was earned in ticket surcharge revenue in fiscal year 2012.

Education expenditures, which represents local operating support provided to the School Division, increased slightly from the prior year. Education expenses represented 28.9% of general fund expenditures.

Public safety expenditures, which comprised 24% of total general fund expenditures, increased by \$561,000 or 3.8% from the prior year due to higher jail costs. Per diems increased as did the number of prisoners. A new ambulance was purchased in fiscal year 2012, partially funded with a grant from the state.

Public works expenditures, which were 18.8% of total general fund expenditures, increased \$332,000 or 2.8% from the prior year. Highway maintenance costs increased approximately \$250,000. Waste disposal costs were also higher than the prior year.

General government expenditures increased \$892,000 or 18.2%. Fiscal year 2012 was the first year of operation of the employee health clinic which incurred expenditures of \$406,000. Software licenses to support to the ERP project were purchased at a cost of \$116,000. Due to aging vehicles and equipment, fleet maintenance costs increased \$75,000.

Health and welfare expenditures were 3.7% or \$290,000 lower than the previous year. Comprehensive Services Act expenditures were less as the City had fewer children requiring long-term therapeutic care, which is very expensive. In addition, certain costs such as child care are now paid directly by the State instead of through social services.

Non-departmental expenditures, which were 4.2% of total general fund expenditures, decreased \$249,000 or 8.6%. The City received funds through the Early Retiree Reinsurance Program, offsetting health insurance claims expense in fiscal year 2012.

Capital Projects Fund

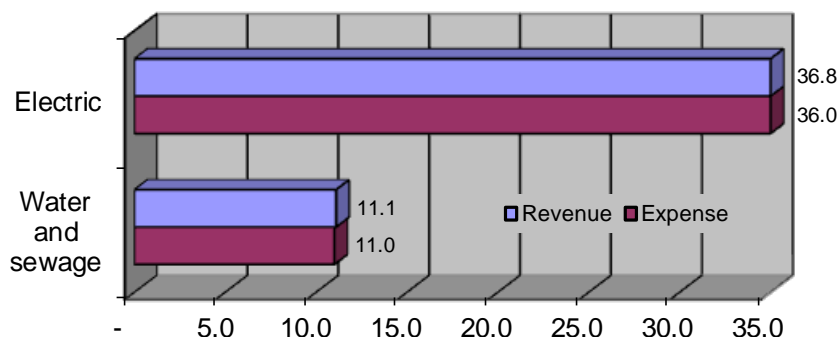
During fiscal year 2012, the capital projects fund total fund balance decreased by \$75,006. Expenditures of approximately \$1.2 million were incurred for the various ERP projects underway for the City and School Division. Legacy systems including financials, human resources, payroll and timekeeping are being replaced and the cashing and billing systems upgraded. Construction of Phase IIIA of the Roanoke

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

River Greenway began. Expenditures of \$206,000 were incurred. Funds from the American Recovery and Reinvestment Act have been awarded to the City to pay a portion of construction costs. The addition of the judge's chambers at the Police Department and the Police Department's new records management/computer aided dispatch/mobile system were completed in fiscal year 2012. Expenditures of \$43,000 and \$33,000, respectively, were incurred in fiscal year 2012 for these two projects.

Proprietary Funds

Revenues and expenses of the major enterprise funds are shown below:



Electric Fund

As of June 30, 2012, the electric fund had \$30.6 million in total net assets, which decreased by \$1.6 million from prior year. Net assets invested in capital assets, net of related debt were \$14.3 million or 46.7% of total net assets and decreased \$417,017 from prior year. Unrestricted net assets available to fund future expenses were \$16.3 million or 53.3% of total net assets and decreased by \$1.2 million from prior year.

For fiscal year 2012, operating revenue was \$36.8 million and increased \$1.1 million from the prior year primarily due to a rate increase instituted to cover rising purchased power costs. Operating expenses were \$35.2 million and were approximately \$900,000 greater than prior year due to higher power costs. Maintenance costs also increased \$219,000. Transfers to the general fund were \$2,150,000 and represent a payment in lieu of taxes of \$1.5 million and \$650,000 in funding assistance for capital purchases. \$252,000 was transferred to capital projects fund for the Electric fund's share of the ERP project.

Water and Sewage Fund

As of June 30, 2012, the water and sewage fund had \$26.2 million in total net assets, a decline of \$77,239 from prior year. Net assets invested in capital assets, net of related debt were \$23.9 million or 91.1% of total net assets and decreased \$1.1 million from prior year. Unrestricted net assets available to fund future expenses were \$2.3 million or 9% of total net assets and increased \$1.0 million from prior year.

For fiscal year 2012, operating revenue was \$11.1 million, an increase of \$1.1 million from the previous year. The City's water and sewer rates were restructured effective July 1, 2010 to include a monthly base service fee and also a volume charge based on metered water usage. A rate increase was then instituted on January 1, 2011 and January 1, 2012. Operating expenses were \$9.6 million and remained level with prior year. As part of the City's normal process of reviewing planned capital improvements, the City determined that certain projects would not proceed due to costs and other factors. As such, costs incurred for these projects totaling \$302,525 were expensed in fiscal year 2012. Treatment of sewage costs were approximately \$80,000 lower due to reduced rainfall and a lower rate charged for treatment. Net nonoperating expenses were \$1.3 million and decreased by \$78,216 from prior year primarily due to lower interest expense.

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

GENERAL FUND BUDGETARY HIGHLIGHTS

The City's budget is prepared in accordance with the *Code of Virginia*. Below is a condensed version of the budgetary comparison of the general fund original budget, amended budget and actual amounts.

Budgetary Highlights for 2012 (In Millions)

	Original Budget	Budget As Amended	Actual
Revenues	\$ 64.8	\$ 66.3	\$ 66.7
Expenditures	(62.9)	(65.0)	(63.8)
Transfers in	2.1	3.0	2.1
Transfers out	(4.5)	(5.3)	(4.8)
Use of fund balance	\$ (0.5)	\$ (1.0)	\$ 0.2

During the year, the City amended the original budget primarily for the following purposes:

- To re-appropriate monies for encumbrances established prior to June 30, 2011.
- To re-appropriate grants, donations and other revenues authorized in fiscal year 2011 or earlier, but not expended or encumbered as of June 30, 2011.
- To appropriate grants, donations and other revenues accepted or adjusted in fiscal year 2012 when official notice of approval was received.
- To appropriate the undesignated general fund balance to capital projects.
- To appropriate funds as authorized by City Council during the mid-year review process.

CAPITAL ASSETS

The City's total primary government capital assets, net of accumulated depreciation, decreased 2.2% from \$200.7 million to \$196.2 million. This investment includes land, construction in progress, machinery and equipment, buildings and improvements, public domain infrastructure, distribution and transmission, utility plant and sewage treatment contract. The following table presents a summary of capital asset balances at the end of the year. The changes in each category of capital assets, along with other important information regarding capital assets, are presented in Note 6 of the financial statements.

	Governmental Activities		Business-type Activities		Total Primary Government		Component Unit	
	2012	2011	2012	2011	2012	2011	2012	2011
Land	\$ 5.8	\$ 5.8	\$ 1.4	\$ 1.4	\$ 7.2	\$ 7.2	\$ 1.1	\$ 1.1
Construction in progress	1.4	2.9	1.4	7.3	2.8	10.2	1.4	0.2
Machinery and equipment	4.5	4.6	1.3	1.6	5.8	6.2	2.4	2.5
Buildings and improvements	26.8	25.7	21.2	17.7	48.0	43.4	32.9	34.1
Public domain infrastructure	59.0	60.7	-	-	59.0	60.7	-	-
Distribution and transmission	-	-	16.5	16.7	16.5	16.7	-	-
Utility plant	-	-	34.1	32.5	34.1	32.5	-	-
Sewage treatment contract	-	-	23.0	23.8	23.0	23.8	-	-
Total	\$ 97.5	\$ 99.7	\$ 98.9	\$ 101.0	\$ 196.4	\$ 200.7	\$ 37.8	\$ 37.9

MANAGEMENT'S DISCUSSION AND ANALYSIS **(Continued)**

Major capital asset additions in the *governmental activities* included:

- In fiscal year 2012, the City and School Division began the implementation process for three new software projects to replace legacy financials, human resources, payroll, timekeeping, cashiering and billing systems. Approximately \$1.2 million was spent on these projects.
- The Police Department addition, which houses a judge presiding on the U. S. Court of Appeals for the Fourth Circuit was substantially completed in July 2011 at a cost of \$1.8 million. This project was funded with bond proceeds of \$1.4 million. The federal government paid the City \$467,000 to cover the costs of finishing the interior of the addition and furnishing the new offices. Existing locker rooms were also expanded. General Services Administration has leased the office space from the City for a period of fifteen years with an optional five year renewal period.
- The Police Department's records management/computer aided dispatch/mobile system was replaced at a cost of \$431,822. Funding of \$150,000 was provided by the state with remaining funding provided from proceeds. The new system became operational in July 2011.
- Construction was begun on Phase IIIA of the Roanoke River Greenway with \$206,000 expended in fiscal year 2012. This phase will extend the trail 1.3 miles from Eddy Street to Mill Lane and is partially funded with monies received under the American Recovery and Reinvestment Act.
- A new ambulance was purchased at a cost of \$168,766. Funding from the state covered \$92,000 of the purchase.
- Traffic signal replacement and improvements totaled \$327,000 in fiscal year 2012.

Major capital asset additions in the *business-type activities* included:

- The Civic Center HVAC replacement project, which was funded from bond proceeds issued in the prior year, was completed at a cost of \$4.3 million. The old steam-based system was replaced with a hot water system that will be more energy efficient. Community room improvements included installation of a new ceiling, floors and lighting.
- The sewer rehabilitation project, which substantially upgraded older and problematic areas of the sewer system was completed at a cost of \$3.4 million. Bonds issued through Virginia Resources Authority funded the project.
- \$688,000 was spent on improvements to Electric distribution and transmission infrastructure.

LONG-TERM DEBT

At June 30, 2012, the City's long-term liabilities, excluding compensated absences, other postemployment benefit liabilities, bond premiums, bond discounts, deferred amounts on refunding, and bond issuance costs, totaled \$80.0 million. This amount was comprised of \$26.1 million related to governmental activities (including \$11.4 million for debt held on behalf of the School Division) and \$53.9 million related to business-type activities. The City made \$5.7 million in principal payments and amortized \$290,713 in bond issuance costs, discounts, premiums, and deferred amounts on refunding.

Total debt decreased \$3,771,872 during the fiscal year. The City issued \$9,485,000 in general obligation bonds on December 15, 2011 to advance refund \$8,800,000 of outstanding 2003A general obligation bonds. The City completed the advance refunding to reduce its total future debt service payments. Detailed information regarding these changes in long-term debt is disclosed in Note 8 to the financial statements.

With its most recent rating, the City maintained a rating of Aa3 from Moody's Investor Service.

The Charter of the City of Salem and the *Code of Virginia* limits the City's net debt to 10% of the assessed valuation of real estate within the City limits. This limit applies to governmental fund tax supported debt and certain long-term liabilities of proprietary funds. The City considers long-term debt of its electric, water and sewage funds to be self-supporting. The City's tax-supported debt of \$26.1 million is below the legal debt limit of \$201.5 million. Table 10 of the statistical section provides additional information related to the legal debt margin.

MANAGEMENT'S DISCUSSION AND ANALYSIS **(Continued)**

The School Division relies upon the City to provide full faith and credit for any debt obligations incurred. Therefore, the City reports School Division long-term liabilities, other than compensated absences and other postemployment benefits liabilities, as its own. In addition to bonded debt, the City's long-term obligations include compensated absences and other postemployment liabilities. Additional information concerning the City's long-term liabilities is presented in Note 8 of the financial statements and Table 9 of the statistical section.

Interest charges for fiscal year 2012 were \$1.1 million or 1.7% of total governmental activities expenses.

FACTORS INFLUENCING FUTURE BUDGETS

General fund revenues are not rebounding as fast after the most recent recession compared to previous recessions. State support for locally-administered programs has fallen, including declines in aid to schools, health and human services funding, funding received under house bill 599 and constitutional officer funding. Stagnant revenues and reduced state support put pressure on local government budgets and require tough choices. Our state continues to face uncertainty from actions taken at the federal level to reduce the budget deficit.

The City experienced limited revenue growth in fiscal year 2012. For fiscal year 2013, it is anticipated that moderate revenue growth will continue. Property taxes comprise approximately 51.3% of the general fund revenue budget and are expected to show slight increases from fiscal year 2012. Other local tax revenues are also expected to show a slow recovery. Limited hiring and reduced capital spending were employed in fiscal year 2012 to deal with budget constraints and will continue in fiscal year 2013. Funding for education comprises approximately 26.9% of the general fund expenditure budget. For the first time in several years, education funding will be increased by \$400,000 in fiscal year 2013. The increase in meals tax which was effective February 1, 2012 will provide additional funding for school capital needs.

The City is in the seventh year of a twenty-year contract to purchase electricity. The rate the City pays for wholesale electricity varies based on the supplier's actual costs, which are affected by fuel and environmental costs. In fiscal year 2012, the cost to purchase electricity increased approximately \$600,000 which is a lower increase than the previous year. To offset the rising costs of wholesale electricity, the City increased rates charged to customers by approximately 9% in fiscal year 2012 and anticipates a corresponding increase in wholesale electricity rates in fiscal year 2013.

Effective July 1, 2010, the City instituted a new rate structure and several new fees for water and sewer services. The monthly bills now include a monthly base service fee and also a volume charge based on metered water usage. Rate increases necessary to produce sufficient revenue to sustain long-term water and sewer systems will be phased incrementally over a four-year period, which began in 2010. A rate increase was effective January 1, 2011 and January 1, 2012 with an additional increase scheduled for January 1, 2013.

In fiscal year 2012, one-time funding from the federal Jobs Bill stimulus helped the School Division alleviate loss of American Recovery and Reinvestment Act funding. In addition, the state provided one-time supplemental support for school operating costs. Neither of these funding sources is available in fiscal year 2013. State aid is expected to be 4.5% higher in fiscal year 2013, but most of the increase is VRS pension and life insurance reimbursements to cover higher rates. In fiscal year 2013, two teaching positions and one instructional position have been eliminated through attrition. Cuts in instructional supplies, textbooks, travel, tuition assistance and personnel has been approved to balance the fiscal year 2013 budget.

In June 2012, the Governmental Accounting Standards Board approved GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, which revises and establishes new financial reporting requirements for governments that provide their employees with pension benefits. Beginning in fiscal

MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)

year 2015, governments providing defined benefit pensions will be required to recognize their long-term obligation for pension benefits and to comparably measure the annual costs of pension benefits for the first time. While the City will be affected by these new requirements, the biggest impact will be felt by the School Division. In recent years, the State has not adequately funded their share of the pension obligation for teachers. The unfunded actuarial accrued liability for the VRS Teacher's pool will be allocated to Schools, resulting in a liability on government-wide financial statements. Some pension reform efforts were passed by the 2012 General Assembly. The new GASB reporting standard is expected to increase volatility in VRS rates and result in higher unfunded liability calculation for all systems.

The City and Salem School Division participate together in a common plan to provide healthcare to employees. This plan is self-insured and to the extent that savings can be created, costs borne by the employer and employees are reduced. After a comprehensive review of benefits and costs, a contract was entered into with HealthStat, Inc. to operate a health clinic available to employees and dependents. The clinic is intended to maximize benefits and lower costs through educating employees and helping them avoid using costly medical facilities. This is a two year pilot program after which an analysis of the effectiveness of the program will determine the impact and continuance of the program. The clinic began operations in July 2011.

REQUESTS FOR INFORMATION

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of the City's finances and to demonstrate the City's accountability for the resources it receives. If you have any questions about this report or need additional information, contact the Director of Finance, City of Salem, 114 North Broad Street, Salem, Virginia 24153, (540) 375-3061, or visit the City's website at www.salemva.gov.

Additional information on the Component Unit can be obtained from the Supervisor of Business, Salem Public Schools, 510 South College Avenue, Salem, Virginia 24153.

BASIC FINANCIAL STATEMENTS



The basic financial statements subsection of the City of Salem, Virginia's Comprehensive Annual Financial Report includes the governmental-wide statement of net assets and statement of activities. Government-wide statements incorporate governmental and business-type activities of the City of Salem and activities of the component unit to provide an overview of the financial position and change in net assets for the reporting entity. Also, this section includes the fund financial statements for governmental, proprietary, and fiduciary funds and the accompanying notes to the financial statements.

CITY OF SALEM, VIRGINIA
STATEMENT OF NET ASSETS
JUNE 30, 2012

	Primary Government			Component Unit
	Governmental Activities	Business-type Activities	Total	
ASSETS				
Cash and cash equivalents	\$ 4,002,583	\$ 15,660,158	\$ 19,662,741	\$ 7,212,133
Receivables, net	3,334,746	5,925,765	9,260,511	4,180
Due from component unit	6,427	-	6,427	-
Due from other governmental units	4,317,199	-	4,317,199	977,576
Internal balances	(400,000)	400,000	-	-
Other postemployment benefits asset	-	-	-	73,243
Inventories	485,055	1,708,057	2,193,112	51,525
Prepaid items	12,151	78,568	90,719	24,138
<i>Restricted assets:</i>				
Cash and cash equivalents	173,407	-	173,407	-
<i>Capital assets:</i>				
Nondepreciable	7,213,336	2,763,291	9,976,627	2,524,142
Depreciable, net	90,280,902	96,098,576	186,379,478	35,312,247
Total assets	109,425,806	122,634,415	232,060,221	46,179,184
LIABILITIES				
Accounts payable and accrued liabilities	2,413,756	3,470,129	5,883,885	697,370
Accrued payroll and related liabilities	417,389	138,934	556,323	3,604,051
Accrued interest	263,802	855,671	1,119,473	-
Self insurance claims liability	272,735	70,691	343,426	376,305
Due to primary government	-	-	-	6,427
Unearned revenue	98,346	134,555	232,901	19,642
Customer security deposits	-	732,156	732,156	-
<i>Long-term liabilities</i>				
<i>due in less than one year:</i>				
Bonds payable	2,755,685	3,215,957	5,971,642	-
Compensated absences	1,827,937	477,344	2,305,281	377,410
<i>Long-term liabilities</i>				
<i>due in more than one year:</i>				
Bonds payable	22,715,041	50,461,943	73,176,984	-
Compensated absences	216,216	187,974	404,190	511,888
Other postemployment benefits	629,278	169,955	799,233	-
Total liabilities	31,610,185	59,915,309	91,525,494	5,593,093
NET ASSETS (DEFICIT)				
Invested in capital assets, net of related debt	87,145,604	44,265,414	131,411,018	37,836,389
Restricted for:				
Grant programs	362,761	-	362,761	-
Highway maintenance	882,225	-	882,225	-
Capital projects	15,244	-	15,244	-
Unrestricted	(10,590,213)	18,453,692	7,863,479	2,749,702
Total net assets	\$ 77,815,621	\$ 62,719,106	\$ 140,534,727	\$ 40,586,091

The Notes to Financial Statements are an integral part of this statement.

**CITY OF SALEM, VIRGINIA
STATEMENT OF ACTIVITIES
YEAR ENDED JUNE 30, 2012**

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Assets			
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Government			Component Unit
					Governmental Activities	Business-type Activities	Total	
Primary Government								
<i>Governmental activities:</i>								
General government	\$ 6,583,782	\$ 321,369	\$ 492,416	\$ 304,873	\$ (5,465,124)		\$ (5,465,124)	
Judicial administration	1,866,052	305,498	958,822	32,932	(568,800)		(568,800)	
Public safety	16,492,831	991,473	1,093,508	-	(14,407,850)		(14,407,850)	
Public works	14,421,981	3,560,239	3,618,615	17,279	(7,225,848)		(7,225,848)	
Health and welfare	2,430,955	-	808,044	-	(1,622,911)		(1,622,911)	
Education	18,471,653	-	-	-	(18,471,653)		(18,471,653)	
Parks, recreation and cultural	5,284,647	355,918	153,299	240,902	(4,534,528)		(4,534,528)	
Community development	2,076,325	22,906	-	-	(2,053,419)		(2,053,419)	
Interest on long-term debt	1,139,218	-	-	-	(1,139,218)		(1,139,218)	
Total governmental activities	<u>68,767,444</u>	<u>5,557,403</u>	<u>7,124,704</u>	<u>595,986</u>	<u>(55,489,351)</u>		<u>(55,489,351)</u>	
<i>Business-type activities:</i>								
Electric	36,047,453	36,824,320	-	-		\$ 776,867	776,867	
Water and sewage	10,952,702	11,114,241	-	13,222		174,761	174,761	
Civic Center	2,472,731	880,306	-	-		(1,592,425)	(1,592,425)	
Catering and concessions	903,039	856,919	-	-		(46,120)	(46,120)	
Total business-type activities	<u>50,375,925</u>	<u>49,675,786</u>	<u>-</u>	<u>13,222</u>		<u>(686,917)</u>	<u>(686,917)</u>	
Total primary government	<u>\$ 119,143,369</u>	<u>\$ 55,233,189</u>	<u>\$ 7,124,704</u>	<u>\$ 609,208</u>	<u>\$ (55,489,351)</u>	<u>\$ (686,917)</u>	<u>\$ (56,176,268)</u>	
Component Unit	<u>\$ 43,078,497</u>	<u>\$ 1,574,520</u>	<u>\$ 7,810,425</u>	<u>\$ -</u>				<u>\$ (33,693,552)</u>
<i>General revenues:</i>								
Property taxes					32,480,280	-	32,480,280	-
Local sales and use taxes					5,891,941	-	5,891,941	-
Business license tax					4,751,638	-	4,751,638	-
Meals tax					3,242,532	-	3,242,532	-
Utility taxes					1,124,383	-	1,124,383	-
Other taxes					2,604,603	-	2,604,603	-
Intergovernmental revenue not restricted					3,747,854	-	3,747,854	-
Unrestricted investment earnings					127,210	4,121	131,331	-
Payments from City of Salem					-	-	-	18,471,653
State aid					-	-	-	13,237,358
Other					411,355	-	411,355	638,972
Transfers					1,656,490	(1,656,490)	-	-
Total general revenues and transfers					<u>56,038,286</u>	<u>(1,652,369)</u>	<u>54,385,917</u>	<u>32,347,983</u>
Change in net assets					548,935	(2,339,286)	(1,790,351)	(1,345,569)
Net assets, beginning					<u>77,266,686</u>	<u>65,058,392</u>	<u>142,325,078</u>	<u>41,931,660</u>
Net assets, ending					<u>\$ 77,815,621</u>	<u>\$ 62,719,106</u>	<u>\$ 140,534,727</u>	<u>\$ 40,586,091</u>

The Notes to Financial Statements are an integral part of this statement.

**CITY OF SALEM, VIRGINIA
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2012**

	General	Debt Service	Capital Projects	Total Governmental Funds
ASSETS				
Cash and cash equivalents	\$ 4,002,583	\$ -	\$ -	\$ 4,002,583
Cash and cash equivalents, restricted	2,500	-	170,907	173,407
Receivables, net	3,334,746	-	-	3,334,746
Due from component unit	6,427	-	-	6,427
Due from other governmental units	4,201,193	-	116,006	4,317,199
Inventories	485,055	-	-	485,055
Prepaid items	12,151	-	-	12,151
Total assets	<u>\$ 12,044,655</u>	<u>\$ -</u>	<u>\$ 286,913</u>	<u>\$ 12,331,568</u>
LIABILITIES				
Accounts payable and accrued liabilities	\$ 2,181,523	\$ -	\$ 232,233	\$ 2,413,756
Accrued payroll and related liabilities	417,389	-	-	417,389
Self insurance claims liability	272,735	-	-	272,735
Due to other funds	400,000	-	-	400,000
Deferred revenue	1,785,175	-	-	1,785,175
Total liabilities	<u>5,056,822</u>	<u>-</u>	<u>232,233</u>	<u>5,289,055</u>
FUND BALANCES				
Nonspendable	497,206	-	-	497,206
Restricted	1,244,986	-	15,244	1,260,230
Committed	519,817	-	39,436	559,253
Assigned	1,256,103	-	-	1,256,103
Unassigned	3,469,721	-	-	3,469,721
Total fund balances	<u>6,987,833</u>	<u>-</u>	<u>54,680</u>	<u>7,042,513</u>
Total liabilities and fund balances	<u>\$ 12,044,655</u>	<u>\$ -</u>	<u>\$ 286,913</u>	<u>\$ 12,331,568</u>

The Notes to Financial Statements are an integral part of this statement.

CITY OF SALEM, VIRGINIA
RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET
TO THE STATEMENT OF NET ASSETS
JUNE 30, 2012

Total fund balance of governmental funds	\$ 7,042,513
Capital assets used in governmental activities are not considered current financial resources and, therefore, are not reported in the governmental funds.	97,494,238
Other long-term assets are not available to pay for current period expenditures and, therefore, are deferred in the governmental funds.	1,686,829
Long-term liabilities are not due and payable in the current period and, therefore, are not reported in the governmental funds:	
Bonds payable	(26,095,236)
Bond premiums	(229,471)
Bond discounts	56,110
Deferred amounts on refunding	532,233
Bond issuance costs	265,638
Accrued interest	(263,802)
Compensated absences	(2,044,153)
Other postemployment benefits	(629,278)
Net assets of governmental activities	<u>\$ 77,815,621</u>

The Notes to Financial Statements are an integral part of this statement.

CITY OF SALEM, VIRGINIA
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
YEAR ENDED JUNE 30, 2012

	General	Debt Service	Capital Projects	Total Governmental Funds
REVENUES				
Property taxes	\$ 32,669,246	\$ -	\$ -	\$ 32,669,246
Other local taxes	17,615,097	-	-	17,615,097
Permits, fees and licenses	202,342	-	-	202,342
Fines and forfeitures	160,816	-	-	160,816
Revenue from use of money and property	641,805	-	262	642,067
Charges for services	4,700,364	-	-	4,700,364
Other	103,964	-	737	104,701
Intergovernmental	10,621,391	250,000	591,113	11,462,504
Total revenues	<u>66,715,025</u>	<u>250,000</u>	<u>592,112</u>	<u>67,557,137</u>
EXPENDITURES				
<i>Current:</i>				
General government	5,792,852	-	-	5,792,852
Judicial administration	1,801,429	-	-	1,801,429
Public safety	15,353,250	-	-	15,353,250
Public works	11,988,380	-	-	11,988,380
Health and welfare	2,391,628	-	-	2,391,628
Education	18,471,653	-	-	18,471,653
Parks, recreation and cultural	4,403,170	-	-	4,403,170
Community development	981,483	-	-	981,483
Non-departmental	2,658,955	-	-	2,658,955
Capital projects	-	-	1,571,118	1,571,118
<i>Debt service:</i>				
Principal retirement	-	2,623,661	-	2,623,661
Interest	-	970,434	-	970,434
Bond issuance costs	-	31,900	-	31,900
Total expenditures	<u>63,842,800</u>	<u>3,625,995</u>	<u>1,571,118</u>	<u>69,039,913</u>
Excess (deficiency) of revenues over expenditures	<u>2,872,225</u>	<u>(3,375,995)</u>	<u>(979,006)</u>	<u>(1,482,776)</u>
OTHER FINANCING SOURCES (USES)				
Proceeds from sale of refunding bonds	-	9,485,000	-	9,485,000
Payment to refunded bond escrow agent	-	(9,513,728)	-	(9,513,728)
Transfers in	2,150,000	3,404,723	904,000	6,458,723
Transfers out	(4,817,065)	-	-	(4,817,065)
Total other financing sources (uses)	<u>(2,667,065)</u>	<u>3,375,995</u>	<u>904,000</u>	<u>1,612,930</u>
Net change in fund balances	<u>205,160</u>	<u>-</u>	<u>(75,006)</u>	<u>130,154</u>
Fund balances, beginning	<u>6,782,673</u>	<u>-</u>	<u>129,686</u>	<u>6,912,359</u>
Fund balances, ending	<u>\$ 6,987,833</u>	<u>\$ -</u>	<u>\$ 54,680</u>	<u>\$ 7,042,513</u>

The Notes to Financial Statements are an integral part of this statement.

CITY OF SALEM, VIRGINIA
RECONCILIATION OF THE GOVERNMENTAL FUNDS STATEMENT OF REVENUES,
EXPENDITURES AND CHANGES IN FUND BALANCES TO THE STATEMENT OF ACTIVITIES
YEAR ENDED JUNE 30, 2012

Net changes in fund balances of governmental funds \$ 130,154

Governmental funds report capital outlays as expenditures while governmental activities report depreciation expense to allocate the cost of those assets over the life of the assets.

Capital outlay	2,155,518
Capital donated	4,873
Depreciation expense	(4,347,869)
Net capital transfer from proprietary fund	14,832

Governmental funds report proceeds from the sale of a capital asset as an increase in financial resources while governmental activities report the gain or loss on the sale of capital asset.

Proceeds from sale of assets	(6,935)
Loss from sale of assets	(29,979)

Revenues in the Statement of Activities that do not provide current financial resources are not reported as fund revenues. 98,099

Issuance of debt provides current financial resources to governmental funds, but increases long-term liabilities in the Statement of Net Assets.

Repayment of bond principal is an expenditure in the governmental funds, but repayment reduces long-term liabilities in the Statement of Net Assets.

Bond Proceeds, net of payment to refunded bond escrow agent	28,728
Principal payments	2,623,661
Amortization of current year bond premiums	18,530
Amortization of current year bond discounts	(1,779)
Amortization of current year deferred amounts on refunding	(181,495)
Bond issuance costs	31,900
Amortization of current year bond issuance costs	(76,367)

Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.

Change in accrued interest payable	83,814
Change in compensated absences	(139,887)
Change in other postemployment benefits	143,137

Changes in net assets of governmental activities	\$ 548,935
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The Notes to Financial Statements are an integral part of this statement.

CITY OF SALEM, VIRGINIA
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
BUDGET AND ACTUAL - GENERAL FUND
YEAR ENDED JUNE 30, 2012

	Budgeted Amounts		Actual Amounts	Variance with Final Budget Positive (Negative)
	Original	Final		
REVENUES				
Property taxes	\$ 32,751,500	\$ 32,851,500	\$ 32,669,246	\$ (182,254)
Other local taxes	16,891,000	16,991,000	17,615,097	624,097
Permits, fees and licenses	240,500	240,500	202,342	(38,158)
Fines and forfeitures	167,000	167,000	160,816	(6,184)
Revenue from use of money and property	591,425	591,425	641,805	50,380
Charges for services	4,706,600	4,708,250	4,700,364	(7,886)
Other	20,750	90,750	103,964	13,214
Intergovernmental	9,389,892	10,626,409	10,621,391	(5,018)
Total revenues	<u>64,758,667</u>	<u>66,266,834</u>	<u>66,715,025</u>	<u>448,191</u>
EXPENDITURES				
General government	5,189,502	5,830,272	5,792,852	37,420
Judicial administration	1,724,972	1,824,229	1,801,429	22,800
Public safety	14,655,246	15,411,082	15,353,250	57,832
Public works	11,742,581	12,318,015	11,988,380	329,635
Health and welfare	1,864,821	2,482,271	2,391,628	90,643
Education	18,420,000	18,471,653	18,471,653	-
Parks, recreation and cultural	4,175,214	4,437,039	4,403,170	33,869
Community development	829,965	984,448	981,483	2,965
Non-departmental	4,272,282	3,276,405	2,658,955	617,450
Total expenditures	<u>62,874,583</u>	<u>65,035,414</u>	<u>63,842,800</u>	<u>1,192,614</u>
Excess of revenues over expenditures	<u>1,884,084</u>	<u>1,231,420</u>	<u>2,872,225</u>	<u>1,640,805</u>
OTHER FINANCING SOURCES (USES)				
Transfers in	2,150,000	3,014,000	2,150,000	(864,000)
Transfers out	(4,484,084)	(5,281,088)	(4,817,065)	464,023
Total other financing uses	<u>(2,334,084)</u>	<u>(2,267,088)</u>	<u>(2,667,065)</u>	<u>(399,977)</u>
Net change in fund balances	<u>\$ (450,000)</u>	<u>\$ (1,035,668)</u>	<u>\$ 205,160</u>	<u>\$ 1,240,828</u>

The Notes to Financial Statements are an integral part of this statement.

CITY OF SALEM, VIRGINIA
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
JUNE 30, 2012

	Business-type Activities - Enterprise Funds			
	Electric	Water and Sewage	Nonmajor Proprietary Funds	Total Proprietary Funds
ASSETS				
<i>Current assets:</i>				
Cash and cash equivalents	\$ 14,342,363	\$ 1,253,708	\$ 64,087	\$ 15,660,158
Receivables, net	4,367,248	1,405,848	152,669	5,925,765
Due from other funds	400,000	-	65,000	465,000
Inventories	1,391,114	298,856	18,087	1,708,057
Prepaid items	-	1,212	77,356	78,568
Total current assets	20,500,725	2,959,624	377,199	23,837,548
<i>Capital assets:</i>				
Nondepreciable	1,243,813	1,342,825	176,653	2,763,291
Depreciable, net	32,080,462	58,128,437	5,889,677	96,098,576
Total capital assets	33,324,275	59,471,262	6,066,330	98,861,867
Total assets	53,825,000	62,430,886	6,443,529	122,699,415
LIABILITIES				
<i>Current liabilities:</i>				
Accounts payable and accrued liabilities	2,939,151	400,439	130,539	3,470,129
Accrued payroll and related liabilities	48,492	43,010	47,432	138,934
Accrued interest	211,703	643,968	-	855,671
Self insurance claims liability	18,569	36,413	15,709	70,691
Due to other funds	-	-	65,000	65,000
Unearned revenue	-	-	134,555	134,555
Customer security deposits	732,156	-	-	732,156
Bonds payable	659,507	2,556,450	-	3,215,957
Compensated absences	205,282	174,928	97,134	477,344
Total current liabilities	4,814,860	3,855,208	490,369	9,160,437
<i>Long-term liabilities:</i>				
Bonds payable	18,217,228	32,244,715	-	50,461,943
Compensated absences	108,990	12,275	66,709	187,974
Other postemployment benefits	45,045	83,364	41,546	169,955
Total long-term liabilities	18,371,263	32,340,354	108,255	50,819,872
Total liabilities	23,186,123	36,195,562	598,624	59,980,309
NET ASSETS (DEFICIT)				
Invested in capital assets, net of related debt	14,311,314	23,887,770	6,066,330	44,265,414
Unrestricted	16,327,563	2,347,554	(221,425)	18,453,692
Total net assets	\$ 30,638,877	\$ 26,235,324	\$ 5,844,905	\$ 62,719,106

The Notes to Financial Statements are an integral part of this statement.

CITY OF SALEM, VIRGINIA
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS
YEAR ENDED JUNE 30, 2012

	Business-type Activities - Enterprise Funds			
	Electric	Water and Sewage	Nonmajor Proprietary Funds	Total Proprietary Funds
OPERATING REVENUES				
Charges for services	\$ 36,545,302	\$ 10,842,539	\$ 1,674,951	\$ 49,062,792
Connections and transfers	10,879	79,210	-	90,089
Penalties	89,928	181,147	-	271,075
Pole rentals	162,211	-	-	162,211
Commissions	-	-	17,881	17,881
Other	16,000	11,345	44,393	71,738
Total operating revenues	<u>36,824,320</u>	<u>11,114,241</u>	<u>1,737,225</u>	<u>49,675,786</u>
OPERATING EXPENSES				
Salaries	-	1,621,679	1,376,050	2,997,729
Fringe benefits	-	689,036	466,160	1,155,196
Show expenses	-	-	119,555	119,555
Maintenance	-	980,434	199,495	1,179,929
Billing and collection	370,221	520,323	-	890,544
Professional services	29,573	47,227	24,335	101,135
Insurance	42,496	54,989	12,019	109,504
Purchased power	29,773,075	-	-	29,773,075
Distribution - operations	1,048,539	-	-	1,048,539
Distribution - maintenance	1,288,181	-	-	1,288,181
Administration	727,609	211,031	27,286	965,926
Travel and training	-	9,137	7,242	16,379
Materials and supplies	-	370,684	267,753	638,437
Expendable equipment and small tools	76,956	1,526	3,030	81,512
Utilities	-	351,858	263,260	615,118
Miscellaneous	148,329	6,913	8,276	163,518
Depreciation	1,640,517	2,915,233	381,850	4,937,600
Amortization	7,266	91,739	-	99,005
Treatment of sewage	-	1,744,511	-	1,744,511
Commissions	-	-	188,998	188,998
Total operating expenses	<u>35,152,762</u>	<u>9,616,320</u>	<u>3,345,309</u>	<u>48,114,391</u>
Operating income (loss)	<u>1,671,558</u>	<u>1,497,921</u>	<u>(1,608,084)</u>	<u>1,561,395</u>
NONOPERATING REVENUES (EXPENSES)				
Interest income	3,916	-	205	4,121
Interest expense	(861,275)	(1,314,931)	-	(2,176,206)
Realized loss on investment	(4,734)	-	-	(4,734)
Loss on sale of capital assets	(28,682)	(21,451)	(30,461)	(80,594)
Net nonoperating expenses	<u>(890,775)</u>	<u>(1,336,382)</u>	<u>(30,256)</u>	<u>(2,257,413)</u>
Income (loss) before contributions and transfers	<u>780,783</u>	<u>161,539</u>	<u>(1,638,340)</u>	<u>(696,018)</u>
Capital contributions in	-	13,222	-	13,222
Capital contributions out	(14,832)	-	-	(14,832)
Transfers in	-	-	1,012,342	1,012,342
Transfers out	<u>(2,402,000)</u>	<u>(252,000)</u>	<u>-</u>	<u>(2,654,000)</u>
Change in net assets	<u>(1,636,049)</u>	<u>(77,239)</u>	<u>(625,998)</u>	<u>(2,339,286)</u>
Net assets, beginning	<u>32,274,926</u>	<u>26,312,563</u>	<u>6,470,903</u>	<u>65,058,392</u>
Net assets, ending	<u>\$ 30,638,877</u>	<u>\$ 26,235,324</u>	<u>\$ 5,844,905</u>	<u>\$ 62,719,106</u>

The Notes to Financial Statements are an integral part of this statement.

**CITY OF SALEM, VIRGINIA
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
YEAR ENDED JUNE 30, 2012**

	Business-type Activities - Enterprise Funds			
	Electric	Water and Sewage	Nonmajor Proprietary Funds	Total Proprietary Funds
OPERATING ACTIVITIES				
Receipts from customers	\$ 36,742,076	\$ 10,969,717	\$ 1,715,018	\$ 49,426,811
Payments to suppliers	(34,823,937)	(4,250,308)	(1,143,415)	(40,217,660)
Payments to employees	(1,728,854)	(2,413,845)	(1,902,875)	(6,045,574)
Other receipts	16,000	11,345	62,274	89,619
Net cash provided by (used in) operating activities	205,285	4,316,909	(1,268,998)	3,253,196
NONCAPITAL FINANCING ACTIVITIES				
Interfund loan	(400,000)	-	-	(400,000)
Transfers in	-	-	1,012,342	1,012,342
Transfers out	(2,402,000)	(252,000)	-	(2,654,000)
Net cash provided by (used in) noncapital financing activities	(2,802,000)	(252,000)	1,012,342	(2,041,658)
CAPITAL AND RELATED FINANCING ACTIVITIES				
Proceeds from sale of capital assets	-	959	-	959
Purchases of capital assets	(666,380)	(1,309,641)	(2,901,624)	(4,877,645)
Proceeds from capital debt	-	1,264,788	-	1,264,788
Principal paid on capital debt	(632,588)	(2,465,410)	-	(3,097,998)
Interest paid on capital debt	(872,113)	(1,440,517)	-	(2,312,630)
Capital contributions	-	13,222	-	13,222
Net cash used in capital and related financing activities	(2,171,081)	(3,936,599)	(2,901,624)	(9,009,304)
INVESTING ACTIVITIES				
Proceeds from the sale of investments	202,620	-	-	202,620
Interest received	3,916	-	205	4,121
Net cash provided by investing activities	206,536	-	205	206,741
Net increase (decrease) in cash and cash equivalents	(4,561,260)	128,310	(3,158,075)	(7,591,025)
Cash and cash equivalents, beginning	18,903,623	1,125,398	3,222,162	23,251,183
Cash and cash equivalents, ending	\$ 14,342,363	\$ 1,253,708	\$ 64,087	\$ 15,660,158
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES				
Operating income (loss)	\$ 1,671,558	\$ 1,497,921	\$ (1,608,084)	\$ 1,561,395
<i>Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities</i>				
Depreciation and amortization	1,647,783	3,006,972	381,850	5,036,605
<i>Decrease (increase) in assets:</i>				
Receivables, net	(160,325)	(133,179)	35,308	(258,196)
Inventories	(54,540)	(50,609)	1,699	(103,450)
Prepaid items	-	(15)	14,598	14,583
<i>Increase (decrease) in liabilities:</i>				
Accounts payable and accrued liabilities	(2,950,634)	104,967	(36,194)	(2,881,861)
Accrued payroll and related liabilities	(59,638)	(76,253)	(67,729)	(203,620)
Self insurance claims liability	(4,266)	(6,018)	(2,269)	(12,553)
Unearned revenue	-	-	4,759	4,759
Customer security deposits payable	94,081	-	-	94,081
Compensated absences	32,930	1,201	13,114	47,245
Other postemployment benefits	(11,664)	(28,078)	(6,050)	(45,792)
Net cash provided by (used in) operating activities	\$ 205,285	\$ 4,316,909	\$ (1,268,998)	\$ 3,253,196
<i>Noncash investing, capital, and financing activities</i>				
Capital assets financed with accounts payable	\$ -	\$ 60,697	\$ -	\$ 60,697
Realized loss on investments	\$ (4,734)	\$ -	\$ -	\$ (4,734)

The Notes to Financial Statements are an integral part of this statement.

**CITY OF SALEM, VIRGINIA
STATEMENT OF FIDUCIARY NET ASSETS
FIDUCIARY FUNDS
JUNE 30, 2012**

	Agency Funds	OPEB Trust Fund
ASSETS		
Cash and cash equivalents	\$ 1,366,133	\$ -
Investments held by trustee, fair value for other pooled funds	-	2,806,443
Receivables, net	1,197	-
Due from Commonwealth of Virginia	71,616	-
Total assets	<u>1,438,946</u>	<u>2,806,443</u>
LIABILITIES		
Accounts payable	70,712	-
Liability to agency	1,368,234	-
Total liabilities	<u>1,438,946</u>	<u>-</u>
NET ASSETS		
Held in trust for other postemployment benefits	<u>\$ -</u>	<u>\$ 2,806,443</u>

**CITY OF SALEM, VIRGINIA
STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
FIDUCIARY FUNDS
YEAR ENDED JUNE 30, 2012**

	OPEB Trust Fund
ADDITIONS	
Employer contributions	\$ 452,323
<i>Investment Income</i>	
Decrease in fair value of investments	(27,623)
Less investment expenses	(3,214)
Total additions	<u>421,486</u>
Net increase in plan net assets	<u>421,486</u>
Net assets held in trust for other postemployment benefits, beginning	<u>2,384,957</u>
Net assets held in trust for other postemployment benefits, ending	<u><u>\$ 2,806,443</u></u>

The Notes to Financial Statements are an integral part of this statement.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

1. Summary of Significant Accounting Policies

The Financial Reporting Entity

The Town of Salem was established by act of the Virginia General Assembly in 1806. The City of Salem, Virginia (City) was established by act of the Virginia General Assembly in 1968. It is a political subdivision of the Commonwealth of Virginia, operating under the council-manager form of government. The City Council consists of a mayor and four other council members elected at large. The City is not part of a county and has taxing powers subject to statewide restrictions and tax limits. The City of Salem is the primary government of the reporting entity.

The City provides a full range of municipal services including police and fire, courts, sanitation, health and social services, public improvements, planning and zoning, general administration, education, parks and recreation, library, electric, civic center, water and sewage services.

Discretely Presented Component Unit

The City of Salem School Division (School Division) is a legally separate entity which operates four elementary schools, a middle school and a high school. School Board members are appointed by City Council. City Council also provides fiscal guidance because it levies taxes for the School Division's operations and issues debt for its capital projects. Based on these facts, the City reports the School Division as a discretely presented component unit. Separately issued financial statements may be obtained by contacting the City of Salem Schools, Supervisor of Business, 510 South College Avenue, Salem, Virginia 24153.

During the current year, the City provided \$18,471,653 of operating support to the School Division and made debt service payments of \$1,606,161 on behalf of the School Division.

Government-Wide Financial Statements

The government-wide financial statements report information on all nonfiduciary activities of the primary government and its component unit. *Governmental activities*, which are normally supported by taxes and intergovernmental revenues, are reported separately from *business-type activities*, which rely to a significant extent on fees and charges for support. Likewise, the *primary government* is reported separately from the legally separate *component unit* for which the primary government is financially accountable.

The **statement of net assets** presents both governmental and business-type activities on the accrual basis of accounting, which incorporates long-term assets and receivables, as well as long-term debt and obligations.

The **statement of activities** demonstrates the degree to which the direct expenses of a given function are offset by program revenues. *Direct expenses* are those that are clearly identifiable with a specific function. *Program revenues* include 1) charges to customers or applicants for goods, services or privileges provided, 2) operating grants and contributions and 3) capital grants and contributions, including special assessments that are clearly identifiable with a specific function. Taxes, internally dedicated resources and other items not reported among program revenues are reported instead as *general revenues*.

Fund Financial Statements

These statements are organized based on funds, each of which is considered a separate accounting entity. The emphasis is on major governmental and enterprise funds. The operation of each fund is accounted for by providing a separate set of self-balancing accounts that comprise its assets, liabilities, fund balances/net assets, revenues and expenditures/expenses, as appropriate.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

1. Summary of Significant Accounting Policies (Continued)

Fund Financial Statements (Continued)

Government resources are allocated to and accounted for in individual funds based upon the purposes for which they are to be spent and the means by which spending activities are controlled. The various funds are grouped in the basic financial statements into three broad fund categories as follows:

Governmental Funds account for expendable financial resources, other than proprietary fund types. The City reports the following major governmental funds:

- The *general fund* is the government's primary operating fund and accounts for all financial resources of the general government, except those required to be accounted for in another fund.
- The *debt service fund* accounts for the accumulation of resources and payments made for principal and interest on long-term general obligation debt not being financed by the proprietary funds.
- The *capital projects fund* accounts for resources to be used for the acquisition or construction of major capital facilities not being financed by the proprietary funds.

Proprietary Funds account for operations that are financed and operated in a manner similar to private business enterprises. The City reports the following major enterprise funds:

- The *electric fund* accounts for the activities of the electric distribution operations.
- The *water and sewage fund* accounts for the activities of the water and sewage operations.

Fiduciary Funds account for assets held by the City in a trustee capacity or as an agent for individuals, other governmental units or other funds. The City reports the following fiduciary funds:

- The *OPEB trust fund* accounts for the receipt and disbursement of assets held in trust for the other postemployment benefit (OPEB) plan of the City.
- The *agency funds* account for monies held in a custodial capacity on behalf of the Cardinal Criminal Justice Academy and Court-Community Corrections Program.

Measurement Focus and Basis of Accounting

Government-wide financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*. Revenues are recognized when earned and expenses are recognized when a liability is incurred, regardless of the timing of related cash flows.

Generally, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are charges between the government's proprietary funds and various other functions of the government. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

1. Summary of Significant Accounting Policies (Continued)

Measurement Focus and Basis of Accounting (Continued)

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized when they become susceptible to accrual; that is, when they become both measurable and available to finance expenditures of the current period. General fund tax revenues are considered measurable when they have been levied and available if collected within 60 days of year-end. Interest revenues are considered measurable and available if collected within 60 days of year-end. Grant revenues are considered measurable when the legal and contractual requirements have been met and available if collected within 90 days of year-end. All other revenue items are considered measurable and available when cash is received by the government. Expenditures are recorded when a liability is incurred, as under accrual accounting. However, debt service, compensated absences, other postemployment benefit expenditures, as well as expenditures related to claims and judgments are recorded only when payment is due.

As a result of the different measurement focus and basis of accounting used in preparing the government-wide statements versus the governmental fund financial statements, a reconciliation between the government-wide and fund financial statements is necessary. The reconciliations are presented following the governmental fund financial statements. As part of the reconciliation process, non-departmental indirect expenditures are allocated to functional expenses based on a percent of functional expenditures.

Proprietary fund financial statements are reported using the *economic financial resources measurement focus* and the *accrual basis of accounting*. These statements distinguish *operating* from *nonoperating* revenues and expenses. Operating revenues and expenses generally result from providing goods and services in connection with a proprietary fund's principal ongoing operations. Operating revenues include charges to customers for sales and services. Operating expenses 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 City's policy to use restricted resources first, then unrestricted resources, as they are needed.

Fiduciary fund financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*, with the exception of agency funds which have no measurement focus but employ the *accrual basis of accounting* for purposes of asset and liability recognition.

Private sector standards of accounting and financial reporting issued prior to December 1, 1989 are generally followed in both the government-wide and proprietary fund financial statements to the extent those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the *option* of following subsequent private sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The City has elected not to follow subsequent private sector guidance.

Budgets and Budgetary Accounting

The City's budget is presented and adopted in accordance with accounting principles generally accepted in the United States of America. The following procedures are used by the City in establishing the budgetary data reflected in the financial statements:

Annual Budget Adoption – Thirty days prior to the last council meeting in May, the City Manager submits to City Council a proposed operating and capital budget for the fiscal year commencing July 1. This budget includes proposed expenditures and the means of financing them. Public hearings are conducted to obtain citizen comments. Prior to June 30, the budgets are legally adopted through passage of an appropriation ordinance by City Council.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

1. Summary of Significant Accounting Policies (Continued)

Budgets and Budgetary Accounting (Continued)

Projects – The capital projects fund utilizes a project length budget, which is not legally enacted on an annual basis; therefore, a budgetary comparison statement is not presented.

Amendment – The City Manager is authorized to transfer amounts within and between departments and categories. In addition, City Council must approve budget amendments between funds and any budget amendments increasing or decreasing appropriations. During the year, City Council approved \$2,957,835 of additional appropriations primarily for grants, capital outlay, unforeseen operating expenditures and the reappropriation of fund balances for encumbrances.

Integration – Formal budgetary integration is employed as a management control device for the general fund. Formal budgetary integration is not employed for the debt service fund because effective budgetary control is alternatively achieved through budgeted transfers from the general fund to the debt service fund for debt payments.

Legal Compliance – Legal budgetary control is maintained at the fund level. Department Heads may use discretion to transfer from one category to another as long as the departmental total does not change. The City Manager may authorize a transfer of any unencumbered balance or portion thereof from one department to another within a fund. All other transfers require approval of City Council. Actual expenditures and operating transfers out may not legally exceed budget appropriations at the fund level. All appropriations lapse on June 30 except for the capital projects fund, which carry unexpended balances through a project's life.

Encumbrances

Encumbrance accounting, under which purchase orders, contracts and other commitments are recorded in order to reserve the applicable appropriation, is employed as an extension of formal budgetary integration in the general and capital project funds. Encumbrances outstanding at year-end are reported as part of the committed or assigned fund balances since they do not constitute expenditures or liabilities. These encumbrances are subject to reappropriation by City Council in the subsequent fiscal year. Significant encumbrances as of June 30, 2012 total \$316,811 in the general fund and \$1,008,042 in the capital projects fund.

Deposits and Investments

The City considers all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents. Investments are recorded at fair value.

Allowance for Uncollectible Accounts

The City calculates its allowance for uncollectible accounts using historical collection data and specific account analysis.

Property Taxes

The City levies *real estate taxes* on all real estate within its boundaries, except that exempted by statute, each year as of July 1 based on 100% of estimated fair market value of the property. The City reassesses all property annually. Real estate taxes are due in equal semiannual payments on December 5 and June 5 and are considered delinquent after each due date. Real estate taxes become a lien on real property the first day of the levy year. The tax rate for 2012 was \$1.18 per \$100 of assessed value.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

1. Summary of Significant Accounting Policies (Continued)

Property Taxes (Continued)

The City levies *personal property taxes* on motor vehicles and business and other tangible personal property each year as of January 1. Personal property taxes are due the following May 31 and are considered delinquent after the due date. Personal property taxes do not create a lien on property; however, City vehicle decals, which are required by law for all vehicles garaged in the City, may not be issued to any individual having outstanding personal property taxes. Personal property transactions during the year are taxed on a prorated basis. The tax rate for 2012 was \$3.20 per \$100 of assessed value.

Interfund Balances

Outstanding balances between funds are reported as due to/from other funds. Any residual balances outstanding between the governmental and business-type activities are reported in the government-wide statements as internal balances. Outstanding balances between the City and its component unit are reported as due to/from component unit or due to/from primary government.

Inventory

Governmental fund inventories consist of street and building materials and general supplies held for consumption. Inventories are valued at cost using the first-in, first-out (FIFO) method. The cost of materials and supplies are recorded as an expenditure at the time inventory is withdrawn for use.

Enterprise fund inventories consist primarily of spare parts held for consumption. Electric fund inventories are valued at cost using the average cost method. All other enterprise fund inventories are valued at cost using the FIFO method. The cost of spare parts is recorded as an expense at the time inventory is withdrawn for use.

Prepaid Items

Governmental fund prepaid items consist primarily of software maintenance fees incurred for consumption in a subsequent fiscal year. Prepaid items are amortized using the consumption method. The fees are recorded as an expenditure in the fiscal year related to the maintenance contract service period.

Enterprise fund prepaid items consist primarily of fees for civic and community events held after year-end. Prepaid items are amortized using the consumption method. The costs of these events are expensed in the subsequent fiscal year to obtain a proper matching of revenues and expenses.

Capital Assets

Capital assets, which include property, plant and equipment and infrastructure assets, are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets belonging to proprietary funds are reported in the applicable fund financial statements. Capital assets are defined by the government as assets with an initial individual cost in excess of \$0 for land, \$5,000 for machinery and equipment or \$10,000 for buildings, plant and infrastructure and an estimated useful life in excess of five years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value on the date of donation. The City includes the cost of certain intangible assets with a definite life in the appropriate asset class.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend the life of the asset are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are completed.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

1. Summary of Significant Accounting Policies (Continued)

Capital Assets (Continued)

Capital assets are depreciated using the straight-line method over the following estimated useful lives:

Machinery, furniture and equipment	5-25 years
Buildings and improvements	10-50 years
Distribution and transmission systems	35 years
Utility plant	35 years
Sewage treatment contract	40 years
Public domain infrastructure	25-50 years

The City capitalizes net interest costs on funds borrowed to finance the construction of proprietary capital assets. Capital asset additions included \$49,345 of net capitalized interest for the current year.

Surety Bond Payable

Deposits may be received in lieu of bond insurance or letter of credit for a performance bond. The amount is included in restricted cash and accounts payable and accrued liabilities since the funds will be returned upon successful completion of the performance bond.

Unearned and Deferred Revenue

In the statement of net assets, unearned revenue arises when assets are received before revenue recognition criteria is satisfied and primarily consists of retiree health insurance premiums billed in advance, advertising, event deposits, rentals and property taxes collected that are not yet due.

In the balance sheet, deferred revenue arises when assets are recognized but are not available to finance expenditures of the current fiscal period or when assets are received before revenue recognition criteria is satisfied. Deferred revenue primarily consists of property taxes and grants not collected within the availability period, retiree health insurance premiums billed in advance, advertising, event deposits, rentals and property taxes collected that are not yet due.

Long-Term Obligations

In the government-wide and proprietary fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund statement of net assets. Bonds payable are reported net of the applicable bond premiums, discounts, issuance costs, or deferred amounts on refunding. Bond premiums and discounts are deferred and amortized over the life of the bonds using the straight-line method. Issuance costs are reported as deferred charges and amortized over the term of the related debt. Deferred amounts on refunding are deferred and amortized as a component of interest expense over the remaining life of the old debt or the life of the new debt, whichever is shorter.

In the fund financial statements, governmental funds recognize bond premiums and discounts, as well as bond issuance costs, during the period incurred. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources, while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Local governments in Virginia have a tenancy in common with the School Board whenever the locality incurs a financial obligation, excluding capital leases, for school property which is payable over more than one fiscal year. The primary government reports this debt in its financial statements while the School Division reports the capital asset.

CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

1. Summary of Significant Accounting Policies (Continued)

Compensated Absences

The City and the School Division have policies to allow the accumulation and vesting of limited amounts of paid leave and extended illness leave until termination or retirement. Amounts of such absences are accrued when incurred in the government-wide, proprietary and fiduciary fund financial statements. A liability for these amounts is reported in governmental funds when the amounts are due for payment.

Other Postemployment Benefits

In connection with the City's funding of other postemployment benefits (OPEB), the City participates in the Virginia Pooled OPEB Trust (OPEB Trust Fund). The City's policy is to fully fund actuarially determined OPEB costs, which include both normal costs and amortization of unfunded accrued liability. The OPEB Trust Fund assets and investments are recorded at fair value. The Trust Board of Trustees establishes investment objectives, risk tolerance and asset allocation policies based on the investment policy, market and economic conditions and generally prevailing prudent investment practices.

Net Assets

Net assets invested in capital assets, net of related debt for governmental activities excludes \$11,178,959 of School Division debt and \$4,208,771 of Civic Center debt reported by the City because the related assets are reported by the School Division and Civic Center, respectively. Noncapital debt of \$335,818 is also excluded in the water and sewage fund.

Fund Balances

Fund balance is divided into five classifications based primarily on the extent to which the City is bound to observe constraints imposed upon the use of the resources in the governmental funds. The classifications are as follows:

- **Nonspendable** – Amounts that cannot be spent because they are not in spendable form, or legally or contractually required to be maintained intact. The “not in spendable form” criterion includes items that are not expected to be converted to cash. It also includes the long-term amount of interfund loans.
- **Restricted** – Amounts constrained to specific purposes by their providers (such as grantors, bondholders, and higher levels of government), through constitutional provisions, or by enabling legislation.
- **Committed** – Amounts constrained to specific purposes by the City, using its highest level of decision making authority; to be reported as committed, amounts cannot be used for any other purposes unless the same highest level of action is taken to remove or change the constraint.
- **Assigned** – Amounts the City intends to use for a specified purpose; intent can be expressed by the governing body or by City Council which has been designated this authority.
- **Unassigned** – Amounts that are available for any purpose; positive amounts are reported only in the general fund.

City Council establishes fund balance commitments by passage of an ordinance or resolution. This is typically done through adoption and amendment of the budget. Assigned fund balance is established by City Council through adoption or amendment of the budget as intended for a specific purpose (such as the purchase of capital assets, construction, debt service, or for other purposes).

Restricted Amounts

The City applies restricted resources first when expenditures are incurred for purposes for which either restricted or unrestricted (committed, assigned, and unassigned) amounts are available. Similarly, within unrestricted fund balance, committed amounts are reduced first followed by assigned, and then unassigned amounts when expenditures are incurred for purposes for which amounts in any of the unrestricted fund balance classifications could be used

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

1. Summary of Significant Accounting Policies (Continued)

Minimum Fund Balance

The General Fund reserve target is 15% of the Fund's current year budgeted appropriations. For the purpose of determining if the target has been met, the unassigned fund balance of the general fund is compared with the annual appropriations budget.

Other government funds of the City do not have specified fund balance targets. Recommended levels of committed and/or assigned fund balance will be determined on a case by case basis, based on the needs of each fund and as recommended by officials and approved by the City Council.

Estimates

Management uses estimates and assumptions in preparing its financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent liabilities, and reported revenues, expenditures and expenses. Actual results could differ from those estimates.

2. Deposits and Investments

The City maintains a concentration bank account used by all nonfiduciary funds, including the School Division. Each fund's portion of this account is presented in the basic financial statements as cash and cash equivalents.

All deposits and investments are reflected in the statements as follows:

	Primary Government	Component Unit
Cash and cash equivalents	\$ 19,662,741	\$ 7,212,133
Cash and cash equivalents, restricted	173,407	-
	<u>\$ 19,836,148</u>	<u>\$ 7,212,133</u>

Restricted cash and cash equivalents consist of a general fund surety bond payable and the capital projects fund cash balances.

Deposits

Deposits with banks are covered by the Federal Deposit Insurance Corporation (FDIC) and collateralized in accordance with the Virginia Security for Public Deposits Act (the "Act") Section 2.2-4400 et. seq. of the Code of Virginia. Under the Act, banks and savings institutions holding public deposits in excess of the amount insured by the FDIC must pledge collateral to the Commonwealth of Virginia Treasury Board. Financial institutions may choose between two collateralization methodologies and depending upon that choice, will pledge collateral that ranges in the amounts from 50% to 130% of excess deposits. Accordingly, all deposits are considered fully collateralized.

Investments

Statutes authorize local governments and other public bodies to invest in obligations of the United States or agencies thereof, obligations of the Commonwealth of Virginia or political subdivisions thereof, obligations of the International Bank for Reconstruction and Development (World Bank), the Asian Development Bank, the African Development Bank, prime quality commercial paper and certain corporate notes, banker's acceptances, repurchase agreements, the State Treasurer's Local Government Investment Pool (LGIP) and the State Treasurer's Non-Arbitrage Program (SNAP).

As of June 30, 2012, the City had no investments.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

2. Deposits and Investments (Continued)

Credit Risk

Although the City does not have a formal policy addressing credit risk, the City adheres to the State guidelines. As required by the *Code of Virginia*, obligations of the Commonwealth of Virginia and its political subdivisions must have a debt rating of at least AA by Standard & Poor's (S&P) or Aa by Moody's Investors Service (Moody's). Repurchase agreements are collateralized by Treasury or Agency obligations of which the market value is at least 102% of the purchase price of the agreement. Commercial paper must be issued by an entity incorporated in the U.S. and rated at least A-1 by S&P or P-1 by Moody's. Corporate notes and bonds have a rating of at least AA by S&P or Aa by Moody's. Money market mutual funds must trade on a constant net asset value and invest solely in securities otherwise eligible for investment under these guidelines.

Interest Rate Risk

Although the City does not have a formal policy addressing interest rate risk, the City manages its exposure to fair value losses arising from increasing interest rates by limiting the length of each investment to achieve a minimal portfolio weighted average maturity.

3. Receivables

Receivables are as follows:

	Governmental Activities	Business-type Activities			Component Unit
		Electric	Water and Sewage	Nonmajor Proprietary	
Tax receivables	\$ 2,628,966	\$ -	\$ -	\$ -	\$ -
Account receivables	-	4,525,338	1,467,302	165,498	-
Other receivables	1,670,187	-	-	-	4,180
Gross receivables	4,299,153	4,525,338	1,467,302	165,498	4,180
Allowance for uncollectibles	(964,407)	(158,090)	(61,454)	(12,829)	-
Receivables, net	<u>\$ 3,334,746</u>	<u>\$ 4,367,248</u>	<u>\$ 1,405,848</u>	<u>\$ 152,669</u>	<u>\$ 4,180</u>

4. Interfund Balances and Transfers

The composition of the interfund balances is as follows:

		Due from (fund)		
		General	Nonmajor enterprise	Total
Due to (fund)	Electric	\$ 400,000	\$ -	\$ 400,000
	Nonmajor enterprise	-	65,000	65,000
	Total	<u>\$ 400,000</u>	<u>\$ 65,000</u>	<u>\$ 465,000</u>

The amount due to the electric fund is a long-term loan to the general fund that will be subsequently paid over a five year period. The amount due to the nonmajor enterprise funds is a short-term loan made to another nonmajor enterprise fund to fund operations.

CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

4. Interfund Balances and Transfers (Continued)

The composition of the interfund transfers is as follows:

	Transfer out (fund)				
	General	Electric	Water and sewage	Nonmajor enterprise	Total
Transfer in (fund)					
General	\$ -	\$ 2,150,000	\$ -	\$ -	\$ 2,150,000
Debt service	3,404,723	-	-	-	3,404,723
Capital projects	400,000	252,000	252,000	-	904,000
Nonmajor enterprise	1,012,342	-	-	1,137	1,013,479
Total	<u>\$ 4,817,065</u>	<u>\$ 2,402,000</u>	<u>\$ 252,000</u>	<u>\$ 1,137</u>	<u>\$ 7,472,202</u>

Transfers to the general fund include a payment in lieu of taxes and funding assistance for operating expenses. Transfers to the debt service fund include principal and interest payments for general government and school debt. Transfers to capital projects include funding for current projects. Transfers to nonmajor enterprise funds include funding assistance for operating expenses.

5. Due from Other Governmental Units

Amounts due from other governmental units are as follows:

	Governmental Activities	Component Unit
Commonwealth of Virginia		
Personal property tax	\$ 2,588,707	\$ -
State sales tax	-	547,574
Local sales tax	994,923	-
Comprehensive Services Act	183,007	-
Communications tax	186,272	-
Constitutional officers reimbursement	89,891	-
Victim Witness program	26,531	-
Rental tax	36,992	-
911 State grant	11,426	-
Colorado Street Bridge project funding	6,500	-
Mason Creek Greenway project funding	10,058	-
Roanoke River Greenway project funding	82,170	-
Transportation Enhancement project funding	17,279	-
Other	48,481	-
Federal government		
School funds	-	430,002
Byrne One-Time Equipment Sheriff's grant	24,300	-
Reimbursement from GSA	10,662	-
	<u>\$ 4,317,199</u>	<u>\$ 977,576</u>

CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

6. Capital Assets

Capital asset activity for the year is as follows:

Governmental Activities	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, nondepreciable				
Land	\$ 5,832,641	\$ -	\$ -	\$ 5,832,641
Construction in progress	2,919,832	1,159,088	(2,698,225)	1,380,695
Capital assets, nondepreciable	8,752,473	1,159,088	(2,698,225)	7,213,336
Capital assets, depreciable				
Machinery and equipment	18,066,333	946,105	(123,835)	18,888,603
Buildings and improvements	38,355,589	2,071,818	(13,465)	40,413,942
Public domain infrastructure	94,644,743	716,974	(51,135)	95,310,582
Capital assets, depreciable	151,066,665	3,734,897	(188,435)	154,613,127
Accumulated depreciation				
Machinery and equipment	(13,453,514)	(1,076,337)	117,399	(14,412,452)
Buildings and improvements	(12,656,103)	(959,496)	5,818	(13,609,781)
Public domain infrastructure	(34,005,723)	(2,332,573)	28,304	(36,309,992)
Accumulated depreciation	(60,115,340)	(4,368,406)	151,521	(64,332,225)
Capital assets, depreciable, net	90,951,325	(633,509)	(36,914)	90,280,902
Capital assets, net	\$ 99,703,798	\$ 525,579	\$ (2,735,139)	\$ 97,494,238
Business-type Activities	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, nondepreciable				
Land	\$ 1,377,952	\$ -	\$ -	\$ 1,377,952
Construction in progress	7,288,528	67,978	(5,971,167)	1,385,339
Capital assets, nondepreciable	8,666,480	67,978	(5,971,167)	2,763,291
Capital assets, depreciable				
Machinery and equipment	6,691,704	92,239	(45,750)	6,738,193
Buildings and improvements	22,912,556	4,315,807	(180,240)	27,048,123
Distribution and transmission	34,012,123	688,399	(292,219)	34,408,303
Utility plant	73,403,330	3,686,941	(233,433)	76,856,838
Sewage treatment contract	28,843,397	-	-	28,843,397
Capital assets, depreciable	165,863,110	8,783,386	(751,642)	173,894,854
Accumulated depreciation				
Machinery and equipment	(5,054,663)	(398,520)	45,752	(5,407,431)
Buildings and improvements	(5,216,956)	(785,669)	149,780	(5,852,845)
Distribution and transmission	(17,242,049)	(945,166)	263,537	(17,923,678)
Utility plant	(40,944,191)	(2,041,391)	211,023	(42,774,559)
Sewage treatment contract	(5,070,911)	(766,854)	-	(5,837,765)
Accumulated depreciation	(73,528,770)	(4,937,600)	670,092	(77,796,278)
Capital assets, depreciable, net	92,334,340	3,845,786	(81,550)	96,098,576
Capital assets, net	\$101,000,820	\$ 3,913,764	\$ (6,052,717)	\$ 98,861,867

CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

6. Capital Assets (Continued)

Depreciation expense is charged to functions/programs of the primary government as follows:

Governmental Activities		Business-type Activities	
General government	\$ 270,309	Electric	\$ 1,640,517
Judicial administration	38,797	Water and sewage	2,915,233
Public safety	711,102	Civic Center	375,569
Public works	2,620,147	Catering	6,281
Parks, recreation and cultural	705,922	Total depreciation expense	<u>\$ 4,937,600</u>
Community development	1,592		
Total depreciation expense	<u>\$ 4,347,869</u>		

Accumulated depreciation shown in the capital asset table for governmental activities exceeds depreciation expense by \$20,537 because the table includes accumulated depreciation for machinery & equipment transferred from the electric department.

Component Unit	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, nondepreciable				
Land	\$ 1,123,637	\$ -	\$ -	\$ 1,123,637
Construction in progress	210,368	1,516,461	(326,324)	1,400,505
Capital assets, nondepreciable	<u>1,334,005</u>	<u>1,516,461</u>	<u>(326,324)</u>	<u>2,524,142</u>
Capital assets, depreciable				
Furniture and equipment	5,949,701	389,597	(218,162)	6,121,136
Buildings and improvements	<u>53,489,020</u>	<u>250,491</u>	<u>(124,194)</u>	<u>53,615,317</u>
Capital assets, depreciable	<u>59,438,721</u>	<u>640,088</u>	<u>(342,356)</u>	<u>59,736,453</u>
Accumulated depreciation				
Furniture and equipment	(3,443,520)	(433,829)	200,408	(3,676,941)
Buildings and improvements	<u>(19,443,550)</u>	<u>(1,349,324)</u>	<u>45,609</u>	<u>(20,747,265)</u>
Accumulated depreciation	<u>(22,887,070)</u>	<u>(1,783,153)</u>	<u>246,017</u>	<u>(24,424,206)</u>
Capital assets, depreciable, net	<u>36,551,651</u>	<u>(1,143,065)</u>	<u>(96,339)</u>	<u>35,312,247</u>
Capital assets, net	<u>\$ 37,885,656</u>	<u>\$ 373,396</u>	<u>\$ (422,663)</u>	<u>\$ 37,836,389</u>

7. Unearned and Deferred Revenue

Unearned revenue reported in the statement of net assets is as follows:

	Governmental Activities	Business-type Activities	Component Unit
Charges for services and fees	\$ 60,564	\$ 134,555	\$ 19,642
Taxes paid for subsequent year	37,782	-	-
Unearned revenue	<u>\$ 98,346</u>	<u>\$ 134,555</u>	<u>\$ 19,642</u>

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

7. Unearned and Deferred Revenue (Continued)

Deferred revenue reported in the governmental funds is as follows:

	Unavailable	Unearned	Total
Property taxes	\$ 1,619,042	\$ -	\$ 1,619,042
Charges for services and fees	67,787	60,564	128,351
Taxes paid for subsequent year	-	37,782	37,782
Deferred revenue	<u>\$ 1,686,829</u>	<u>\$ 98,346</u>	<u>\$ 1,785,175</u>

8. Long-Term Liabilities

The government issues general obligation bonds to provide funds for the acquisition and construction of major capital facilities. General obligation bonds have been issued for both governmental and business-type activities. These bonds are direct obligations and pledge the full faith and credit of the government and are subject to the provisions of the Internal Revenue Code of 1986 related to arbitrage, interest and income tax regulations under those provisions.

Prior Year Defeasances of Debt

In prior years, the City defeased certain general obligation bonds by placing the proceeds in irrevocable trusts to provide for all future debt service on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the City's financial statements. As of June 30, 2012, \$12,800,000 of bonds are considered defeased.

Current Year Debt Issuance and Defeasances of Debt

On December 15, 2011, the City issued \$9,485,000 in series 2011 general obligation bonds with an average interest rate of 2.14% to advance refund \$8,800,000 of outstanding 2003A series general obligations bonds with an average interest rate of 4.3%. The net proceeds of \$9,451,257 (after payment of \$33,743 in issuance costs) plus an additional \$62,471 from prior issue debt service funds were used to purchase government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for future debt service payments on the 2003A series general obligation bonds. As a result, \$8,800,000 of the 2003A series general obligations bonds are considered to be defeased and the liability for those bonds has been removed from the government-wide statement of net assets.

The advance refunding resulted in a difference between the reacquisition price and the net carrying value of the old debt of \$713,728. This difference, reported in the accompanying financial statements as a deduction from bonds payable, is being amortized over the remaining life of the old bonds as a component of interest expense through the year 2014. The City completed the advance refunding to reduce its total debt service payments by \$871,218 and to obtain an economic gain (difference between the present values of the old and new debt service payments) of \$825,340.

CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

8. Long-Term Liabilities (Continued)

The following is a summary of changes in long-term liabilities:

	Beginning Balance	Increases	Decreases	Ending Balance	Due Within One Year
Governmental Activities					
General obligation bonds	\$28,033,897	\$ 9,485,000	\$(11,423,661)	\$26,095,236	\$2,755,685
Bond premiums	248,001	-	(18,530)	229,471	-
Bond discounts	(57,889)	-	1,779	(56,110)	-
Deferred amounts on refunding	-	(713,728)	181,495	(532,233)	-
Bond issuance costs	(310,105)	(31,900)	76,367	(265,638)	-
Bonds payable	27,913,904	8,739,372	(11,182,550)	25,470,726	2,755,685
Compensated absences	1,904,266	1,967,824	(1,827,937)	2,044,153	1,827,937
Other postemployment benefits	772,415	1,375,308	(1,518,445)	629,278	-
	<u>\$30,590,585</u>	<u>\$12,082,504</u>	<u>\$(14,528,932)</u>	<u>\$28,144,157</u>	<u>\$4,583,622</u>
Business-type Activities					
General obligation bonds	\$55,710,739	\$ 1,264,788	\$(3,097,998)	\$53,877,529	\$3,215,957
Bond premiums	1,117,593	-	(62,851)	1,054,742	-
Bond issuance costs	(1,366,824)	-	112,453	(1,254,371)	-
Bonds payable	55,461,508	1,264,788	(3,048,396)	53,677,900	3,215,957
Compensated absences	618,073	524,589	(477,344)	665,318	477,344
Other postemployment benefits	215,747	439,969	(485,761)	169,955	-
	<u>\$56,295,328</u>	<u>\$ 2,229,346</u>	<u>\$ (4,011,501)</u>	<u>\$54,513,173</u>	<u>\$3,693,301</u>
Component Unit					
Compensated absences	\$ 872,000	\$ 186,198	\$(168,900)	\$ 889,298	\$ 377,410
Other postemployment benefits	-	284,897	(358,140)	(73,243)	-
	<u>\$ 872,000</u>	<u>\$ 471,095</u>	<u>\$ (527,040)</u>	<u>\$ 816,055</u>	<u>\$ 377,410</u>

The general fund has been used to liquidate the liabilities for all long-term debt excluding bond and other debt payments in prior years.

CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

8. Long-Term Liabilities (Continued)

Details of long-term indebtedness are as follows:

	Interest Rates	Issue Date	Maturity Date	Issue Amount	Governmental Activities	Business-type Activities
General Obligation Bonds						
2003 Public Improvement	2.00-4.50%	10/03	10/15	22,000,000	4,400,000	-
2004 Refunding	1.50-3.50%	03/04	04/16	9,640,000	1,490,695	1,874,305
2004 Public Improvement	3.00%	04/04	07/26	11,052,222	-	8,798,272
2006 Public Improvement	4.00-5.00%	05/06	04/31	25,000,000	2,166,701	18,928,299
2007 Refunding	4.00-5.00%	02/07	01/27	17,045,000	-	16,750,000
2010 Taxable Build America	4.57-6.56%	12/10	02/31	2,700,000	2,700,000	-
2010 Taxable	1.55-3.17%	12/10	02/16	1,010,000	790,000	-
2010 Public Improvement	3.00-4.25%	12/10	02/28	2,830,000	2,830,000	-
2010 Public Improvement	3.15%	09/10	03/30	3,648,124	-	3,559,493
2010 Refunding	2.50-5.25%	12/10	02/19	7,410,000	1,652,840	3,967,160
2010 Refunding	2.50-3.00%	12/10	02/13	1,160,000	580,000	-
2011 Refunding	2.14%	12/11	10/23	9,485,000	9,485,000	-
					26,095,236	53,877,529
				Bond premiums	229,471	1,054,742
				Bond discounts	(56,110)	-
				Deferred Amount on Refunding	(532,233)	-
				Bond issuance costs	(265,638)	(1,254,371)
					<u>\$ 25,470,726</u>	<u>\$ 53,677,900</u>

The annual requirements to amortize long-term debt and related interest are as follows:

Fiscal Year	Governmental Activities		Business-type Activities	
	Bonds payable		Bonds payable	
	Principal	Interest	Principal	Interest
2013	\$ 2,755,685	\$ 822,349	\$ 3,215,957	\$ 2,225,287
2014	2,170,264	730,060	3,270,581	2,112,667
2015	2,176,488	648,504	3,339,875	1,987,970
2016	2,092,623	566,433	3,309,899	1,845,022
2017	1,800,666	497,030	3,038,673	1,708,636
2018-2022	8,206,699	1,775,869	15,124,400	6,671,818
2023-2027	4,548,081	857,894	16,488,198	3,367,923
2028-2031	2,344,730	259,742	6,089,946	663,595
	<u>\$26,095,236</u>	<u>\$6,157,881</u>	<u>\$53,877,529</u>	<u>\$20,582,918</u>

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

9. Fund Balance

Fund balance is classified as nonspendable, restricted, committed, assigned and/or unassigned based primarily on the extent to which the City is bound to observe constraints imposed upon the use of the resources in the governmental funds. The constraints placed on fund balance for the governmental funds are presented below:

	General Fund	Debt Service Fund	Capital Projects Fund
Fund Balances:			
Nonspendable:			
Inventories	\$ 485,055	\$ -	\$ -
Prepaid items	12,151	-	-
Restricted for:			
Judicial administration	3,619	-	-
Public safety	359,142	-	-
Public works	882,225	-	-
Parks & recreation	-	-	15,244
Committed to:			
General government administration	-	-	39,436
Education	519,817	-	-
Assigned to:			
General government administration	175,664	-	-
Judicial administration	72,153	-	-
Public safety	430,906	-	-
Public works	469,790	-	-
Parks & recreation	100,309	-	-
Community development	7,281	-	-
Unassigned:	3,469,721	-	-
Total fund balances	<u>\$ 6,987,833</u>	<u>\$ -</u>	<u>\$ 54,680</u>

10. Risk Management

The risk management programs of the City and School Division are as follows:

Worker's Compensation

Worker's Compensation Insurance is provided through the Virginia Municipal Self Insurance Association for the City and through School Systems of Virginia for the School Division. Benefits are those afforded through the Commonwealth of Virginia as outlined in *Code of Virginia* §65.2-100. Premiums are based on covered payroll, job rates and claims experience. Total premiums for the current year were \$487,511 and \$78,908 for the City and School Division, respectively.

General Liability and Other

The City provides general liability and other insurance through Selective Insurance Company of America. General liability and business automobile have a \$2,000,000 limit. Boiler and machinery coverage and property insurance are covered as per statement of values. The City maintains an additional \$5,000,000 umbrella policy over all forms of liability. In addition, both police professional liability and public officials' liability insurance with a \$1,000,000 limit are covered through a policy with the Commonwealth of Virginia. Total premiums for the current fiscal year were \$491,596.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

10. Risk Management (Continued)

General Liability and Other (Continued)

The School Division provides general liability and other insurance through the Virginia Municipal League (VML) Self Insurance Association. General liability and business automobile have a \$1,000,000 limit. Boiler and machinery coverage and property insurance are covered as per statement of values. The School Division maintains an additional \$10,000,000 umbrella policy over all forms of liability. Total premiums for the current fiscal year were \$114,467.

Healthcare

The City's professionally administered self-insurance program provides health coverage for employees of the City and School Division on a cost-reimbursement basis. All active employees, retired City employees and retired School employees pay a premium equivalent for participation. Effective October 1, 2010, the premium equivalent represented a minimum of 5% active or retired employee participation. Effective October 1, 2011, the premium increased to 10% participation. The City is obligated for claims payments under the program. A stop loss insurance contract executed with an insurance carrier covers claims in excess of \$150,000 per covered individual and approximately \$7,149,180 in the aggregate.

During the current fiscal year total claim expenses of \$6,048,672, which did not exceed the stop loss provisions, were incurred. This represents claims processed and an estimate for claims incurred but not reported (IBNR) as of June 30, 2012. The assigned portion of fund balance for self-insurance equaled \$939,292 at year-end. The estimated liability for both the City and School Division was \$738,264 at year-end.

Changes in the reported liability during the last three fiscal years are as follows:

Year Ended June 30	Beginning Balance	Claim Expenses	Claim Payments	Ending Balance
2012	\$ 798,857	\$ 6,048,672	\$ 6,109,265	\$ 738,264
2011	\$ 685,650	\$ 5,884,636	\$ 5,771,429	\$ 798,857
2010	\$ 618,152	\$ 5,417,326	\$ 5,349,828	\$ 685,650

Other

There were no significant changes in insurance coverage from the prior year and no settlements that exceeded the amount of insurance coverage during the last three fiscal years.

11. Pension Plan

Plan Description

The City and School Division contribute to the Virginia Retirement System (VRS), a mixed agent and cost-sharing multiple-employer defined benefit pension plan administered by the Virginia Retirement System (System). Professional employees of the School Division participate in a VRS statewide teacher cost-sharing pool and non-professional employees of the School Division participate as a separate group in the agent multiple-employer retirement system.

All full-time, salaried permanent (professional) employees of public school divisions and employees of participating employers are automatically covered by VRS upon employment. Benefits vest after five years of service credit. Members earn one month of service credit for each month they are employed and their employer is paying into the VRS. Members are eligible to purchase prior public service, active duty military service, certain periods of leave and previously refunded VRS service as credit in their plan.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

11. Pension Plan (Continued)

Plan Description (Continued)

VRS administers two defined benefit plans for local government employees – Plan 1 and Plan 2:

- Members hired before July 1, 2010 and who have service credits before July 1, 2010 are covered under Plan 1. Non-hazardous duty members are eligible for an unreduced retirement benefit beginning at age 65 with at least five years of service credit or age 50 with at least 30 years of service credit. They may retire with a reduced benefit as early as 55 with at least five years of service credit or age 50 with at least 10 years of service credit.
- Members hired or rehired on or after July 1, 2010 and who have no service credits before July 1, 2010 are covered under Plan 2. Non-hazardous duty members are eligible for an unreduced benefit beginning at their normal Social Security retirement age with at least five years of service credit or when the sum of their age and service equals 90. They may retire with a reduced benefit as early as age 60 with at least five years of service credit.
- Eligible hazardous duty members in Plan 1 and Plan 2 are eligible for an unreduced benefit beginning at age 60 with at least 5 years of service credit or age 50 with at least 25 years of service credit. These members include sheriffs, deputy sheriffs and hazardous duty employees of political subdivisions that have elected to provide enhanced coverage for hazardous duty service. They may retire with a reduced benefit as early as age 50 with at least five years of service credit. All other provisions of the member's plan apply.

The VRS Basic Benefit is a lifetime monthly benefit based on a retirement multiplier as a percentage of the member's average final compensation multiplied by the member's total service credit. Under Plan 1, average final compensation is the average of the member's 36 consecutive months of highest compensation. Under Plan 2, average final compensation is the average of the member's 60 consecutive months of highest compensation. The retirement multiplier for non-hazardous duty members is 1.70%. The retirement multiplier for sheriffs and regional jail superintendents is 1.85%. The retirement multiplier for eligible political subdivision hazardous duty employees other than sheriffs and jail superintendents is 1.70% or 1.85% as elected by the employer. At retirement, members can elect the Basic Benefit, the Survivor Option, a Partial Lump-Sum Option Payment (PLOP) or the Advance Pension Option. A retirement reduction factor is applied to the Basic Benefit amount for members electing the Survivor Option, PLOP or Advance Pension Option or those retiring with a reduced benefit.

Retirees are eligible for an annual cost-of-living adjustment (COLA) effective July 1 of the second calendar year of retirement. Under Plan 1, the COLA cannot exceed 5%; under Plan 2, the COLA cannot exceed 6%. During years of no inflation or deflation, the COLA is 0%. The VRS also provides death and disability benefits. Title 51.1 of the *Code of Virginia* (1950), as amended, assigns the authority to establish and amend benefit provisions to the General Assembly of Virginia.

The system issues a publicly available comprehensive annual financial report (CAFR) that includes financial statements and required supplementary information for the plans administered by VRS. A copy of the most recent report may be obtained from the VRS Web site at <http://www.varetire.org/Pdf/Publications/2011-annual-report.pdf>, or by writing to the System's Chief Financial Officer at P.O. Box 2500, Richmond, VA 23218-2500.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

11. Pension Plan (Continued)

Funding Policy

Plan members are required by Title 51.1 of the *Code of Virginia* (1950), as amended, to contribute 5% of their compensation toward their retirement. This 5% member contribution has been assumed by both the City and School Division. In addition, the City and School Division are required to contribute the remaining amounts necessary to fund its participation in the VRS using the actuarial basis specified by the *Code of Virginia* and approved by the VRS Board of Trustees. The City's and School Division's non-professional employee contribution rates for the fiscal year ended June 30, 2012 were 16.78% and 11.49% of the annual covered payroll, respectively (including the employee share of 5% paid by the employer).

For the three years ended June 30, 2012, 2011 and 2010, total employer and employee contributions made to the VRS statewide teacher cost-sharing pool for professional employees by the School Division were \$2,403,733, \$1,881,002, and \$2,470,710 representing 11.33%, 8.93%, 5% (last three months of the fiscal year 2010), and 13.81% (first nine months of the fiscal year 2010) of annual covered payroll, respectively (including the employee share of 5% paid by the employer). Contributions for fiscal year 2010 were reduced in the last three months of the year because of a VRS holiday.

Annual Pension Cost

For the fiscal year ended June 30, 2012, the City's and School Division's annual pension cost of \$3,803,207 and \$142,347, respectively, for VRS were equal to their required and actual contributions.

Three-Year Trend Information

	Fiscal Year Ending	Annual Pension	Percentage of	Net Pension
		Cost (APC)	APC Contributed	
City of Salem	June 30, 2012	\$ 3,803,207	100%	\$ -
	June 30, 2011	\$ 3,810,025	100%	\$ -
	June 30, 2010	\$ 3,487,206	100%	\$ -
Component Unit Non-Professional Staff	June 30, 2012	\$ 142,347	100%	\$ -
	June 30, 2011	\$ 142,127	100%	\$ -
	June 30, 2010	\$ 136,108	100%	\$ -

The fiscal year 2012 required contribution was determined as part of the June 30, 2009 actuarial valuation using the entry age normal actuarial cost method. The actuarial assumptions at June 30, 2009 included (a) an investment rate of return (net of administrative expenses) of 7.50%, (b) projected salary increases ranging from 3.75% to 5.60% per year for general government employees and 3.50% to 4.75% per year for employees eligible for enhanced benefits available to law enforcement officers, firefighters and sheriffs, and (c) a cost-of-living adjustment of 2.50% per year. Both the investment rate of return and the projected salary increases also include an inflation component of 2.50%. The actuarial value of the City's and School Division's assets is equal to the modified market value of assets. This method uses techniques that smooth the effects of short-term volatility in the market value of assets over a five-year period. The City's and School Division's unfunded actuarial accrued liabilities are being amortized as a level percentage of projected payroll on an open basis. The remaining amortization period at June 30, 2009 for the unfunded actuarial accrued liability (UAAL) was 20 years.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

11. Pension Plan (Continued)

Funded Status and Funding Progress

As of June 30, 2011, the most recent actuarial valuation date for the City, the plan was 74.43% funded. The actuarial accrued liability for benefits was \$170,752,509 and the actuarial value of assets was \$127,092,832, resulting in an unfunded actuarial accrued liability (UAAL) of \$43,659,677. The covered payroll (annual payroll of active employees covered by the plan) was \$22,707,562 and the ratio of the UAAL to the covered payroll was 192.27%.

As of June 30, 2011, the most recent actuarial valuation date for the School Division's non-professional employees, the plan was 95.43% funded. The actuarial accrued liability for benefits was \$4,369,904 and the actuarial value of assets was \$4,170,371, resulting in an unfunded actuarial accrued liability (UAAL) of \$199,533. The covered payroll (annual payroll of active employees covered by the plan) was \$1,218,992 and the ratio of the UAAL to the covered payroll was 16.37%.

The schedule of funding progress, presented as Required Supplementary Information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability (AAL) for benefits.

12. Other Postemployment Benefits

GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions* establishes standards for the measurement, recognition and display of OPEB expense and related liabilities in the financial statements. In addition to salary, many employees earn benefits over their years of service that will not be received until they retire. The cost of these postemployment benefits are part of the compensation employees earn each year, rather than costs of future years when the benefits are paid and should be recognized during their years of service.

In accordance with GASB 45, an actuarial valuation was performed as of June 30, 2011. The specific limitations, which the new actuarial valuation was based on, are outlined under the plan description.

Plan Description

The City and School Division participate in a single-employer defined benefit healthcare plan (Retiree Health Plan) administered and sponsored by the City. Effective October 1, 2010, full-time employees retiring from the City with at least 15 years of service and receiving an early or regular retirement benefit from the VRS are eligible to participate in the Retiree Health Plan.

Eligible employees and dependents covered at the time of retirement may continue participation in the Retiree Health Plan at the same premium levels as active employees. This creates a benefit to the retiree in the form of a lower insurance rate by blending retirees with active employees, also known as an implicit rate subsidy.

In addition to the implicit rate subsidy, all pre-65 retirees who retired on or before September 30, 2010 will receive a premium subsidy for 95% of the subscriber-only premium rate. For individuals retiring on or after October 1, 2010, the City will contribute 3% of the subscriber-only premium for each year of service up to 95% of the total subscriber-only premium for pre-65 retirees. Effective October 1, 2011, the maximum subsidy was reduced to 90% of the total subscriber-only premium for pre-65 retirees. Employees hired on or after July 1, 2010 will receive a maximum subsidy of 50% of the total subscriber-only premium for pre-65 retirees.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

12. Other Postemployment Benefits (Continued)

Plan Description (Continued)

When a retiree turns age 65 or otherwise becomes eligible for Medicare, the retiree transfers to a Medicare Health Supplement and Part D Drug plan. These individuals no longer receive the implicit rate subsidy; however, they still receive a premium subsidy for 95% of the subscriber-only premium rate. Effective January 1, 2011, the City contributed 3% of the subscriber-only premium for each year of service up to 95% and not to exceed \$3,300. Effective January 1, 2012, the maximum contribution was reduced to 90% not to exceed \$3,300. Employees hired on or after July 1, 2010 are no longer eligible to receive the Medicare Health Supplement and Part D Drug plan benefit.

City retirees do not receive a premium subsidy for dependents and are responsible to pay the difference in the actual premium rates above the premium subsidy. School Division retirees do not receive any premium subsidy and are responsible to pay the entire premium.

The benefits and employee/employer contributions are governed by City Council or School Board policy and can be amended through Council or School Board action. The Retiree Health Plan does not issue a publicly available financial report.

The City participates in the Virginia Pooled OPEB Trust Fund, an irrevocable trust established for the purpose of accumulating assets to fund postemployment benefits other than pensions. The Virginia Pooled OPEB Trust Fund issues a separate report. Financial statements may be obtained from VML/VACo Finance Program, PO Box 12164, Richmond, Virginia 23241.

As of June 30, 2011, the date of the latest actuarial valuation for the City and School Division, plan participation consisted of:

	City of Salem	Component Unit
Active employees	520	528
Retired participants	<u>269</u>	<u>67</u>
Total participants	<u>789</u>	<u>595</u>

Funding Policy

The Retiree Health Plan is funded through member and employer contributions. Effective October 1, 2010, City Retirees receiving benefits contributed a minimum of 5%, 25%, 48% and 48% of the health insurance premium rate for subscriber only, subscriber + one minor child, employee & spouse, and family coverage, respectively. Effective October 1, 2011, these rates increased to 10%, 29%, 50% and 50%, respectively. School Division Retirees receiving benefits contributed 100% of the health insurance premium rate. Retired City and School Division members contributed \$271,345 and \$342,478, respectively, of the total premiums through their required contributions of between \$3.15 and \$1,361, depending on the type of coverage and years of service.

Based on the June 30, 2011 actuarial valuation, the City contributed \$2,004,206 to the Retiree Health Plan. Included in this amount is a current year contribution of \$437,743 to the Virginia Pooled OPEB Trust, which consisted of \$248,816 representing 100% of the annual required contribution (ARC) and \$188,927 to reduce the net other postemployment benefit (OPEB) obligation. It is the City's intent to reduce this obligation to zero and fully fund the ARC each year.

Based on the June 30, 2011 actuarial valuation, the School Division contributed \$358,140 to the Retiree Health Plan. Included in this amount is a current year contribution of \$129,617 to the Virginia Pooled OPEB Trust, which consisted of \$56,374 representing 100% of the annual required contribution (ARC) and \$73,243 to create a net other postemployment benefit (OPEB) asset. It is the School Division's intent to fully fund the ARC each year.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

12. Other Postemployment Benefits (Continued)

Annual OPEB Cost and Net OPEB Obligation

The City's and School Division's annual OPEB cost is calculated based on the ARC of the employer, an amount actuarially determined in accordance with the parameters of Governmental Accounting Standards Board (GASB) Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other than Pensions*. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal costs each year and amortize any unfunded actuarial liability (or funding excess) over a period not to exceed 30 years.

The following table presents the City's and School Division's annual OPEB cost, amount contributed and changes in the net OPEB obligation for the fiscal year ended June 30, 2012.

	City of Salem	Component Unit
Annual required contribution	\$ 1,805,415	\$ 284,897
Interest on net OPEB obligation	69,382	-
Adjustment to annual required contribution	(59,520)	-
Annual OPEB cost	1,815,277	284,897
Contributions made	(2,004,206)	(358,140)
Decrease in net OPEB obligation	(188,929)	(73,243)
Net OPEB obligation (asset), beginning	988,162	-
Net OPEB obligation (asset), ending	<u>\$ 799,233</u>	<u>\$ (73,243)</u>

The following table presents the three-year trend information on the City's and School Division's annual OPEB cost, percentage of annual OPEB cost contributed and net OPEB obligation.

Three-Year Trend Information

	Fiscal Year Ending	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation (Asset)
City of Salem	June 30, 2012	\$ 1,815,277	110.4%	\$ 799,233
	June 30, 2011	\$ 1,812,735	104.3%	\$ 988,162
	June 30, 2010	\$ 1,765,258	105.7%	\$ 1,065,890
Component Unit	June 30, 2012	\$ 284,897	125.7%	\$ (73,243)
	June 30, 2011	\$ 326,317	100.0%	\$ -
	June 30, 2010	\$ 277,617	100.0%	\$ -

Funded Status and Funding Progress

As of June 30, 2011, the City's most recent actuarial valuation date, the plan was 9.9% funded. The actuarial accrued liability (AAL) for benefits was \$24,152,578 and the actuarial value of assets was \$2,384,957, resulting in an unfunded actuarial accrued liability (UAAL) for benefits of \$21,767,621. The covered payroll (annual payroll of active employees covered by the plan) was \$22,707,562 and the ratio of the UAAL to the covered payroll was 95.9%.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

12. Other Postemployment Benefits (Continued)

Funded Status and Funding Progress (Continued)

As of June 30, 2011, the School Division's most recent actuarial valuation date, the plan was 15.1% funded. The AAL for benefits was \$3,041,121 and the actuarial value of assets was \$460,426, resulting in a UAAL for benefits of \$2,580,695. The covered payroll (annual payroll of active employees covered by the plan) was \$22,300,816 and the ratio of the UAAL to the covered payroll was 11.6%.

The schedule of funding progress, presented as Required Supplementary Information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the AAL for benefits.

Methods and Assumptions

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality and healthcare cost trends. Amounts determined regarding the funded status of the plan and the ARC of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

Calculations for financial reporting purposes are based on the benefits provided under terms of the substantive plan (the plan as understood by the employer and the plan members) in effect at the time of each valuation and on the pattern of sharing of costs between the employer and plan members to that point. The projection of benefits for financial reporting purposes does not explicitly incorporate the potential effects of legal or contractual funding limitations on the pattern of cost sharing between the employer and plan members in the future. Actuarial calculations reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in AAL and the actuarial value of assets.

The actuarial methods and assumptions, which are the basis for the actuarial valuation are detailed in the following schedule. The investment rate of return shown was based on the projected returns of the Virginia Pooled OPEB Trust.

	<u>City of Salem</u>	<u>Component Unit</u>
Actuarial valuation date	June 30, 2011	June 30, 2011
<u>Actuarial methods</u>		
Actuarial cost method	Projected Unit Credit	Projected Unit Credit
Amortization method	Level percent of payroll	Level percent of payroll
Amortization period	Open over 30 years	Open over 30 years
Asset valuation method	Cost basis	Cost basis
Liability valuation method	Closed group	Closed group
<u>Actuarial assumptions</u>		
Investment rate of return	7.00%	7.00%
Projected annual salaries increase	2.50%	2.50%
Healthcare cost trend rate	10% for fiscal year 2011 grading to 5% for fiscal year 2016	10% for fiscal year 2011 grading to 5% for fiscal year 2016

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

13. Operating Leases

Rental Costs

The City and School Division entered several non-cancelable operating leases for office space and equipment. Rent expenditures for the current year were \$79,589 and \$58,929 for the City and School Division, respectively. Scheduled minimum rental payments for the next five years are as follows:

Fiscal Year Ending	Governmental Activities	Component Unit
June 30, 2013	\$ 86,549	\$ 34,012
June 30, 2014	70,888	30,759
June 30, 2015	47,460	15,092
June 30, 2016	5,844	11,421
June 30, 2017	4,870	5,962
	\$ 215,611	\$ 97,246

Rental Revenues

The City entered into a fifteen year lease agreement with the General Services Administration (GSA). The lease provides for the use of 2,875 rentable square feet of space located on the third floor of the City of Salem Police Department at 36 East Calhoun Street, Salem, Virginia 24153 to be used for such purposes as may be determined by the GSA. The lease includes a five year renewal option under the same terms and conditions. The net book value of leased assets of \$1,783,547 (cost of \$1,843,485 less accumulated depreciation of \$59,938) is included in capital assets in the government-wide financial statements. Rent revenues for the current year were \$123,127. Scheduled minimum rental revenues over the remaining lease period are \$1,796,008. Scheduled minimum rental revenues for the next five years are as follows:

Fiscal Year	Total Revenues
June 30, 2013	\$ 127,942
June 30, 2014	127,942
June 30, 2015	127,942
June 30, 2016	127,942
June 30, 2017	127,942
	\$ 639,710

14. Commitments and Contingencies

Construction Commitments

Active construction projects at the end of the year are as follows:

	Spent To Date	Remaining Contract
Water Storage Tank Renovation	\$ 60,696	\$ 74,184
Roanoke River Greenway Phase 3A	186,464	361,486
South Salem Elementary School	413,002	14,508,832
	\$ 660,162	\$14,944,502

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

14. Commitments and Contingencies (Continued)

Electrical Service

On July 1, 2006, the City entered an agreement with American Electric Power Service Corporation to purchase electricity for consumption and resale to City residents. The rates are recalculated annually based on the supplier's cost. As part of the agreement, an annual cost true-up is required based upon American Electric Power's FERC filing. The City's policy is to recognize the true-up as an expense when it is billed. The true-up for December 31, 2011 expensed in the current fiscal year was \$30,373. The agreement expires May 31, 2026 with two possible five-year period renewals and may be terminated under certain circumstances.

On July 1, 2006, the City entered an agreement with the United States Department of Energy to purchase electricity during American Electric Power's peak usage periods. The agreement requires a 37-month notification prior to termination.

Solid Waste Disposal

On July 1, 2006, the City entered an agreement with Waste Management Inc. for disposal of nonhazardous solid waste. The agreement amended the original contract by extending the expiration date to June 30, 2016.

On January 1, 2008, the City entered an agreement with Botetourt County to accept the County's solid waste at the City's transfer station. The agreement expires June 30, 2016 or upon expiration of the City's agreement with Waste Management, Inc., whichever occurs first.

Water and Wastewater Treatment Contract

On July 1, 1981, the City entered an agreement with County of Roanoke, Virginia to sell surplus water at a bulk rate determined by a mutually agreed upon formula. The agreement expires June 30, 2021. The agreement automatically renews for 10-year terms upon expiration and requires a 24-month notification prior to termination.

On November 1, 2003, the City entered an agreement with the City of Roanoke, Virginia for the transportation and treatment of wastewater and to fund a portion of the sewage treatment plant improvements. Rates for the former services are adjusted annually, while the costs recognized by the City for the latter have been capitalized as the sewage treatment contract in capital assets. The agreement expires October 31, 2033.

On July 1, 2004, the Western Virginia Water Authority (WVWA) was created by the County of Roanoke and the City of Roanoke. The WVWA is a full service authority that provides water and wastewater treatment to the Roanoke Valley region. This authority assumed both of the previously mentioned water and wastewater treatment contractual obligations.

Special Services

On July 1, 1973, the City entered an agreement with the County of Roanoke, Virginia for social services, agricultural and home demonstration services and jail services. The agreement can be renewed or terminated at the end of any two-year period with proper notice.

Performance Agreement

On July 30, 2008, the City entered a performance agreement with a company to provide incentive payments for development of property located at 4th Street and Main Street. The City will make maximum annual payments of \$500,000 for no more than 10 years not to exceed \$3,000,000. As of June 30, 2012, \$462,347 has been remitted.

Special Purpose Grants

Special purpose grants are subject to audit to determine compliance with their requirements. City officials believe that if any refunds are required, they will be immaterial.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

14. Commitments and Contingencies (Continued)

Litigation

Various claims and lawsuits are pending against the City. In the opinion of management, after consulting with legal counsel, the potential loss on all claims and lawsuits will not materially affect the City's financial position.

15. Jointly Governed Organizations

The following entities are considered to be jointly governed. The City has no ongoing financial responsibility or interest in jointly governed organizations.

Blue Ridge Behavioral Healthcare

The Counties of Botetourt, Craig and Roanoke and the Cities of Roanoke and Salem formed Blue Ridge Behavioral Healthcare (BRBH) to provide a system of comprehensive community mental health, mental retardation and substance abuse services. BRBH is governed by a 16-member board; three members are appointed by the City of Salem. Each locality's financial obligation is based on the type and amount of services performed for individuals in the locality. For the year ended June 30, 2012, the City remitted \$103,500 to BRBH for services. Financial statements may be obtained from Blue Ridge Behavioral Healthcare at 301 Elm Street, Roanoke, Virginia, 24016.

Roanoke Valley Detention Commission

The Counties of Botetourt, Franklin and Roanoke and the Cities of Roanoke and Salem formed the Roanoke Valley Detention Commission (Commission) to renovate, expand and operate a detention facility for juveniles. The Commission is governed by a six-member board, of which one member is appointed by the City of Salem. Each locality's financial obligation is based on the number of juveniles housed at the facility. The Commission has the authority to issue debt and such debt is the responsibility of the Commission. For the year ended June 30, 2012, the City remitted \$201,490 to the Commission for per diem charges. Financial statements may be obtained from the Roanoke Valley Detention Commission at 498 Coyner Springs Road, Roanoke, Virginia 24012.

Roanoke Valley Regional Board

The Counties of Botetourt, Craig and Franklin, the City of Roanoke and the City of Salem School Division jointly participate in a regional education program for severely disabled students operated by the Roanoke Valley Regional Board (Regional Board). The Regional Board is governed by a five-member board, one from each participating locality. The School Division has control over budget and financing only to the extent of representation by the one board member appointed. Each locality's financial obligation is based on their proportionate share of students attending the regional program. For the year ended June 30, 2012, the School Division remitted \$661,212 to the Regional Board for services. Financial statements may be obtained from the Roanoke Valley Regional Board at 12 Barron Drive, Suite 1, Troutville, Virginia 24175.

Roanoke Valley Regional Fire/EMS Training Center

The County of Roanoke, the Cities of Roanoke and Salem and the Town of Vinton jointly operate a fire/EMS training center (Center). The Center is governed by a committee designated by the participating jurisdictions. New fire/EMS recruits are required to take a 17-week training course at the facility before being assigned to a station. After completion of the training, the new recruits are state certified. Each jurisdiction is responsible for a percentage of the annual operating costs of the facility. The City of Salem is responsible for 8% of the annual operating costs. For the year ended June 30, 2012, the City remitted \$7,090 for operating costs of the facility. Financial statements may be obtained from the Roanoke Valley Regional Fire/EMS Training Center at 1220 Kessler Mill Road, Salem, Virginia 24153.

**CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012**

15. Jointly Governed Organizations (Continued)

Western Virginia Regional Jail Authority

The Counties of Franklin, Montgomery and Roanoke and the City of Salem formed the Western Virginia Regional Jail Authority (Jail Authority) to develop and operate a regional jail. The Jail Authority is governed by a 12-member board; three from each participating locality. Each locality's financial obligation is based on the number of prisoner days used and a share of the capital costs to build the facility. For the year ended June 30, 2012, the City remitted \$904,599 for per diem charges and \$379,635 for capital costs to the Jail Authority. Financial statements may be obtained from Western Virginia Regional Jail Authority at 5885 West River Road, Salem, Virginia 24153.

16. Subsequent Event

Prior to June 30, 2012, Salem City Council authorized the issuance of up to \$15 million general obligation bonds to finance the South Salem School Project. On October 10, 2012, the City issued a general obligation note in the amount of \$5,010,000 to obtain interim financing for the design, engineering, replacement, acquisition, construction, and equipping of capital facilities for the new South Salem Elementary School, together with related costs and expenses, through the VML/VACo Commercial Paper Program.

17. New Accounting Standards

The GASB has issued Statement No. 61, *The Financial Reporting Entity: Omnibus-an amendment of GASB Statements No. 14 and No. 34*, which provides guidance for including, presenting, and disclosing information about component units and equity interest transactions of a financial reporting entity. The provisions of this statement are effective for financial statements for periods beginning after June 15, 2012. Management has not completed the process of evaluating the impact that will result from adoption of the standard and is therefore unable to disclose the impact of adoption.

The GASB has issued Statement 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. The statement standardizes the presentation of deferred outflows of resources and deferred inflows of resources and their effects on a government's net position. The provisions of this statement are effective for financial statements for periods beginning after December 15, 2011. Management has not completed the process of evaluating the impact that will result from adoption of the standard and is therefore unable to disclose the impact of adoption.

The GASB has issued Statement 65, *Items Previously Reported as Assets and Liabilities*. The statement clarifies the appropriate use of the financial statement elements deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting. The provisions of this statement are effective for financial statements for periods beginning after December 15, 2012. Management has not completed the process of evaluating the impact that will result from adoption of this standard and is therefore unable to disclose the impact of adoption.

The GASB has issued Statement 66, *Technical Corrections-2012-an amendment of GASB Statements No. 10 and No. 62*. The statement resolves conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The provisions of this statement are effective for financial statements for periods beginning after December 15, 2012. Management has not completed the process of evaluating the impact that will result from adoption of the standard and is therefore unable to disclose the impact of adoption.

CITY OF SALEM, VIRGINIA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2012

17. New Accounting Standards (Continued)

The GASB has issued Statement 67, *Financial Reporting for Pension Plans-an amendment of GASB Statement No. 25*. The statement requires enhanced note disclosures and schedules of required supplementary information that will be presented by the pension plans that are within its scope. The new information will enhance the decision-usefulness of the financial reports of these pension plans, their value for assessing accountability, and their transparency by providing information about measures of net pension liabilities and explanations of how and why those liabilities changed from year to year. The provisions of this statement are effective for fiscal years beginning after June 15, 2013. Management has not completed the process of evaluating the impact that will result from adoption of the standard and is therefore unable to disclose the impact of adoption.

The GASB has issued Statement 68, *Accounting and Financial Reporting for Pensions-an amendment of GASB Statement No. 27*. The statement will improve the decision-usefulness of information in employer and governmental nonemployer contributing entity financial reports and will enhance its value for assessing accountability and interperiod equity by requiring recognition of the entire net pension liability and a more comprehensive measure of pension expense. Decision-usefulness and accountability also will be enhanced through new note disclosures and required supplementary information. The provisions of this statement are effective for fiscal years beginning after June 15, 2014. Management has not completed the process of evaluating the impact that will result from adoption of the standard and is therefore unable to disclose the impact of adoption.

REQUIRED SUPPLEMENTARY INFORMATION



The Required Supplementary Information subsection of the City of Salem, Virginia's Comprehensive Annual Financial Report includes an analysis of funding progress for the defined benefit pension plan, an analysis of funding progress for other postemployment benefits, and employer contributions for other postemployment benefits.

CITY OF SALEM, VIRGINIA
REQUIRED SUPPLEMENTARY INFORMATION
ANALYSIS OF FUNDING PROGRESS FOR DEFINED BENEFIT PENSION PLAN
JUNE 30, 2012

City of Salem

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded Actuarial Accrued Liability (UAAL)	Funded Ratio	Annual Covered Payroll	UAAL as of Percentage of Covered Payroll
	(a)	(b)	(b-a)	(a/b)	(c)	((b-a)/c)
June 30, 2011	\$ 127,092,832	\$ 170,752,509	\$ 43,659,677	74.43%	\$ 22,707,562	192.27%
June 30, 2010	\$ 126,786,583	\$ 166,392,547	\$ 39,605,964	76.20%	\$ 23,172,968	170.91%
June 30, 2009	\$ 129,680,495	\$ 153,476,528	\$ 23,796,033	84.50%	\$ 24,004,460	99.13%

Component Unit
School Division (Non-Professional Staff)

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded Actuarial Accrued Liability (UAAL)	Funded Ratio	Annual Covered Payroll	UAAL as of Percentage of Covered Payroll
	(a)	(b)	(b-a)	(a/b)	(c)	((b-a)/c)
June 30, 2011	\$ 4,170,371	\$ 4,369,904	\$ 199,533	95.43%	\$ 1,218,992	16.37%
June 30, 2010	\$ 4,130,907	\$ 4,030,617	\$ (100,290)	102.49%	\$ 1,258,062	-7.97%
June 30, 2009	\$ 4,144,935	\$ 4,243,552	\$ 98,617	97.68%	\$ 1,538,657	6.41%

CITY OF SALEM, VIRGINIA
REQUIRED SUPPLEMENTARY INFORMATION
ANALYSIS OF FUNDING PROGRESS FOR OTHER POSTEMPLOYMENT BENEFITS
JUNE 30, 2012

City of Salem

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded Actuarial Accrued Liability (UAAL)	Funded Ratio	Annual Covered Payroll	UAAL as of Percentage of Covered Payroll
	(a)	(b)	(b-a)	(a/b)	(c)	((b-a)/c)
June 30, 2011	\$ 2,384,957	\$ 24,152,578	\$ 21,767,621	9.9%	\$ 22,707,562	95.9%
July 1, 2009	\$ 936,910	\$ 23,073,994	\$ 22,137,084	4.1%	\$ 24,004,460	92.2%
July 1, 2008	\$ -	\$ 37,824,191	\$ 37,824,191	0.0%	\$ 22,986,624	164.5%

**Component Unit
School Division**

Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL)	Unfunded Actuarial Accrued Liability (UAAL)	Funded Ratio	Annual Covered Payroll	UAAL as of Percentage of Covered Payroll
	(a)	(b)	(b-a)	(a/b)	(c)	((b-a)/c)
June 30, 2011	\$ 460,426	\$ 3,041,121	\$ 2,580,695	15.1%	\$ 22,300,816	11.6%
July 1, 2008	\$ -	\$ 2,594,210	\$ 2,594,210	0.0%	\$ 23,509,649	11.0%

**CITY OF SALEM, VIRGINIA
REQUIRED SUPPLEMENTARY INFORMATION
EMPLOYER CONTRIBUTIONS FOR OTHER POSTEMPLOYMENT BENEFITS
JUNE 30, 2012**

City of Salem

<u>Fiscal year</u>	<u>Annual Required Contribution</u>	<u>Percentage Contributed</u>
June 30, 2012	\$ 1,805,415	111.0%
June 30, 2011	\$ 1,802,502	104.9%
June 30, 2010	\$ 1,754,024	106.3%

**Component Unit
School Division**

<u>Fiscal year</u>	<u>Annual Required Contribution</u>	<u>Percentage Contributed</u>
June 30, 2012	\$ 284,897	125.7%
June 30, 2011	\$ 326,317	100.0%
June 30, 2010	\$ 277,617	100.0%

OTHER SUPPLEMENTARY INFORMATION



The Other Supplementary Information subsection of the City of Salem, Virginia's Comprehensive Annual Financial Report includes the combining statement of net assets; combining statement of revenues, expenses, and changes in fund net assets; and combining statement of cash flows for the nonmajor proprietary funds. This subsection also includes the combining statement of fiduciary assets and liabilities and the combining statement of changes in fiduciary assets and liabilities for the agency funds.

CITY OF SALEM, VIRGINIA
COMBINING STATEMENT OF NET ASSETS
NONMAJOR PROPRIETARY FUNDS
JUNE 30, 2012

	Business-type Activities - Enterprise Funds		
	Civic Center	Catering and Concessions	Total Nonmajor Proprietary Funds
ASSETS			
<i>Current assets:</i>			
Cash and cash equivalents	\$ 285	\$ 63,802	\$ 64,087
Receivables, net	105,631	47,038	152,669
Due from other funds	-	65,000	65,000
Inventories	-	18,087	18,087
Prepaid items	77,356	-	77,356
Total current assets	183,272	193,927	377,199
<i>Capital assets:</i>			
Nondepreciable	176,653	-	176,653
Depreciable, net	5,858,602	31,075	5,889,677
Total capital assets	6,035,255	31,075	6,066,330
Total assets	6,218,527	225,002	6,443,529
LIABILITIES			
<i>Current liabilities:</i>			
Accounts payable and accrued liabilities	90,550	39,989	130,539
Accrued payroll and related liabilities	40,263	7,169	47,432
Self insurance claims liability	12,850	2,859	15,709
Due to other funds	65,000	-	65,000
Unearned revenue	133,310	1,245	134,555
Compensated absences	73,188	23,946	97,134
Total current liabilities	415,161	75,208	490,369
<i>Long-term liabilities:</i>			
Compensated absences	45,983	20,726	66,709
Other postemployment benefits	31,456	10,090	41,546
Total long-term liabilities	77,439	30,816	108,255
Total liabilities	492,600	106,024	598,624
NET ASSETS (DEFICIT)			
Invested in capital assets, net of related debt	6,035,255	31,075	6,066,330
Unrestricted	(309,328)	87,903	(221,425)
Total net assets	\$ 5,725,927	\$ 118,978	\$ 5,844,905

CITY OF SALEM, VIRGINIA
COMBINING STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
NONMAJOR PROPRIETARY FUNDS
YEAR ENDED JUNE 30, 2012

	Business-type Activities - Enterprise Funds		
	Civic Center	Catering and Concessions	Total Nonmajor Proprietary Funds
OPERATING REVENUES			
Charges for services	\$ 836,023	\$ 838,928	\$ 1,674,951
Commissions	17,881	-	17,881
Other	26,402	17,991	44,393
Total operating revenues	<u>880,306</u>	<u>856,919</u>	<u>1,737,225</u>
OPERATING EXPENSES			
Salaries	1,033,588	342,462	1,376,050
Fringe benefits	372,729	93,431	466,160
Show expenses	119,555	-	119,555
Maintenance	195,765	3,730	199,495
Professional services	7,460	16,875	24,335
Insurance	12,019	-	12,019
Administration	18,968	8,318	27,286
Travel and training	7,017	225	7,242
Materials and supplies	29,063	238,690	267,753
Expendable equipment and small tools	3,030	-	3,030
Utilities	262,627	633	263,260
Miscellaneous	4,880	3,396	8,276
Depreciation	375,569	6,281	381,850
Commissions	-	188,998	188,998
Total operating expenses	<u>2,442,270</u>	<u>903,039</u>	<u>3,345,309</u>
Operating loss	<u>(1,561,964)</u>	<u>(46,120)</u>	<u>(1,608,084)</u>
NONOPERATING REVENUES (EXPENSES)			
Interest income	205	-	205
Gain (loss) on sale of capital assets	(30,461)	-	(30,461)
Net nonoperating revenue (expenses)	<u>(30,256)</u>	<u>-</u>	<u>(30,256)</u>
Income (loss) before contributions and transfers	<u>(1,592,220)</u>	<u>(46,120)</u>	<u>(1,638,340)</u>
Transfers in	<u>1,011,205</u>	<u>1,137</u>	<u>1,012,342</u>
Change in net assets	<u>(581,015)</u>	<u>(44,983)</u>	<u>(625,998)</u>
Net assets, beginning	<u>6,306,942</u>	<u>163,961</u>	<u>6,470,903</u>
Net assets, ending	<u>\$ 5,725,927</u>	<u>\$ 118,978</u>	<u>\$ 5,844,905</u>

CITY OF SALEM, VIRGINIA
COMBINING STATEMENT OF CASH FLOWS
NONMAJOR PROPRIETARY FUNDS
YEAR ENDED JUNE 30, 2012

	Business-type Activities - Enterprise Funds		
	Civic Center	Catering and Concessions	Total Nonmajor Proprietary Funds
OPERATING ACTIVITIES			
Receipts from customers	\$ 865,581	\$ 849,437	\$ 1,715,018
Payments to suppliers	(683,211)	(460,204)	(1,143,415)
Payments to employees	(1,452,548)	(450,327)	(1,902,875)
Other receipts	44,283	17,991	62,274
Net cash used in operating activities	(1,225,895)	(43,103)	(1,268,998)
NONCAPITAL FINANCING ACTIVITIES			
Interfund Loan	65,000	(65,000)	-
Transfers in	1,012,342	-	1,012,342
Net cash provided by (used in) noncapital financing activities	1,077,342	(65,000)	1,012,342
CAPITAL AND RELATED FINANCING ACTIVITIES			
Purchases of capital assets	(2,901,624)	-	(2,901,624)
Net cash used in capital and related financing activities	(2,901,624)	-	(2,901,624)
INVESTING ACTIVITIES			
Interest received	205	-	205
Net cash provided by investing activities	205	-	205
Net decrease in cash and cash equivalents	(3,049,972)	(108,103)	(3,158,075)
Cash and cash equivalents, beginning	3,050,257	171,905	3,222,162
Cash and cash equivalents, ending	<u>\$ 285</u>	<u>\$ 63,802</u>	<u>\$ 64,087</u>
RECONCILIATION OF OPERATING LOSS TO NET CASH USED IN OPERATING ACTIVITIES			
Operating loss	\$ (1,561,964)	\$ (46,120)	\$ (1,608,084)
<i>Adjustments to reconcile operating loss to net cash used in operating activities</i>			
Depreciation	375,569	6,281	381,850
<i>Decrease (increase) in assets:</i>			
Receivables, net	22,678	12,630	35,308
Inventories	-	1,699	1,699
Prepaid items	14,598	-	14,598
<i>Increase (decrease) in liabilities:</i>			
Accounts payable and accrued liabilities	(35,577)	(617)	(36,194)
Accrued payroll and related liabilities	(51,935)	(15,794)	(67,729)
Self insurance claims liability	(1,848)	(421)	(2,269)
Unearned revenue	6,880	(2,121)	4,759
Compensated absences	11,059	2,055	13,114
Other postemployment benefits	(5,355)	(695)	(6,050)
Net cash used in operating activities	<u>\$ (1,225,895)</u>	<u>\$ (43,103)</u>	<u>\$ (1,268,998)</u>

CITY OF SALEM, VIRGINIA
COMBINING STATEMENT OF FIDUCIARY ASSETS AND LIABILITIES
AGENCY FUNDS
JUNE 30, 2012

	Cardinal Criminal Justice Academy	Court- Community Corrections Program	Total Agency Funds
ASSETS			
Cash and cash equivalents	\$ 533,291	\$ 832,842	\$ 1,366,133
Receivables, net	1,197	-	1,197
Due from Commonwealth of Virginia	-	71,616	71,616
Total assets	<u>\$ 534,488</u>	<u>\$ 904,458</u>	<u>\$ 1,438,946</u>
LIABILITIES			
Accounts payable	\$ 7,119	\$ 63,593	\$ 70,712
Liability to agency	527,369	840,865	1,368,234
Total liabilities	<u>\$ 534,488</u>	<u>\$ 904,458</u>	<u>\$ 1,438,946</u>

CITY OF SALEM, VIRGINIA
COMBINING STATEMENT OF CHANGES IN FIDUCIARY ASSETS AND LIABILITIES
AGENCY FUNDS
YEAR ENDED JUNE 30, 2012

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Deductions</u>	<u>Ending Balance</u>
<u>CARDINAL CRIMINAL JUSTICE ACADEMY</u>				
ASSETS				
Cash and cash equivalents	\$ 442,148	\$ 681,019	\$ (589,876)	\$ 533,291
Receivables, net	47,550	5,937	(52,290)	1,197
Total assets	<u>\$ 489,698</u>	<u>\$ 686,956</u>	<u>\$ (642,166)</u>	<u>\$ 534,488</u>
LIABILITIES				
Accounts payable	\$ 3,034	\$ 6,683	\$ (2,598)	\$ 7,119
Liability to agency	486,664	680,273	(639,568)	527,369
Total liabilities	<u>\$ 489,698</u>	<u>\$ 686,956</u>	<u>\$ (642,166)</u>	<u>\$ 534,488</u>
<u>COURT-COMMUNITY CORRECTIONS PROGRAM</u>				
ASSETS				
Cash and cash equivalents	\$ 644,021	\$ 2,513,645	\$ (2,324,824)	\$ 832,842
Due from Commonwealth of Virginia	93,930	71,616	(93,930)	71,616
Total assets	<u>\$ 737,951</u>	<u>\$ 2,585,261</u>	<u>\$ (2,418,754)</u>	<u>\$ 904,458</u>
LIABILITIES				
Accounts payable	\$ 66,415	\$ 61,729	\$ (64,551)	\$ 63,593
Liability to agency	671,536	2,523,532	(2,354,203)	840,865
Total liabilities	<u>\$ 737,951</u>	<u>\$ 2,585,261</u>	<u>\$ (2,418,754)</u>	<u>\$ 904,458</u>
<u>TOTAL AGENCY FUNDS</u>				
ASSETS				
Cash and cash equivalents	\$ 1,086,169	\$ 3,194,664	\$ (2,914,700)	\$ 1,366,133
Receivables, net	47,550	5,937	(52,290)	1,197
Due from Commonwealth of Virginia	93,930	71,616	(93,930)	71,616
Total assets	<u>\$ 1,227,649</u>	<u>\$ 3,272,217</u>	<u>\$ (3,060,920)</u>	<u>\$ 1,438,946</u>
LIABILITIES				
Accounts payable	\$ 69,449	\$ 68,412	\$ (67,149)	\$ 70,712
Liability to agency	1,158,200	3,203,805	(2,993,771)	1,368,234
Total liabilities	<u>\$ 1,227,649</u>	<u>\$ 3,272,217</u>	<u>\$ (3,060,920)</u>	<u>\$ 1,438,946</u>

STATISTICAL SECTION



The Statistical Section of the City of Salem, Virginia's Comprehensive Annual Financial Report presents additional detail, context, and historical information to assist in understanding the information in the financial statements, note disclosures and required supplementary information.

Contents	Page
Financial Trends.....	86
<i>These schedules contain trend information to help the reader understand how the government's financial performance and well-being have changed over time.</i>	
Revenue Capacity.....	91
<i>These schedules contain information to help the reader assess the government's most significant local revenue sources, property tax and sale of electricity.</i>	
Debt Capacity.....	93
<i>These schedules present information to help the reader assess the affordability of the government's current level of outstanding debt and the government's ability to issue additional debt in the future.</i>	
Demographic and Economic Information.....	95
<i>These schedules offer demographic and economic indicators to help the reader understand the environment within which the government's financial activities take place.</i>	
Operating Information.....	97
<i>These schedules contain service and infrastructure data to help the reader understand how the information in the government's financial report relates to the services the government provides and the activities it performs.</i>	

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**TABLE 1
UNAUDITED**

**CITY OF SALEM, VIRGINIA
NET ASSETS BY COMPONENT
LAST TEN FISCAL YEARS**

	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003
						(1)	(2)	(2)	(2)	(2)
Governmental Activities										
Invested in capital assets, net of related debt	\$ 87,145,604	\$ 88,456,284	\$ 90,258,361	\$ 89,946,841	\$ 88,463,741	\$ 85,853,628	\$ 88,112,343	\$ 89,479,130	\$ 88,551,933	\$ 76,959,696
Restricted	1,260,230	1,416,694	-	-	-	-	-	-	2,313,457	2,473,586
Unrestricted	(10,590,213)	(12,606,292)	(9,373,128)	(10,704,656)	(9,598,627)	(9,132,365)	(12,509,444)	(12,674,607)	(15,644,583)	(3,239,660)
Total governmental net assets	<u>\$ 77,815,621</u>	<u>\$ 77,266,686</u>	<u>\$ 80,885,233</u>	<u>\$ 79,242,185</u>	<u>\$ 78,865,114</u>	<u>\$ 76,721,263</u>	<u>\$ 75,602,899</u>	<u>\$ 76,804,523</u>	<u>\$ 75,220,807</u>	<u>\$ 76,193,622</u>
Business-type activities										
Invested in capital assets, net of related debt	\$ 44,265,414	\$ 44,172,488	\$ 43,180,397	\$ 40,790,077	\$ 39,787,750	\$ 41,636,232	\$ 36,954,684	\$ 36,501,799	\$ 31,689,583	\$ 23,078,380
Restricted	-	1,989,529	-	-	-	-	-	-	-	-
Unrestricted	18,453,692	18,896,375	20,437,874	23,324,884	25,278,681	20,760,143	21,804,567	21,839,306	24,685,946	31,038,458
Total business-type activities net assets	<u>\$ 62,719,106</u>	<u>\$ 65,058,392</u>	<u>\$ 63,618,271</u>	<u>\$ 64,114,961</u>	<u>\$ 65,066,431</u>	<u>\$ 62,396,375</u>	<u>\$ 58,759,251</u>	<u>\$ 58,341,105</u>	<u>\$ 56,375,529</u>	<u>\$ 54,116,838</u>
Primary government										
Invested in capital assets, net of related debt	\$ 131,411,018	\$ 132,628,772	\$ 133,438,758	\$ 130,736,918	\$ 128,251,491	\$ 127,489,860	\$ 125,067,027	\$ 125,980,929	\$ 120,241,516	\$ 100,038,076
Restricted	1,260,230	3,406,223	-	-	-	-	-	-	2,313,457	2,473,586
Unrestricted	7,863,479	6,290,083	11,064,746	12,620,228	15,680,054	11,627,778	9,295,123	9,164,699	9,041,363	27,798,798
Total primary government net assets	<u>\$ 140,534,727</u>	<u>\$ 142,325,078</u>	<u>\$ 144,503,504</u>	<u>\$ 143,357,146</u>	<u>\$ 143,931,545</u>	<u>\$ 139,117,638</u>	<u>\$ 134,362,150</u>	<u>\$ 135,145,628</u>	<u>\$ 131,596,336</u>	<u>\$ 130,310,460</u>

Notes:

Source: City of Salem Finance Department

(1) Unrestricted net assets of business-type activities were restated.

(2) Invested in capital assets, net of related debt and unrestricted net assets of governmental activities were restated to properly classify School Division debt.

**TABLE 2
UNAUDITED**

**CITY OF SALEM, VIRGINIA
CHANGES IN NET ASSETS
LAST TEN FISCAL YEARS
(accrual basis of accounting)**

	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003
						(1)			(2)	
Expenses										
<i>Governmental activities</i>										
General government	\$ 6,583,782	\$ 6,110,416	\$ 5,328,382	\$ 5,937,208	\$ 5,031,352	\$ 4,803,246	\$ 5,107,268	\$ 4,283,754	\$ 4,402,755	\$ 4,156,677
Judicial administration	1,866,052	1,887,444	1,779,072	1,897,961	1,687,507	1,540,762	1,457,720	1,292,722	1,224,425	1,190,643
Public safety	16,492,831	15,818,359	15,330,477	15,932,421	15,048,715	13,869,676	13,547,191	11,535,321	10,574,969	10,409,689
Public works	14,421,981	13,915,318	14,019,163	14,906,728	14,067,674	13,476,019	12,443,334	10,789,008	9,603,482	9,471,217
Health and welfare	2,430,955	2,738,894	2,333,736	2,354,803	2,450,245	2,193,126	2,055,166	1,823,783	1,419,802	1,217,958
Education	18,471,653	18,420,000	18,420,000	18,420,000	17,995,000	17,095,000	16,266,005	15,618,081	29,340,564	14,747,635
Parks, recreation and cultural	5,284,647	5,495,431	5,064,065	5,620,844	5,721,997	5,796,220	5,239,517	3,851,575	4,257,005	3,697,241
Community development	2,076,325	1,834,749	1,725,528	1,830,327	1,122,221	1,022,096	933,002	513,272	842,963	1,290,922
Nondepartmental	-	-	-	-	-	-	-	2,424,022	1,788,744	2,253,821
Interest on long-term debt	1,139,218	1,151,867	1,137,667	1,188,350	1,263,858	1,202,201	1,267,296	1,478,103	1,339,037	1,045,306
Total governmental activities	68,767,444	67,372,478	65,138,090	68,088,642	64,388,569	60,998,346	58,316,499	53,609,641	64,793,746	49,481,109
<i>Business-type activities</i>										
Electric	36,047,453	35,145,346	30,978,370	28,763,182	26,505,160	24,308,309	24,692,031	16,311,434	15,116,855	16,810,659
Water and sewage	10,952,702	11,034,638	11,065,592	11,253,172	11,150,046	10,991,783	10,836,280	9,502,885	7,305,334	7,427,270
Civic Center	2,472,731	2,374,165	2,332,330	2,440,459	2,435,383	2,563,090	2,364,891	2,199,589	2,096,344	1,856,562
Catering and concessions	903,039	878,171	965,556	1,033,658	1,081,528	1,103,860	1,036,737	960,320	953,609	932,823
Total business-type activities	50,375,925	49,432,320	45,341,848	43,490,471	41,172,117	38,967,042	38,929,939	28,974,228	25,472,142	27,027,314
Total primary government	\$ 119,143,369	\$ 116,804,798	\$ 110,479,938	\$ 111,579,113	\$ 105,560,686	\$ 99,965,388	\$ 97,246,438	\$ 82,583,869	\$ 90,265,888	\$ 76,508,423
Program revenues										
<i>Governmental activities</i>										
Charges for services										
Public safety	\$ 991,473	\$ 911,073	\$ 900,837	\$ 1,107,794	\$ 1,048,587	\$ 1,148,627	\$ 1,315,417	\$ 1,083,694	\$ 532,717	\$ 553,437
Public works	3,560,239	3,418,637	3,248,138	3,627,290	3,203,179	2,892,913	1,799,284	1,821,717	1,805,400	1,781,202
Other activities	1,005,691	782,662	716,248	587,294	566,814	535,125	471,137	415,225	508,282	426,281
Operating grants and contributions	7,124,704	7,159,171	6,827,928	6,763,352	6,613,064	7,024,034	6,038,168	5,979,520	5,359,113	5,557,143
Capital grants and contributions	595,986	1,517,633	2,709,381	2,119,392	1,359,606	1,168,709	6,392,874	314,789	3,260,581	300,000
Total governmental activities	13,278,093	13,789,176	14,402,532	14,205,122	12,791,250	12,769,408	16,016,880	9,614,945	11,466,093	8,618,063
<i>Business-type activities</i>										
Charges for services										
Electric	36,824,320	35,726,379	32,915,660	30,863,283	31,000,915	29,300,625	27,699,386	20,192,965	20,092,111	19,640,717
Water and sewage	11,114,241	9,988,563	10,329,200	10,981,350	11,569,453	10,740,194	9,529,125	8,510,106	8,368,156	7,663,093
Civic Center	880,306	912,697	865,314	919,781	937,520	1,006,344	793,716	887,312	862,129	716,643
Catering and concessions	856,919	858,714	940,834	994,016	1,048,994	1,097,172	991,208	967,446	975,666	995,280
Capital grants and contributions										
Electric	-	39,929	-	-	-	-	-	-	-	-
Water and sewage	13,222	-	-	-	-	-	-	-	-	-
Total business-type activities	49,689,008	47,526,282	45,051,008	43,758,430	44,556,882	42,144,335	39,013,435	30,557,829	30,298,062	29,015,733
Total primary government	\$ 62,967,101	\$ 61,315,458	\$ 59,453,540	\$ 57,963,552	\$ 57,348,132	\$ 54,913,743	\$ 55,030,315	\$ 40,172,774	\$ 41,764,155	\$ 37,633,796

	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003
Net (expense) revenue										
Total governmental activities	\$ (55,489,351)	\$ (53,583,302)	\$ (50,735,558)	\$ (53,883,520)	\$ (51,597,319)	\$ (48,228,938)	\$ (42,299,619)	\$ (43,994,696)	\$ (53,327,653)	\$ (40,863,046)
Total business-type activities	(686,917)	(1,906,038)	(290,840)	267,959	3,384,765	3,177,293	83,496	1,583,601	4,825,920	1,988,419
Total primary government	<u>\$ (56,176,268)</u>	<u>\$ (55,489,340)</u>	<u>\$ (51,026,398)</u>	<u>\$ (53,615,561)</u>	<u>\$ (48,212,554)</u>	<u>\$ (45,051,645)</u>	<u>\$ (42,216,123)</u>	<u>\$ (42,411,095)</u>	<u>\$ (48,501,733)</u>	<u>\$ (38,874,627)</u>
General Revenues and Other Changes in Net Assets										
<i>Governmental activities:</i>										
Taxes										
Property taxes	\$ 32,480,280	\$ 32,068,912	\$ 31,477,369	\$ 31,335,765	\$ 30,082,026	\$ 27,606,560	\$ 27,161,942	\$ 25,062,245	\$ 24,868,585	\$ 23,353,997
Local sales and use taxes	5,891,941	5,707,813	5,492,934	5,568,978	5,908,920	5,711,940	5,634,585	5,601,846	5,397,710	4,996,579
Business license tax	4,751,638	4,564,531	4,421,129	4,827,348	4,714,965	4,258,059	3,866,585	4,032,843	3,647,786	3,496,933
Meals tax	3,242,532	2,551,880	2,429,239	2,448,064	2,546,104	2,397,412	2,351,010	2,190,099	2,091,998	2,055,706
Utility taxes	1,124,383	1,123,400	1,105,818	1,123,616	1,156,775	1,228,975	1,372,250	1,339,238	1,122,167	1,141,696
Other taxes	2,604,603	2,805,271	2,684,054	2,856,119	2,362,788	2,700,657	2,625,066	2,486,633	2,484,614	2,233,301
Intergovernmental revenue not restricted	3,747,854	3,747,722	3,735,738	3,860,269	4,030,210	3,878,955	3,523,634	3,597,191	3,213,462	3,243,932
Unrestricted investment earnings	127,210	129,640	132,522	213,671	568,689	789,526	556,039	501,808	394,977	319,062
Gain on sale of property	-	-	-	24,624	5,715	-	402,089	571,311	-	-
Other	411,355	603,696	324,136	375,139	812,702	279,223	218,274	266,019	285,750	302,877
Transfers	1,656,490	(3,338,110)	575,667	1,626,999	1,552,276	495,995	975,685	(70,821)	236,756	226,527
Total governmental activities	<u>56,038,286</u>	<u>49,964,755</u>	<u>52,378,606</u>	<u>54,260,592</u>	<u>53,741,170</u>	<u>49,347,302</u>	<u>48,687,159</u>	<u>45,578,412</u>	<u>43,743,805</u>	<u>41,370,610</u>
<i>Business-type activities:</i>										
Unrestricted investment earnings	4,121	8,049	23,297	179,714	706,658	928,710	271,303	311,154	110,832	369,743
Gain on sale of property	-	-	-	205,932	-	6,967	-	-	-	-
Other	-	-	346,520	21,924	130,909	20,149	-	-	-	-
Transfers	(1,656,490)	3,338,110	(575,667)	(1,626,999)	(1,552,276)	(495,995)	(975,685)	70,821	(236,756)	(226,527)
Total business-type activities	<u>(1,652,369)</u>	<u>3,346,159</u>	<u>(205,850)</u>	<u>(1,219,429)</u>	<u>(714,709)</u>	<u>459,831</u>	<u>(704,382)</u>	<u>381,975</u>	<u>(125,924)</u>	<u>143,216</u>
Total primary government	<u>\$ 54,385,917</u>	<u>\$ 53,310,914</u>	<u>\$ 52,172,756</u>	<u>\$ 53,041,163</u>	<u>\$ 53,026,461</u>	<u>\$ 49,807,133</u>	<u>\$ 47,982,777</u>	<u>\$ 45,960,387</u>	<u>\$ 43,617,881</u>	<u>\$ 41,513,826</u>
Changes in Net Assets										
Total governmental activities	\$ 548,935	\$ (3,618,547)	\$ 1,643,048	\$ 377,072	\$ 2,143,851	\$ 1,118,364	\$ 6,387,540	\$ 1,583,716	\$ (9,583,848)	\$ 507,564
Total business-type activities	(2,339,286)	1,440,121	(496,690)	(951,470)	2,670,056	3,637,124	(620,886)	1,965,576	4,699,996	2,131,635
Total primary government	<u>\$ (1,790,351)</u>	<u>\$ (2,178,426)</u>	<u>\$ 1,146,358</u>	<u>\$ (574,398)</u>	<u>\$ 4,813,907</u>	<u>\$ 4,755,488</u>	<u>\$ 5,766,654</u>	<u>\$ 3,549,292</u>	<u>\$ (4,883,852)</u>	<u>\$ 2,639,199</u>

Notes:

Source: City of Salem Finance Department

(1) Electric expenses and Water and Sewage expenses of business-type activities were restated.

(2) Education expenses of governmental activities includes \$14,000,000 of bond funds transferred to the School Division to fund capital projects.

**TABLE 3
UNAUDITED**

**CITY OF SALEM, VIRGINIA
FUND BALANCES, GOVERNMENTAL FUNDS
LAST TEN FISCAL YEARS**

	2010	2009	2008	2007	2006	2005	2004	2003
Pre-GASB 54 implementation:								
General Fund								
Reserved	\$ 1,038,347	\$ 916,227	\$ 893,623	\$ 1,357,034	\$ 1,431,926	\$ 1,179,343	\$ 1,009,767	\$ 745,321
Unreserved	5,183,434	5,486,537	7,086,974	6,547,440	6,419,834	10,534,365	11,124,617	10,319,757
Total general fund	<u>\$ 6,221,781</u>	<u>\$ 6,402,764</u>	<u>\$ 7,980,597</u>	<u>\$ 7,904,474</u>	<u>\$ 7,851,760</u>	<u>\$ 11,713,708</u>	<u>\$ 12,134,384</u>	<u>\$ 11,065,078</u>
All Other Governmental Funds								
Reserved	\$ 784,005	\$ 2,130,298	\$ 3,388,893	\$ 1,083,915	\$ 1,251,705	\$ 3,777,959	\$ 7,434,079	\$ 2,920,546
<i>Unreserved, reported in:</i>								
Capital projects fund	(1,051,141)	(2,031,615)	(3,152,261)	(189,129)	(463,348)	(1,691,345)	2,914,998	(305,531)
Total all other governmental funds	<u>\$ (267,136)</u>	<u>\$ 98,683</u>	<u>\$ 236,632</u>	<u>\$ 894,786</u>	<u>\$ 788,357</u>	<u>\$ 2,086,614</u>	<u>\$ 10,349,077</u>	<u>\$ 2,615,015</u>
	2012	2011						
Post-GASB 54 implementation:								
General Fund								
Nonspendable	\$ 497,206	\$ 554,962						
Restricted	1,244,986	1,287,008						
Committed	519,817	-						
Assigned	1,256,103	1,588,768						
Unassigned	3,469,721	3,351,935						
Total general fund	<u>\$ 6,987,833</u>	<u>\$ 6,782,673</u>						
All Other Governmental Funds								
Restricted	\$ 15,244	\$ 129,686						
Committed	39,436	-						
Total all other governmental funds	<u>\$ 54,680</u>	<u>\$ 129,686</u>						

Note:

Source: City of Salem Finance Department
FY2011 was the first year the City implemented GASB 54 which revised fund balance classifications

**TABLE 4
UNAUDITED**

**CITY OF SALEM, VIRGINIA
CHANGES IN FUND BALANCE, GOVERNMENTAL FUNDS
LAST TEN FISCAL YEARS**

	2012	2011	2010	2009	2008	2007	2006	2005 (1)	2004	2003
Revenues										
Taxes	\$ 50,284,343	\$ 48,794,986	\$ 47,592,620	\$ 48,272,897	\$ 47,254,766	\$ 44,555,391	\$ 44,037,357	\$ 41,593,054	\$ 40,747,374	\$ 38,137,448
Permits, fees and licenses	202,342	218,094	243,035	228,687	303,958	293,004	294,314	286,150	308,511	257,796
Fines and forfeitures	160,816	164,161	159,179	171,056	159,489	159,363	150,860	162,207	197,297	170,922
Revenue from use of money and property	642,067	677,805	465,564	539,930	786,455	1,434,893	1,385,122	1,861,432	579,303	482,878
Charges for services	4,700,364	4,463,860	4,282,550	4,602,745	4,154,836	3,915,569	2,959,842	2,749,670	2,186,113	2,168,506
Other	104,701	284,324	172,872	195,505	152,478	47,673	32,544	43,796	53,590	385,733
Intergovernmental	11,462,504	12,562,674	12,525,033	12,526,047	10,859,986	10,336,870	8,720,129	8,765,664	7,764,376	8,562,593
Total revenues	67,557,137	67,165,904	65,440,853	66,536,867	63,671,968	60,742,763	57,580,168	55,461,973	51,836,564	50,165,876
Expenditures										
General government	5,792,852	4,900,770	5,232,405	6,380,771	4,891,569	4,694,442	4,994,542	4,386,061	4,005,851	3,555,873
Judicial administration	1,801,429	1,788,821	1,695,531	1,723,427	1,649,871	1,506,395	1,321,052	1,256,107	1,207,990	1,172,370
Public safety	15,353,250	14,792,022	14,358,932	14,371,192	14,397,297	13,358,739	12,707,985	11,670,171	10,740,352	10,103,738
Public works	11,988,380	11,656,775	11,101,013	12,113,469	12,156,138	11,434,040	9,400,116	9,777,021	8,879,090	8,514,725
Health and welfare	2,391,628	2,682,090	2,293,464	2,315,841	2,410,340	2,163,687	1,918,490	1,823,783	1,419,802	1,217,958
Education	18,471,653	18,420,000	18,420,000	18,420,000	17,995,000	17,095,000	16,266,005	15,618,081	15,340,564	14,747,635
Parks, recreation and cultural	4,403,170	4,203,452	4,204,705	4,716,767	4,464,456	4,354,144	4,316,920	4,037,410	3,696,621	3,336,510
Community development	981,483	879,709	618,217	1,148,291	469,835	639,535	815,991	513,272	842,963	1,290,922
Non-departmental	2,658,955	2,908,441	2,579,752	3,349,639	1,976,756	1,769,127	3,610,694	2,424,022	1,788,744	2,253,821
Capital projects	1,571,118	3,703,365	2,350,384	1,624,611	1,397,376	2,750,335	4,325,562	5,519,655	14,604,233	76,230
<i>Debt service:</i>										
Principal retirement	2,623,661	2,606,810	2,593,118	2,618,896	2,612,403	2,607,365	2,863,024	5,616,505	1,055,518	1,628,985
Interest	970,434	930,767	1,029,641	1,105,218	1,171,197	1,119,793	1,185,708	1,432,203	1,150,476	1,063,168
Bond Issuance Cost	31,900	117,689	-	-	-	-	-	-	-	-
Total expenditures	69,039,913	69,590,711	66,477,162	69,888,122	65,592,238	63,492,602	63,726,089	64,074,291	64,732,204	48,961,935
Excess (deficiency) of revenues over expenditures	(1,482,776)	(2,424,807)	(1,036,309)	(3,351,255)	(1,920,270)	(2,749,839)	(6,145,921)	(8,612,318)	(12,895,640)	1,203,941
Other Financing Sources (Uses)										
Proceeds from long-term debt	-	6,540,000	-	-	-	-	-	-	31,970,540	-
Proceeds from sale of refunding bonds	9,485,000	3,339,279	-	-	-	-	-	-	-	-
Payment to refunded bond escrow agent	(9,513,728)	(3,430,000)	-	-	-	-	-	-	(10,508,287)	-
Premium on sale of bonds	-	248,757	-	-	-	-	-	-	-	-
Discount on sale of bonds	-	(48,989)	-	-	-	-	-	-	-	-
Transfers in	6,458,723	5,683,661	4,985,609	6,043,796	6,474,312	7,536,323	8,235,360	5,417,206	4,252,823	3,993,355
Transfers out	(4,817,065)	(8,950,187)	(4,496,102)	(4,408,322)	(5,136,073)	(4,627,341)	(7,249,644)	(5,488,027)	(4,016,067)	(3,766,828)
Total other financing sources (uses)	1,612,930	3,382,521	489,507	1,635,474	1,338,239	2,908,982	985,716	(70,821)	21,699,009	226,527
Net change in fund balances	\$ 130,154	\$ 957,714	\$ (546,802)	\$ (1,715,781)	\$ (582,031)	\$ 159,143	\$ (5,160,205)	\$ (8,683,139)	\$ 8,803,369	\$ 1,430,468
Debt service as a percentage of noncapital expenditures	5.37%	5.39%	5.76%	5.73%	6.04%	6.26%	7.06%	12.35%	4.60%	5.68%

Notes:

Source: City of Salem Finance Department

(1) Principal retirement includes one-time balloon payment of \$2,715,000.

TABLE 5
UNAUDITED

CITY OF SALEM
ASSESSED VALUE AND ACTUAL VALUE OF TAXABLE PROPERTY
LAST TEN FISCAL YEARS

Fiscal Year Ended June 30,	Real Estate	Personal Property	Machinery and Tools	Public Service Corporation	Mobile Homes	Total Taxable Assessed Value	Total Direct Tax Rate
2012	\$ 1,977,986,400	\$ 267,877,285	\$ 90,287,324	\$ 37,468,284	\$ 1,668,743	\$ 2,375,288,036	1.48
2011	1,973,655,843	265,450,351	80,706,659	37,993,502	1,460,966	2,359,267,321	1.48
2010	1,940,941,700	262,153,501	79,120,695	36,874,789	1,543,032	2,320,633,717	1.48
2009	1,912,957,600	263,305,279	80,517,625	36,468,242	1,655,642	2,294,904,388	1.48
2008	1,805,483,900	263,662,393	82,535,751	36,451,099	1,780,273	2,189,913,416	1.50
2007	1,601,239,600	254,765,656	86,685,532	34,992,259	1,632,022	1,979,315,069	1.52
2006	1,572,732,200	262,141,563	86,409,864	33,586,047	1,855,348	1,956,725,022	1.54
2005	1,414,891,600	253,619,878	82,714,938	35,032,203	2,186,076	1,788,444,695	1.55
2004	1,386,790,100	250,218,290	88,317,031	35,658,160	2,092,797	1,763,076,378	1.56
2003	1,276,162,600	262,415,563	75,075,156	36,825,471	2,257,457	1,652,736,247	1.60

Note:

Source: City of Salem Finance Department

Tax rates are per \$100 of assessed value. Real estate tax rate = \$1.18; Personal property tax rate = \$3.20.

TABLE 6
UNAUDITED

CITY OF SALEM, VIRGINIA
PROPERTY TAX LEVIES AND COLLECTIONS
LAST TEN FISCAL YEARS

Fiscal Year	Taxes Levied for the Fiscal Year	Collected within the Fiscal Year of the Levy		Collections in Subsequent Year	Total Collections to Date	
		Amount	Percentage of Levy		Amount	Percentage of Levy
		(1)				
2012	\$ 32,680,202	\$ 31,137,614	95.28%	\$ -	\$ 31,137,614	95.28%
2011	32,106,299	30,836,143	96.04%	600,761	31,436,904	97.92%
2010	31,800,432	30,440,194	95.72%	1,017,621	31,457,815	98.92%
2009	31,444,294	30,288,062	96.32%	1,013,903	31,301,965	99.55%
2008	30,065,979	28,917,803	96.18%	1,076,013	29,993,816	99.76%
2007	27,719,526	26,652,953	96.15%	1,023,750	27,676,703	99.85%
2006	27,433,382	26,209,290	95.54%	1,204,762	27,414,052	99.93%
2005	25,004,098	24,282,081	97.11%	705,348	24,987,429	99.93%
2004	24,913,869	24,017,690	96.40%	883,500	24,901,190	99.95%
2003	23,424,897	22,753,153	97.13%	659,335	23,412,488	99.95%

Note:

Source: City of Salem Finance Department

(1) Includes state share of personal property taxes.

**TABLE 7
UNAUDITED**

**CITY OF SALEM, VIRGINIA
PRINCIPAL REAL ESTATE PROPERTY TAXPAYERS
CURRENT YEAR AND NINE YEARS AGO**

Taxpayer	2012			2003		
	Taxable Assessed Value	Rank	Percentage of Total City Taxable Assessed Value	Taxable Assessed Value	Rank	Percentage of Total City Taxable Assessed Value
Lewis-Gale Hospital HCA	\$ 36,118,600	1	1.82%	\$ 22,377,700	2	1.79%
HRT of Roanoke, Inc.	22,095,300	2	1.11%	29,762,900	1	2.38%
Yokohama Industries	16,142,400	3	0.81%	16,264,300	3	1.30%
BET/Lowe's	12,462,800	4	0.63%			
General Electric	10,665,400	5	0.54%	10,889,100	4	0.87%
U.S. Food Service, Inc.	10,524,500	6	0.53%	6,524,000	8	0.52%
Chateau Riviera Apartments	9,190,500	7	0.46%	7,565,700	7	0.61%
Spartan Square	8,737,700	8	0.44%	5,672,500	10	0.45%
Salem Terrace	8,690,500	9	0.44%			
Carter Machinery/Carthy Corporation	7,586,000	10	0.38%			
Home Shopping Network Virginia Division				8,636,500	5	0.69%
Rowe Furniture/Salem Frame				7,808,600	6	0.63%
Wal-Mart, Inc.				5,912,200	9	0.47%

Note:

Source: City of Salem Real Estate Valuation Department

**TABLE 8
UNAUDITED**

**CITY OF SALEM, VIRGINIA
PRINCIPAL ELECTRIC CUSTOMERS
CURRENT YEAR AND NINE YEARS AGO**

Customer	2012			2003		
	Services Billed	Rank	Percentage of Total Services Billed	Services Billed	Rank	Percentage of Total Services Billed
Lewis-Gale Hospital HCA	\$1,804,836	1	4.94%	\$734,147	1	3.83%
Roanoke College	1,299,560	2	3.56%	516,665	2	2.70%
Graham White	721,132	3	1.97%	399,340	5	2.08%
U.S. Food Service, Inc.	713,443	4	1.95%	414,707	4	2.16%
Rowe Furniture/Salem Frame	679,869	5	1.86%	376,829	6	1.97%
Wal-Mart, Inc.	571,570	6	1.56%	208,935	10	1.09%
Kroger	548,894	7	1.50%	297,911	7	1.55%
Sewell Products	486,153	8	1.33%			
Carthy Corporation/Carter Machinery	439,619	9	1.20%	235,246	8	1.23%
Old Virginia Brick Co	338,066	10	0.93%	227,774	9	1.19%
Valleydale Foods				431,296	3	2.25%

Note:

Source: City of Salem Finance Department

TABLE 9
UNAUDITED

CITY OF SALEM, VIRGINIA
RATIOS OF GENERAL BONDED DEBT OUTSTANDING
LAST TEN FISCAL YEARS

Fiscal Year	Governmental Activities				Business-Type Activities	Total Primary Government
	General Obligation Bonds	Other Long-term Debt	Amounts Restricted to Repaying Principal	Total	General Obligation Bonds	
	(1)	(1)				
2012	\$ 26,095,236	\$ -	\$ -	\$ 26,095,236	\$ 53,877,529	\$ 79,972,765
2011	28,033,897	-	-	28,033,897	55,710,739	83,744,636
2010	24,066,428	125,000	-	24,191,428	56,518,876	80,710,304
2009	26,534,546	250,000	-	26,784,546	59,416,149	86,200,695
2008	29,028,442	375,000	-	29,403,442	62,254,430	91,657,872
2007	31,515,845	500,000	-	32,015,845	64,951,116	96,966,961
2006	31,498,210	625,000	-	32,123,210	66,855,732	98,978,942
2005	34,236,234	750,000	-	34,986,234	40,495,352	75,481,586
2004	39,727,739	875,000	(2,988,308)	37,614,431	39,779,649	77,394,080
2003	18,362,717	1,000,000	(2,673,586)	16,689,131	42,047,283	58,736,414

Fiscal Year	Total Taxable Assessed Value	Percentage of Estimated Actual Value of Taxable Property	Population	Bonded Debt Per Capita	Per Capita Personal Income	Percentage of Bonded Debt Per Capita to Per Capita Personal Income
	(2)		(3)		(3)	
2012	\$ 2,375,288,036	3.37%	25,145	\$ 3,180	\$ 39,866	8.00%
2011	2,359,267,321	3.55%	24,970	3,354	39,866	8.00%
2010	2,320,633,717	3.48%	24,860	3,247	39,866	8.00%
2009	2,294,904,388	3.76%	24,684	3,492	39,525	9.00%
2008	2,189,913,416	4.19%	24,673	3,715	40,760	9.00%
2007	1,979,315,069	4.90%	24,482	3,961	39,479	10.00%
2006	1,956,725,022	5.06%	24,508	4,039	38,194	11.00%
2005	1,788,444,695	4.22%	24,310	3,105	36,611	8.00%
2004	1,763,076,378	4.39%	24,096	3,212	35,882	9.00%
2003	1,652,736,247	3.55%	24,465	2,401	34,111	7.00%

Notes:

Source: City of Salem Finance Department

Details regarding the City's outstanding debt can be found in the notes to the financial statements.

The City is independent from any county, town, or other political subdivisions of the Commonwealth of Virginia. There is no overlapping general obligation debt or taxing powers.

(1) Outstanding debt for School Division is included with Governmental Activities.

(2) See Table 5 for actual value of taxable property.

(3) See Table 11 for population and per capita personal income.

TABLE 10
UNAUDITED

CITY OF SALEM, VIRGINIA
LEGAL DEBT MARGIN INFORMATION
LAST TEN FISCAL YEARS

Fiscal Year	Assessed Value of Real Property	Debt Limit 10% of Assessed Value	Amount of Debt Applicable to Limit					Legal Debt Margin
			Total General Obligation Bonds	Total Other Long-term Debt	Enterprise Bonds	Amounts Restricted to Repaying Principal	Net Debt Applicable to Limit	
	(1)				(2)		(3)	
2012	\$ 2,015,454,684	\$ 201,545,468	\$ 79,972,765	\$ -	\$ (53,877,529)	\$ -	\$ 26,095,236	1.29%
2011	2,011,649,345	201,164,935	83,744,636	-	(55,710,739)	-	28,033,897	1.39%
2010	1,977,816,489	197,781,649	80,585,304	125,000	(56,518,876)	-	24,191,428	1.22%
2009	1,949,425,842	194,942,584	85,950,695	250,000	(59,416,149)	-	26,784,546	1.37%
2008	1,841,934,999	184,193,500	91,282,872	375,000	(62,254,430)	-	29,403,442	1.60%
2007	1,636,231,859	163,623,186	96,466,961	500,000	(64,951,116)	-	32,015,845	1.96%
2006	1,606,318,247	160,631,825	98,353,942	625,000	(66,855,732)	-	32,123,210	2.00%
2005	1,449,923,803	144,992,380	74,731,586	750,000	(40,495,352)	-	34,986,234	2.41%
2004	1,422,448,260	142,244,826	79,507,388	875,000	(39,779,649)	(2,988,308)	37,614,431	2.64%
2003	1,312,988,071	131,298,807	60,410,000	1,000,000	(42,047,283)	(2,673,586)	16,689,131	1.27%

Notes:

Source: City of Salem Finance Department

(1) Includes real estate and public service corporation assessments from table 5.

(2) The Enterprise Fund bonds are backed by the full faith and credit of the City but are expected to be paid from the revenue and receipts of the Enterprise Funds.

(3) School debt is included in the amount of debt applicable to limit.

**TABLE 11
UNAUDITED**

**CITY OF SALEM, VIRGINIA
DEMOGRAPHIC STATISTICS
LAST TEN FISCAL YEARS**

Fiscal Year Ended	Population	Total Personal Income (In Thousands)	Per Capita Personal Income	Public School Enrollment	Unemployment Rate
(1)	(2)	(3)	(3)	(4)	(5)
2012	25,145	\$ 4,672,291	\$ 39,866	3,867	6.5%
2011	24,970	4,672,291	39,866	3,892	6.1%
2010	24,860	4,672,291	39,866	3,907	7.2%
2009	24,684	4,620,761	39,525	3,905	6.3%
2008	24,673	4,743,543	40,760	3,911	3.6%
2007	24,482	4,563,905	39,479	3,966	3.0%
2006	24,508	4,392,229	38,194	3,902	2.9%
2005	24,310	4,157,343	36,611	3,882	2.5%
2004	24,096	4,028,616	35,882	3,888	2.7%
2003	24,465	3,813,705	34,111	3,910	3.8%

Notes:

(1) Population, public school enrollment and unemployment rate figures are based on fiscal years ending June 30, per capita personal income figures are as of April 2012.

(2) Population is based on Intercensal estimates of the resident population for counties of Virginia: April 1, 2000 to July 1, 2010. US Census Bureau, Population Division. Population for 2011 and 2012 were obtained from Weldon Cooper Center, University of Virginia.

(3) Bureau of Economic Analysis (BEA) . Total personal income reported is for Roanoke County and the City of Salem. No data is available for the City of Salem only. Per capital personal income was computed using Census Bureau midyear population estimates. Estimates for 2000-2010 reflect county population estimates available as of April 2012.

(4) Supervisor of Business Services, School Division

(5) Virginia Employment Commission

TABLE 12
UNAUDITED

CITY OF SALEM, VIRGINIA
PRINCIPAL EMPLOYERS
CURRENT YEAR AND NINE YEARS AGO

Employer	2012			2003		
	Employees	Rank	Percentage of Total City Employment (1)	Employees	Rank	Percentage of Total City Employment (1)
Veterans Administration Medical Center	1,950	1	8.71%	1,458	1	6.04%
Lewis-Gale Hospital HCA	1,445	2	6.46%	1,420	2	5.88%
Yokohama Industries	940	3	4.20%	1,222	3	5.06%
General Electric	804	4	3.59%	1,210	4	5.01%
Virginia Department of Transportation	782	5	3.49%			
City of Salem Schools	587	6	2.62%	538	7	2.23%
City of Salem	508	7	2.27%	510	8	2.11%
Roanoke College	476	8	2.13%	455	9	1.89%
U.S. Food Service, Inc.	443	9	1.98%	352	10	1.46%
Carter Machinery/Carthy Corporation	368	10	1.64%			
Lewis-Gale Clinic				1,167	5	4.84%
Home Shopping Network				850	6	3.52%

Notes:

Source: City of Salem Planning and Economic Development Department, Virginia Employment Commission

(1) Calculated using data provided by Virginia Employment Commission

TABLE 13
UNAUDITED

CITY OF SALEM, VIRGINIA
FULL-TIME EQUIVALENT CITY GOVERNMENT EMPLOYEES BY FUNCTION
LAST TEN FISCAL YEARS

Function	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003
General government	71	74	72	74	76	74	72	72	71	70
Judicial administration	21	20	20	20	20	20	19	19	19	19
Public safety	160	161	162	167	165	164	162	159	154	154
Public works	100	105	110	112	113	111	115	115	114	115
Parks, recreation and cultural	32	32	33	33	26	25	25	20	22	22
Community development	3	3	3	3	3	3	4	2	2	2
Electric	26	28	29	29	29	29	28	29	29	28
Water and sewage	51	52	53	58	58	59	58	60	63	63
Civic Center	18	18	17	18	20	19	19	20	20	19
Catering and concessions	4	4	4	5	5	5	5	5	5	5
Total	<u>486</u>	<u>497</u>	<u>503</u>	<u>519</u>	<u>515</u>	<u>509</u>	<u>507</u>	<u>501</u>	<u>499</u>	<u>497</u>

Notes:

Source: City of Salem Finance Department

TABLE 14
UNAUDITED

CITY OF SALEM, VIRGINIA
OPERATING INDICATORS BY FUNCTION
LAST TEN FISCAL YEARS

Function	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003
General government										
<i>Finance</i>										
Accounts payable checks issued	11,002	12,260	13,595	12,104	13,991	14,617	15,638	16,307	16,836	16,183
<i>Human resources</i>										
Positions filled (full-time and temporary)	146	143	129	257	244	201	246	233	219	246
<i>Registrar</i>										
Number of registered voters	16,678	16,436	16,309	16,258	15,897	15,524	14,995	15,652	15,146	14,442
<i>Fleet</i>										
Pieces of equipment maintained	573	565	551	560	600	558	527	517	510	498
Judicial administration										
<i>Sheriff</i>										
Inmates housed	2,668	2,587	2,343	1,494	1,294	1,296	1,125	1,067	1,497	1,708
Inmate transports	1,069	1,276	1,879	1,594	1,545	1,427	1,391	1,315	1,471	1,292
Courts worked	648	691	676	695	624	639	611	593	588	580
Public safety										
<i>Police</i>										
Calls for service	36,549	33,903	34,342	35,159	34,526	33,776	30,163	30,442	31,566	30,396
Accidents	919	1,063	975	1,024	1,300	1,329	1,221	1,263	1,258	1,221
DUI Arrests	62	95	129	122	146	176	159	124	196	254
<i>Fire</i>										
Emergency responses - fire	3,241	3,661	3,270	3,441	3,083	2,715	3,006	2,537	2,182	2,106
Emergency responses - medic units	3,358	3,632	3,335	3,596	3,085	2,982	3,289	2,934	2,281	2,007
Hazardous conditions responses	105	137	134	161	182	146	82	101	72	79
<i>Building inspections</i>										
Residential construction permits	122	123	130	148	169	336	309	319	272	599
Commercial construction permits	116	124	63	71	103	93	92	139	163	53
Public works										
<i>Refuse collection</i>										
Refuse collected (tons per year)	81,427	81,485	83,607	88,365	77,027	90,405	81,379	84,270	92,665	90,762
Tons recycled	2,844	1,764	3,883	4,841	4,623	4,724	2,154	3,594	3,550	3,559
<i>Other public works</i>										
Tons of asphalt used in resurfacing	7,507	5,821	3,616	5,185	6,958	14,510	9,111	11,966	8,005	7,088
Square yards of milling completed	143,962	99,960	39,959	80,155	68,091	84,386	58,605	25,480	17,973	15,990
Tons of salt used	183	817	1,389	176	170	277	901	705	1,350	1,574
Leaves collected (loads)	369	494	507	448	323	421	422	604	375	400
Parks, recreation and cultural										
<i>Parks and recreation</i>										
Tournaments hosted	58	49	53	50	54	57	59	54	51	54
Special events held	24	24	25	24	24	25	21	18	18	18
Youth sports teams	205	225	210	195	252	186	184	219	219	214
Adult sports teams	37	44	49	48	59	48	40	40	40	42
<i>Library</i>										
Circulation	295,911	285,337	290,309	276,578	264,184	241,816	233,852	232,892	224,712	230,848
Children's program attendance	4,926	6,891	7,129	8,792	7,647	4,591	3,580	4,164	2,622	3,324
Patron visits to the library	226,696	232,559	245,807	239,745	233,524	234,379	228,560	217,477	220,571	214,911
New patrons	1,315	1,288	1,417	1,648	1,694	1,694	1,510	1,537	1,492	1,553
Internet sessions	51,033	52,397	58,517	50,711	62,650	55,689	32,650	25,834	27,973	25,845
Electric										
Number of customer accounts	13,202	13,163	13,131	13,175	13,130	13,032	12,968	12,856	12,883	12,678
Water										
Number of customer accounts	9,365	9,341	9,301	9,304	9,256	9,170	9,107	9,055	9,035	8,916
Million gallons sold to customers	955	1,004	977	1,003	1,067	1,043	1,090	1,097	1,098	1,066
Sewage										
Number of customer accounts	8,803	8,764	8,717	8,706	8,664	8,561	8,513	8,461	8,446	8,339
Waste/water treated (million gallons/day)	7.0	6.5	8.3	6.2	5.7	8.1	6.8	9.2	7.3	7.8
Civic Center										
Concerts	13	13	9	9	9	13	6	8	12	16
Meetings	792	936	1,156	1,216	1,295	1,081	1,209	1,282	1,259	1,282
Tickets sold	87,006	102,678	103,891	112,997	99,581	147,491	163,972	129,248	150,801	162,263
Arena utilization days	173	178	179	202	219	201	175	203	180	175

Notes:

Source: Various City of Salem Departments

TABLE 15
UNAUDITED

CITY OF SALEM, VIRGINIA
CAPITAL ASSET STATISTICS BY FUNCTION
LAST TEN FISCAL YEARS

Function	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003
Public safety										
Police station	1	1	1	1	1	1	1	1	1	1
Law enforcement vehicles	47	47	46	49	50	48	45	42	56	52
Fire stations	3	3	3	3	3	3	3	3	3	3
Fire trucks	6	6	6	6	7	6	5	5	5	5
Ambulances	4	5	5	5	5	5	4	3	3	3
Public works										
Primary streets (lane miles)	68	68	68	68	68	68	65	65	64	64
Secondary streets (lane miles)	272	272	272	272	272	270	225	225	223	223
Alleys (lane miles)	12	12	12	12	12	12	11	11	11	11
Garbage trucks	12	12	12	12	13	13	10	11	12	12
Parks, recreation and cultural										
Community center/senior center	1	1	1	1	1	1	3	3	3	3
Parks/athletic fields	15	15	15	15	15	15	15	15	15	14
Acres of parks maintained	495	495	495	495	495	495	495	495	495	495
Library	1	1	1	1	1	1	1	1	1	1
Golf course	1	1	1	1	1	1	1	1	1	1
Dog park	1	0	0	0	0	0	0	0	0	0
Electric										
Substations	11	11	11	11	11	11	7	7	7	7
Overhead distribution lines (miles)	172	172	172	171	158	158	159	161	161	183
Underground distribution lines (miles)	38	38	38	38	33	33	33	31	31	30
Transmission lines (miles)	17	17	17	17	17	17	23	23	23	23
Water and sewage										
Water treatment plant	1	1	1	1	1	1	1	2	2	2
Water distribution lines (miles)	175	182	182	181	182	181	181	180	155	154
Sanitary sewer lines (miles)	177	177	177	171	176	176	174	174	144	143

Notes:

Source: City of Salem Finance Department

COMPLIANCE SECTION



The compliance section of the City of Salem, Virginia's Comprehensive Annual Financial Report presents a schedule of expenditures of federal awards. Also included are reports from the independent auditors.

CITY OF SALEM, VIRGINIA
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
JUNE 30, 2012

<u>Federal Grantor</u> <i>Pass-through Grantor: Commonwealth of Virginia</i> Program Title	Federal CFDA Number	Federal Expenditures
<u>Department of Agriculture</u>		
<i>Department of Agriculture and Nutrition Service</i>		
Supplemental Nutrition Assistance Program	10.551	\$ 6,267
<i>Department of Agriculture and Consumer Services</i>		
Food Distribution – Commodities	10.555	117,328
<i>Department of Education</i>		
National School Breakfast Program	10.553	146,667
National School Lunch Program	10.555	509,611
<u>Department of Justice</u>		
<i>Direct Payments</i>		
Drug Enforcement Task Force	16.000	7,705
Bulletproof Vest Partnership Program	16.607	3,959
Byrne Justice Assistance Grant	16.738	24,300
<i>Department of Criminal Justice Services</i>		
Crime Victim Assistance	16.575	53,063
<u>Department of Transportation</u>		
<i>Direct Payments</i>		
Highway Planning and Construction	20.205	243,674
<i>Division of Motor Vehicles</i>		
Alcohol Traffic Safety and Drunk Driving Prevention	20.601	30,034
<u>Department of Education</u>		
<i>Department of Education</i>		
Education Consolidation Improvement Act of 1981:		
Title I: Grants to Local Educational Agencies	84.010	379,300
Title I: Distinguished Schools	84.010	18,066
Title I: Perkins Career and Technical Education	84.048	46,573
Title II: Part A, Improving Teacher Quality	84.367	136,570
Elementary and Secondary Education Act (ESEA):		
Special Education – Grants to States	84.027	738,562
Special Education – Preschool Grants	84.173	11,294
Vocational Education:		
Adult Education	84.002	80,376
Special Projects:		
Safe and Drug Free Schools and Communities	84.186	60
Carol White PEP Grant	84.215	192,118
English Language Acquisition	84.365	8,772
American Recovery and Reinvestment Act of 2009 (ARRA):		
ARRA Title I: Grants to Local Educational Agencies	84.389	7,903
ARRA Special Education Grants to States	84.391	41,309
ARRA Special Education - Preschool Grants	84.392	10,714
ARRA Education Jobs Fund	84.410	783,102
<u>Department of Homeland Security</u>		
<i>Department of Emergency Management</i>		
State Homeland Security Grant	97.073	27,385
Emergency Management Performance Grant	97.042	1,416
Flood Mitigation Assistance	97.029	77,023
Total Expenditures of Federal Awards		\$ 3,703,151

Note 1: Basis of Accounting

This schedule was prepared on the modified accrual basis of accounting.

Note 2: Nonmonetary Assistance

Nonmonetary assistance is reported in the Schedule of Expenditures of Federal Awards at the fair market value of the food commodities disbursed. At June 30, 2012, the Component Unit – School Division had food commodities in inventory of \$27,780.

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL
STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

Honorable Members of City Council
City of Salem, Virginia
Salem, Virginia

We have audited the financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Salem, Virginia (“City”), as of and for the year ended June 30, 2012, which collectively comprise the City’s basic financial statements and have issued our report thereon dated November 20, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and *Specifications for Audits of Counties, Cities, and Towns*, issued by the Auditor of Public Accounts of the Commonwealth of Virginia.

Internal Control Over Financial Reporting

Management of the City is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the City’s internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City’s internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City’s internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity’s financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. **We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.**

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, including certain provisions of the compliance matters described in the Summary of Compliance Matters, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. **The results of our tests disclosed an instance of noncompliance or other matter that is required to be reported under *Government Auditing Standards*, and which is described in the accompanying schedule of findings and questioned costs as Item 12-1.**

We noted certain matters that we reported to management of the City in a separate letter dated November 20, 2012.

The City's response to the finding identified in our audit is described in the accompanying schedule of findings and questioned costs. We did not audit the City's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, others within the City, state and federal awarding agencies and pass-through entities, and City Council, and is not intended to be and should not be used by anyone other than these specified parties.

Brown, Edwards & Company, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

Roanoke, Virginia
November 20, 2012

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS THAT
COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND
ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH
*OMB CIRCULAR A-133***

Honorable Members of City Council
City of Salem, Virginia
Salem, Virginia

Compliance

We have audited the compliance of the City of Salem, Virginia ("City"), with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the City's major federal programs for the year ended June 30, 2012. The City's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the City's management. Our responsibility is to express an opinion on the City's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and *OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and *OMB Circular A-133* require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City's compliance with those requirements.

In our opinion, the City complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012.

Internal Control over Compliance

Management of the City is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the City's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. **We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.**

This report is intended solely for the information and use of management, others within the City, state and federal awarding agencies and pass-through entities, and the City Council and is not intended to be and should not be used by anyone other than those specified parties.

Brown, Edwards & Company, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

Roanoke, Virginia
November 20, 2012

CITY OF SALEM, VIRGINIA
SUMMARY OF COMPLIANCE MATTERS
June 30, 2012

As more fully described in the Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*, we performed tests of the City's compliance with certain provisions of the laws, regulations, contracts, and grants shown below.

STATE COMPLIANCE MATTERS

Code of Virginia:

Budget and Appropriation Laws
Cash and Investment Laws
Conflicts of Interest Act
Debt Provisions
Local Retirement Systems
Procurement Laws
Uniform Disposition of Unclaimed Property Act
Sheriff Internal Controls
Comprehensive Services Act

State Agency Requirements:

Education

FEDERAL COMPLIANCE MATTERS

U.S. Office of Management and Budget (OMB A-133) Compliance Supplement:

Provisions and conditions of agreements related to federal programs selected for testing.

CITY OF SALEM, VIRGINIA

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Year Ended June 30, 2012**

A. SUMMARY OF AUDITOR'S RESULTS

1. The auditor's report expresses an **unqualified** opinion on the basic financial statements.
2. **No significant deficiencies** related to the audit of the financial statements are reported in the Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*.
3. **No instances of noncompliance material** to the basic financial statements were disclosed during the audit.
4. **No significant deficiencies** are disclosed in the Independent Auditor's Report on Compliance with Requirements That Could Have a Direct and Material Effect on Each Major Program and on Internal Control over Compliance in Accordance with *OMB Circular A-133*.
5. The auditor's report on compliance for the major federal award programs expresses an **unqualified opinion**.
6. The audit disclosed **no audit findings** relating to major programs.
7. The programs tested as major programs include:

<u>Name of Programs</u>	<u>CFDA#</u>
ARRA: Education Jobs Fund	84.410
Carol White PEP Grant	84.215

8. The threshold for distinguishing Types A and B programs was \$300,000.
9. The City was determined to be a **low-risk auditee**.

B. FINDINGS – FINANCIAL STATEMENT AUDIT

None

C. FINDINGS AND QUESTIONED COSTS – MAJOR FEDERAL AWARD PROGRAMS

None

CITY OF SALEM, VIRGINIA
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Year Ended June 30, 2012

D. FINDINGS AND QUESTIONED COSTS – COMMONWEALTH OF VIRGINIA

12-1: Disclosure Statements

Condition:

Four out of forty-five members of City appointed boards did not file their completed statements of economic interest by the required deadline.

Recommendation:

Management should ensure all economic interest forms are submitted by the state mandated deadline.

Management's Response:

The City concurs with the comment and has noted it for future reference.

**Department of Finance
City of Salem, Virginia**

Frank P. Turk

Director of Finance

Accounting/Accounts Payable/Purchasing

Vickie L. Akers	Accounting Assistant
Kathryn K. Fox, CPA	Senior Accountant
Yen T. Ha	Senior Accountant
Linda K. Harris	Buyer
Amy R. Morris, CPA	Senior Accountant
Mary Ann Penney, CPA	Senior Accountant
Tammy H. Todd, CPA	Accounting Supervisor
Karen M. Vaught	Accounting Technician
Kathryn B. Williams	Accounting Assistant

Administrative

Alyson R. Chaisson	Finance Administrative Secretary/ Accounting Technician
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Payroll

Mechelle Bennett-Stump	Payroll Technician
Patricia K. Poage	Payroll Supervisor