



Mary Taylor, CPA  
Auditor of State



CITY OF HILLSBORO  
HIGHLAND COUNTY

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**CITY OF HILLSBORO  
HIGHLAND COUNTY**

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# Mary Taylor, CPA

## Auditor of State

### INDEPENDENT ACCOUNTANTS' REPORT

City of Hillsboro  
Highland County  
130 North High Street  
Hillsboro, Ohio 43160

To the Members of Council:

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hillsboro, Highland County, Ohio (the City), as of and for the year ended December 31, 2006, 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 and the standards applicable to financial audits contained in the Comptroller General of the United States' *Government Auditing Standards*. Those standards require that we plan and perform the audit to reasonably assure 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 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, each major fund, and the aggregate remaining fund information of the City of Hillsboro, Highland County, Ohio, as of December 31, 2006, and the respective changes in financial position and where applicable, cash flows, thereof and the budgetary comparison 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, 2007, on our consideration of the City's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. While we did not opine on the internal control over financial reporting or on compliance, that report describes the scope of our testing of internal control over financial reporting and compliance and the results of that testing. That report is an integral part of an audit performed in accordance with *Government Auditing Standards*. You should read it in conjunction with this report in assessing the results of our audit.

Management's Discussion and Analysis is not a required part of the basic financial statements but is supplementary information accounting principles generally accepted in the United States of America requires. We have applied certain limited procedures, consisting principally of inquiries of management regarding the methods of measuring and presenting the required supplementary information. However, we did not audit the information and express no opinion on it.

We conducted our audit to opine on the financial statements that collectively comprise the City's basic financial statements. The federal awards expenditure schedule is 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 basic financial statements. We subjected the federal awards expenditure schedule to the auditing procedures applied in the audit of the basic financial statements. In our opinion, this information is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

A handwritten signature in black ink that reads "Mary Taylor". The signature is written in a cursive, flowing style.

**Mary Taylor, CPA**  
Auditor of State

November 20, 2007

**City of Hillsboro, Ohio**  
Management's Discussion and Analysis  
For the Year Ended December 31, 2006  
(Unaudited)

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The discussion and analysis of the City of Hillsboro's financial performance provides an overall review of the City's financial activities for the year ended December 31, 2006. The intent of this discussion and analysis is to look at the City's financial performance as a whole; readers should also review the basic financial statements and the notes to the basic financial statements to enhance their understanding of the City's financial performance.

### **Financial Highlights**

Key financial highlights for 2006 are as follows:

- In total, net assets increased \$1,795,563. Net assets of governmental activities increased \$606,521. Net assets of business-type activities increased \$1,189,042.
- Governmental Activities general revenues accounted for \$4,653,830 in revenue or 72 percent of all revenues. Program specific revenues in the form of charges for services and sales, grants and contributions accounted for \$1,771,431 or 28 percent of total revenues of \$6,425,261. Business-type activities general revenues accounted for \$115,183 in revenue or 3 percent of all revenues. Program specific revenues accounted for \$3,630,406 or 97 percent of total revenues of \$3,745,589.
- The City had \$5,818,740 in expenses related to governmental activities; \$1,771,431 of these expenses was offset by program specific charges for services and sales, grants and contributions. The City had \$2,556,547 in expenses related to business-type activities; the entire amount was offset by program specific charges for services, grants and contributions.

### **Using the Annual Financial Report**

This annual report consists of a series of financial statements and notes to the financial statements. These statements are organized so the reader can understand the City of Hillsboro as a financial whole or as an entire operating entity. The statements then proceed to provide a detailed look at specific financial conditions.

The statement of net assets and statement of activities provide information about the activities of the whole City, presenting both an aggregate view of the City's finances and a longer-term view of those assets. Fund financial statements provide the next level of detail. For governmental funds, these statements tell how services were financed in the short-term as well as what monies remain for future spending. The fund financial statements also look at the City's most significant funds with all other non-major funds presented in total in a single column.

### **Reporting the City as a Whole**

#### Statement of Net Assets and Statement of Activities

While this report contains information about the funds used by the City to provide services to our citizens, the view of the City as a whole looks at all financial transactions and asks the question, "How did we do financially during 2006?" The statement of net assets and the statement of activities answer this question. These statements include all assets and liabilities using the accrual basis of accounting similar to the accounting system used by private sector companies. This basis of accounting takes into account all of the current year's revenues and expenses regardless of when the cash is received or paid.

These two statements report the City's net assets and the changes in those assets. The change in assets is important because it identifies whether the financial position of the City has improved or diminished for the City as a whole. However, in evaluating the overall position of the City, non financial information such as changes in the City's tax base and the condition of the City's capital assets will also need to be evaluated.

**City of Hillsboro, Ohio**  
Management's Discussion and Analysis  
For the Year Ended December 31, 2006  
(Unaudited)

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In the statement of net assets and the statement of activities, the City is divided into two types of activities:

- **Governmental Activities** - Most of the City's services are reported as governmental activities including police, fire, administration, and all departments with the exception of business-type activities (sanitation, wastewater treatment, storm water utility and water services).
- **Business-Type Activities** - These services have a charge based upon usage. The City charges fees to recoup the cost of the entire operation of the Water Plant and Wastewater Treatment Plant as well as all capital expenses associated with these facilities. The City also charges fees to recoup the cost of disposal of solid waste, leaf and brush removal and also a fee to provide for improvements to the City's storm water removal system. These fees are accounted for in the Sewer Fund.

### **Reporting the City's Most Significant Funds**

#### Fund Financial Statements

Fund financial statements provide detailed information about the City's major funds. Based on restrictions on the use of monies, the City has established many funds which account for the multitude of services provided to our residents; however, fund financial statements focus on the City's most significant funds. The City of Hillsboro's major funds are the General Fund and the Water and Sewer enterprise funds.

**Governmental Funds** - Most of the City's activities are reported in governmental funds, which focus on how monies flow into and out of those funds and the year-end balances available for spending in the future periods. These funds are reported using the modified accrual basis of accounting, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund statements provide a detailed short-term view of the City's general governmental operations and the basic services provided. Governmental fund information helps determine whether there are more or less financial resources that can be spent in the near future on services provided to residents. The relationships between governmental activities reported in the statement of net assets and the statement of activities and the governmental fund statements are reconciled in the financial statements.

**Enterprise Funds** - When the City charges customers for the services it provides, these services are generally reported in enterprise funds. Enterprise funds use the same basis of accounting as business-type activities; therefore, these statements are essentially the same.

**Fiduciary Funds** - Fiduciary Funds are used to account for resources held for the benefit of parties outside the City. Fiduciary funds are not reflected on the government-wide financial statements because the resources from these funds are not available to support the City's programs. These funds also use the accrual basis of accounting.

**City of Hillsboro, Ohio**  
Management's Discussion and Analysis  
For the Year Ended December 31, 2006  
(Unaudited)

**The City as a Whole**

The statement of net assets reviews the City as a whole. Table 1 provides a summary of the City's net assets for 2006 compared to the prior year:

Table 1  
Net Assets

	Governmental Activities		Business-Type Activities		Total	
	2006	2005*	2006	2005*	2006	2005
<b>Assets</b>						
Current and Other Assets	\$ 5,851,246	\$ 5,580,919	\$ 1,770,401	\$ 2,082,791	\$ 7,621,647	\$ 7,663,710
Capital Assets, Net	10,026,517	9,781,795	15,324,232	14,122,258	25,350,749	23,904,053
Total Assets	15,877,763	15,362,714	17,094,633	16,205,049	32,972,396	31,567,763
<b>Liabilities</b>						
Current and Other Liabilities	662,806	767,794	111,756	625,934	774,562	1,393,728
Long-Term Liabilities	449,021	435,505	8,395,514	7,908,094	8,844,535	8,343,599
Total Liabilities	1,111,827	1,203,299	8,507,270	8,534,028	9,619,097	9,737,327
<b>Net Assets</b>						
Invested in Capital Assets						
Net of Debt	9,942,251	9,614,912	7,275,964	6,263,501	17,218,215	15,878,413
Restricted	2,339,931	1,883,160	-	-	2,339,931	1,883,160
Unrestricted	2,483,754	2,661,343	1,311,399	1,134,820	3,795,153	3,796,163
Total Net Assets	\$ 14,765,936	\$ 14,159,415	\$ 8,587,363	\$ 7,398,321	\$ 23,353,299	\$ 21,557,736

\* As restated – See note 3.

Total governmental activities assets increased \$606,521 while business-type activities increased \$1,189,042.

Capital assets reported on the government-wide statements represent the largest portion of the City's net assets. At year-end, capital assets represented 77% of total assets. Capital assets include land, land improvements, buildings and improvements, furniture and equipment, vehicles, construction in progress and infrastructure. Capital assets, net of related debt to acquire the assets at December 31, 2006, were \$17,218,215. These capital assets are used to provide services to citizens and are not available for future spending. Although the City's investment in capital assets is reported net of related debt, it should be noted that the resources to repay the debt must be provided from other sources, since capital assets may not be used to liquidate these liabilities. Invested in capital assets, net of related debt for the City as a whole increased consistent with the increase in capital assets during 2006.

A portion of the City's net assets, \$2,339,931 or 16%, represents resources that are subject to external restrictions on how they may be used. There was an increase of \$456,771 or 24% in restricted net assets as the result of an increase in restrictions on assets associated with capital projects. The remaining balance of the government-wide unrestricted net assets is \$3,795,001. Unrestricted net assets decreased \$1,162.

**City of Hillsboro, Ohio**  
**Management's Discussion and Analysis**  
**For the Year Ended December 31, 2006**  
(Unaudited)

Table 2 shows the changes in net assets for the year 2006 compared to the prior year.

Table 2  
Changes in Net Assets

	Governmental Activities		Business Type Activities		Total	
	2006	2005*	2006	2005*	2006	2005*
<b>Revenue</b>						
<b>Program Revenues:</b>						
Charges for Services and Sales	\$ 1,007,781	\$ 989,482	\$ 2,730,406	\$ 2,786,990	\$ 3,738,187	\$ 3,776,472
Operating Grants and Contributions	763,650	1,160,911	-	-	763,650	1,160,911
Capital Grants and Contributions	-	-	900,000	344,558	900,000	344,558
<b>Total Program Revenues</b>	<b>1,771,431</b>	<b>2,150,393</b>	<b>3,630,406</b>	<b>3,131,548</b>	<b>5,401,837</b>	<b>5,281,941</b>
<b>General Revenues:</b>						
Property & Income Taxes	3,863,146	3,767,201	-	-	3,863,146	3,767,201
Unrestricted Investment Earnings	124,953	59,209	17,252	13,166	142,205	72,375
Grants and Contributions Not Restricted to Specific Programs	360,549	-	-	-	360,549	-
Gain on Sale of Capital Assets	2,090	14,800	-	-	2,090	14,800
Other	303,092	284,659	97,931	136,259	401,023	420,918
<b>Total General Revenues</b>	<b>4,653,830</b>	<b>4,125,869</b>	<b>115,183</b>	<b>149,425</b>	<b>4,769,013</b>	<b>4,275,294</b>
<b>Total Revenues</b>	<b>6,425,261</b>	<b>6,276,262</b>	<b>3,745,589</b>	<b>3,280,973</b>	<b>10,170,850</b>	<b>9,557,235</b>
<b>Program Expenses</b>						
<b>General Government -</b>						
Legislative and Executive	1,255,553	1,316,413	-	-	1,255,553	1,316,413
Judicial	239,200	242,754	-	-	239,200	242,754
Security of Persons and Property	2,907,838	2,826,116	-	-	2,907,838	2,826,116
Public Health	155,663	134,053	-	-	155,663	134,053
Leisure Time Activities	131,985	118,738	-	-	131,985	118,738
Community Environment	495,994	440,298	-	-	495,994	440,298
Transportation	625,244	643,567	-	-	625,244	643,567
Interest and Fiscal Charges	7,263	11,222	-	-	7,263	11,222
Water Fund	-	-	1,398,983	1,178,408	1,398,983	1,178,408
Sewer Fund	-	-	1,157,564	1,150,915	1,157,564	1,150,915
<b>Total Expenses</b>	<b>5,818,740</b>	<b>5,733,161</b>	<b>2,556,547</b>	<b>2,329,323</b>	<b>8,375,287</b>	<b>8,062,484</b>
<b>Increase in Net Assets</b>	<b>606,521</b>	<b>543,101</b>	<b>1,189,042</b>	<b>951,650</b>	<b>1,795,563</b>	<b>1,494,751</b>
<b>Beginning Net Assets</b>	<b>14,159,415</b>	<b>13,616,314</b>	<b>7,398,321</b>	<b>6,446,671</b>	<b>21,557,736</b>	<b>20,062,985</b>
<b>Ending Net Assets</b>	<b>\$ 14,765,936</b>	<b>\$ 14,159,415</b>	<b>\$ 8,587,363</b>	<b>\$ 7,398,321</b>	<b>\$ 23,353,299</b>	<b>\$ 21,557,736</b>

\* As restated – See note 3.

**City of Hillsboro, Ohio**  
Management's Discussion and Analysis  
For the Year Ended December 31, 2006  
(Unaudited)

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**Governmental Activities**

Governmental activities increased \$606,521 or 4% during 2006.

The state and federal government contributed to the County revenues of \$763,650 in operating grants and contributions. These revenues are restricted to a particular program or purpose. Operating grants and contributions decreased 397,261 or 34% in 2006 due to a decrease in funding related to the economic development and transportation programs.

General revenues totaled \$4,653,830, and amounted to 72% of total revenues. These revenues primarily consist of property and income tax revenue of \$3,863,146, or 83% of total general revenues in 2006. Property tax revenue increased by \$437,931. This is a result of more real estate tax revenue collected at December 31, 2006 compared to December 31, 2005. The income tax revenue for 2006 was comparable to 2005.

General government expenses include legislative and executive and judicial programs, totaled \$1,494,753 or 26% of total governmental expenses. Legislative and executive expenses decreased \$60,860 due to decreases in salaries and payments for retirement earnings.

Security of persons and property is one of the major activities of the City, generating 50% of total expenses. The expense increased slightly from 2005 to 2006.

**Business-Type Activities**

The City's business-type activities are its water and sewer departments. The water and wastewater treatment plants provide services to the City's residents. The water plant generated operating revenues of \$1,240,912 and had operating expenses of \$1,141,995. The wastewater treatment plant generated operating revenues of \$1,587,425 and had operating expenses of \$1,089,051. The City's goal is to cover the costs of operations as well as to build a cash balance in these funds. The City is also generating funds for additional capital expansion to ensure continued capacity and capacity improvements for future growth and development. The City received \$400,000 in OPWC grant monies and \$500,000 in other capital grants for sewer plant improvements.

**The City's Funds**

Information about the City's major fund starts on page 13. Governmental funds are accounted for using the modified accrual basis of accounting. All governmental funds had total revenues and other financing sources of \$7,185,481 and expenditures and other financing uses of \$6,719,708. The net change in fund balance for the year was most significant in the General Fund, an increase of \$326,381. The majority of the increase in fund balance is due to an increase in the City's property tax revenue from 2005 to 2006.

**City of Hillsboro, Ohio**  
Management's Discussion and Analysis  
For the Year Ended December 31, 2006  
(Unaudited)

**General Fund Budgeting Highlights**

The City's budget is prepared according to Ohio law and is based on accounting for certain transactions on a basis of cash receipts, disbursements, and encumbrances. The most significant budgeted fund is the General Fund.

During the course of 2006, the City amended its General Fund budget. With the General Fund supporting many of the major activities such as the City's police and fire departments, as well as most general government activities, the General Fund is monitored closely to prevent possible revenue shortfalls or over spending by individual departments.

For the General Fund, original budgeted revenues were \$4,552,760 and final budgeted revenues were \$4,667,760. The increase of \$115,000 was mainly due to an increase in the budgeted property tax revenue which was partially offset by a decrease in the budgeted income tax revenue. Original budgeted expenditures were \$5,212,600 and final budgeted expenditures were \$5,247,600. The increase of \$35,000 was due to an increase in the amount budgeted for transfers out which was partially offset by a reduction in budget of general government expenditures.

The General Fund's actual revenues exceeded final budgeted revenues by \$255,083 which was primarily due to charges for services, fines and forfeitures, and interest revenue exceeding final budgeted revenues.

The General Fund's actual expenditures were \$419,296 less than final budgeted expenditures mainly due to legislative and executive, judicial system and community environment expenditures being lower than estimated.

**Capital Assets and Debt Administration**

**Capital Assets**

At the end of the 2006 the City had \$25,350,749 invested in land, land improvements, construction in progress, buildings and improvements, furniture and equipment, vehicles, and infrastructure. Table 3 shows 2006 and 2005 balances.

Table 3

	Governmental Activities		Business-Type Activities		Total	
	2006	2005*	2006	2005*	2006	2005
Land	\$ 384,072	\$ 384,072	\$ -	\$ -	\$ 384,072	\$ 384,072
Land Improvements	1,076,706	1,113,155	100,415	109,467	1,177,121	1,222,622
Buildings and Improvements	1,123,842	1,098,182	8,632,445	8,748,397	9,756,287	9,846,579
Furniture and Equipment	649,499	596,435	370,767	289,669	1,020,266	886,104
Vehicles	672,389	567,110	48,837	38,851	721,226	605,961
Infrastructure	6,017,714	5,920,546	3,088,106	3,051,808	9,105,820	8,972,354
Construction in Progress	102,295	102,295	3,083,662	1,611,366	3,185,957	1,713,661
<b>Totals</b>	<b>\$ 10,026,517</b>	<b>\$ 9,781,795</b>	<b>\$ 15,324,232</b>	<b>\$ 13,849,558</b>	<b>\$ 25,350,749</b>	<b>\$ 23,631,353</b>

\* As more fully described in note 3 to the basic financial statements, the City restated beginning net assets from 2005. This change is reflected in the above table.

See Note 14 for additional information on the City's capital assets.

**City of Hillsboro, Ohio**  
Management's Discussion and Analysis  
For the Year Ended December 31, 2006  
(Unaudited)

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**Debt**

At December 31, 2006, the City of Hillsboro had \$8,132,534 in bonds, loans, and leases outstanding, \$505,992 due within one year.

Table 5  
Outstanding Debt, at Year End

	Governmental Activities		Business-Type Activities		Total	
	2006	2005	2006	2005	2006	2005
O.W.D.A. Loan	\$ -	\$ -	\$ 1,643,634	\$ 817,590	\$ 1,643,634	\$ 817,590
Capital Lease	34,266	66,883	-	-	34,266	66,883
Mortgage Revenue Bonds	-	-	6,677,334	7,041,167	6,677,334	7,041,167
Bonds	50,000	100,000	-	-	50,000	100,000
<b>Total</b>	<b>\$ 84,266</b>	<b>\$ 166,883</b>	<b>\$ 8,320,968</b>	<b>\$ 7,858,757</b>	<b>\$ 8,405,234</b>	<b>\$ 8,025,640</b>

The City's overall legal debt margin was \$3,109,966 at December 31, 2006.

See Note 15 for additional information about the City's debt.

**The Future**

The City of Hillsboro continues to work diligently to increase revenues and decrease costs to put the City on more stable footing. The City has continued to grow with new homes constructed annually, and several new commercial facilities opened with more planned for the future.

The City of Hillsboro has committed itself to financial excellence in the coming years. Our commitment to the residents of the City of Hillsboro will be full disclosure of the financial position of the City.

**Contacting the City's Finance Department**

This financial report is designed to provide our citizens, taxpayers, creditors, and investors with a general overview of the City's finances and to reflect the City's accountability for the monies it receives. Questions about this report or additional financial information needs should be directed to Gary Lewis, City Auditor, 130 North High Street, Hillsboro, Ohio 45133, (937) 393-5791.

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**City of Hillsboro, Ohio**  
Statement of Net Assets  
December 31, 2006

	Governmental Activities	Business-Type Activities	Totals
<b><u>ASSETS</u></b>			
Equity in Pooled Cash and Cash Equivalents	\$ 2,636,471	\$ 850,184	\$ 3,486,655
Investments	6,234	-	6,234
Cash and Cash Equivalents in Segregated Accounts	-	434,300	434,300
Receivables:			
Taxes	1,694,802	-	1,694,802
Accounts	270,847	462,848	733,695
Due From Other Governments	410,843	-	410,843
Loans Receivable	832,049	-	832,049
Deferred Expense on Refunding	-	23,069	23,069
Non-Depreciable Capital Assets	486,367	3,083,662	3,570,029
Depreciable Capital Assets	9,540,150	12,240,570	21,780,720
<b>Total Assets</b>	<b>\$ 15,877,763</b>	<b>\$ 17,094,633</b>	<b>\$ 32,972,396</b>
<b><u>Liabilities</u></b>			
Accounts Payable	\$ 54,793	\$ 28,371	\$ 83,164
Accrued Wages and Benefits	56,526	19,342	75,868
Due to Other Governments	185,587	27,357	212,944
Deferred Revenue	365,900	-	365,900
Accrued Interest Payable	-	36,686	36,686
Long-Term Liabilities			
Due Within One Year	103,953	421,726	525,679
Due in More than One Year	345,068	7,973,788	8,318,856
<b>Total Liabilities</b>	<b>1,111,827</b>	<b>8,507,270</b>	<b>9,619,097</b>
<b><u>Net Assets</u></b>			
Invested in Capital Assets, Net of Related Debt	9,942,251	7,275,964	17,218,215
Restricted for:			
Debt Service	317,158	-	317,158
Revolving Loan	1,069,588	-	1,069,588
Street	238,547	-	238,547
Other Purposes	714,638	-	714,638
Unrestricted	2,483,754	1,311,399	3,795,153
<b>Total Net Assets</b>	<b>\$ 14,765,936</b>	<b>\$ 8,587,363</b>	<b>\$ 23,353,299</b>

See accompanying notes to the basic financial statements.

**City of Hillsboro, Ohio**  
**Statement of Activities**  
For the Year Ended December 31, 2006

Functions/Programs	Program Revenues				Net (Expense) Revenue and Changes in Net Assets		
	Expenses	Charges for Services and Sales	Operating	Capital	Governmental Activities	Business-Type Activities	Totals
			Grants and Contributions	Grants and Contributions			
<b>Governmental Activities:</b>							
<b>General Government:</b>							
Legislative and Executive	\$ 1,255,553	\$ 173,812	\$ 78,195	\$ -	\$ (1,003,546)		\$ (1,003,546)
Judicial	239,200	36,039	1,257	-	(201,904)		(201,904)
Security of Persons and Property	2,907,838	669,379	175,793	-	(2,062,666)		(2,062,666)
Public Health	155,663	15,597	49,906	-	(90,160)		(90,160)
Leisure Time Activities	131,985	11,363	47,366	-	(73,256)		(73,256)
Community Environment	495,994	58,545	228,072	-	(209,377)		(209,377)
Transportation	625,244	42,906	178,846	-	(403,492)		(403,492)
Interest and Fiscal Charges	7,263	140	4,215	-	(2,908)		(2,908)
<b>Total Governmental Activities</b>	<b>5,818,740</b>	<b>1,007,781</b>	<b>763,650</b>	<b>-</b>	<b>(4,047,309)</b>		<b>(4,047,309)</b>
<b>Business-Type activities:</b>							
Sewer	1,157,564	1,567,806	-	900,000		1,310,242	1,310,242
Water	1,398,983	1,162,600	-	-		(236,383)	(236,383)
<b>Total Business-Type Activities</b>	<b>2,556,547</b>	<b>2,730,406</b>	<b>-</b>	<b>900,000</b>	<b>-</b>	<b>1,073,859</b>	<b>1,073,859</b>
<b>Total Government</b>	<b>\$ 8,375,287</b>	<b>\$ 3,738,187</b>	<b>\$ 763,650</b>	<b>\$ 900,000</b>	<b>\$ (4,047,309)</b>	<b>\$ 1,073,859</b>	<b>\$ (2,973,450)</b>
<b>General revenues:</b>							
<b>Taxes:</b>							
<b>Property taxes levied for:</b>							
General Purposes					280,216	-	280,216
Special Purposes					65,830	-	65,830
Debt Service					81,815	-	81,815
Capital Projects					117,128	-	117,128
Income taxes					3,318,157	-	3,318,157
Grants and Contributions Not Restricted to Specific Programs					360,549	-	360,549
Gain on Sale of Capital Assets					2,090	-	2,090
Unrestricted Investment Earnings					124,953	17,252	142,205
Rent					20,155	-	20,155
Miscellaneous					282,937	97,931	380,868
<b>Total general revenues</b>					<b>4,653,830</b>	<b>115,183</b>	<b>4,769,013</b>
<b>Change in net assets</b>					<b>606,521</b>	<b>1,189,042</b>	<b>1,795,563</b>
<b>Net assets - January 1, 2006 (Restated - See Note 3)</b>					<b>14,159,415</b>	<b>7,398,321</b>	<b>21,557,736</b>
<b>Net assets - December 31, 2006</b>					<b>\$ 14,765,936</b>	<b>\$ 8,587,363</b>	<b>\$ 23,353,299</b>

See accompanying notes to the basic financial statements.

**City of Hillsboro, Ohio**  
 Balance Sheet  
 Governmental Funds  
 December 31, 2006

	<u>General</u>	All Other Governmental <u>Funds</u>	Total Governmental <u>Funds</u>
<b>ASSETS:</b>			
Equity in Pooled Cash and Cash Equivalents	\$ 1,271,739	\$ 1,364,732	\$ 2,636,471
Investments	6,234	-	6,234
Accounts Receivable	270,847	-	270,847
Interfund Receivable	350,000	-	350,000
Taxes Receivable	1,477,275	217,527	1,694,802
Due from Other Governments	161,402	249,441	410,843
Loans Receivable	-	832,049	832,049
<i>Total Assets</i>	<u>\$ 3,537,497</u>	<u>\$ 2,663,749</u>	<u>\$ 6,201,246</u>
<b>LIABILITIES:</b>			
Accounts Payable	\$ 27,613	\$ 27,180	\$ 54,793
Accrued Wages and Benefits	52,194	4,332	56,526
Due to Other Governments	79,571	106,016	185,587
Interfund Payable	-	350,000	350,000
Deferred Revenue	806,974	303,901	1,110,875
<i>Total Liabilities</i>	<u>966,352</u>	<u>791,429</u>	<u>1,757,781</u>
<b>FUND BALANCES:</b>			
Reserved:			
Reserved for Encumbrances	108,173	129,090	237,263
Reserved for Loans Receivable	-	832,049	832,049
Unreserved, Undesignated, Reported in:			
General Fund	2,462,972	-	2,462,972
Special Revenue Funds	-	919,432	919,432
Debt Service Funds	-	283,900	283,900
Capital Projects Funds	-	(292,151)	(292,151)
<i>Total Fund Balances</i>	<u>2,571,145</u>	<u>1,872,320</u>	<u>4,443,465</u>
<i>Total Liabilities and Fund Balances</i>	<u>\$ 3,537,497</u>	<u>\$ 2,663,749</u>	<u>\$ 6,201,246</u>

See accompanying notes to the basic financial statements.

**City of Hillsboro, Ohio**  
 Reconciliation of Total Governmental Fund Balances to  
 Net Assets of Governmental Activities  
 December 31, 2006

<b>Total Governmental Fund Balances</b>		\$ 4,443,465
<p>Amounts reported for governmental activities in the statement of net assets are different because:</p>		
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.		10,026,517
Other long-term assets are not available to pay for current period expenditures and therefore are deferred in the funds.		
Taxes	560,614	
Intergovernmental	<u>184,361</u>	
Total		744,975
<p>Long-Term Liabilities, including bonds, capital lease obligations, and the long-term portion of compensated absences are not due and payable in the current period and therefore are not reported in the funds.</p>		
Capital Lease Payable	(34,266)	
Compensated Absences	(364,755)	
General Obligation Bonds	<u>(50,000)</u>	
Total		<u>(449,021)</u>
<b>Net Assets of Governmental Activities</b>		<u><u>\$ 14,765,936</u></u>

See accompanying notes to the basic financial statements.

**City of Hillsboro, Ohio**  
**Statement of Revenues, Expenditures and Changes in Fund Balances**  
**Governmental Funds**  
**For the Year Ended December 31, 2006**

	<u>General</u>	<u>All Other Governmental Funds</u>	<u>Total Governmental Funds</u>
<b>REVENUES:</b>			
Taxes	\$ 3,714,982	\$ 281,528	\$ 3,996,510
Charges for Services	578,506	-	578,506
Licenses and Permits	19,790	-	19,790
Fines and Forfeitures	227,154	182,330	409,484
Intergovernmental	359,672	721,623	1,081,295
Interest	105,608	19,345	124,953
Rent	8,000	12,155	20,155
Other	80,484	202,453	282,937
<i>Total Revenues</i>	<u>5,094,196</u>	<u>1,419,434</u>	<u>6,513,630</u>
<b>EXPENDITURES:</b>			
<b>Current:</b>			
<b>General Government:</b>			
Legislative and Executive	1,008,683	161,358	1,170,041
Judicial	237,248	2,594	239,842
Security of Persons and Property	2,569,664	362,757	2,932,421
Public Health	23,993	102,984	126,977
Lesiure Time Activities	-	97,741	97,741
Community Environment	25,358	470,636	495,994
Transportation	-	369,164	369,164
Capital Outlay	224,814	306,833	531,647
<b>Debt Service:</b>			
Principal Retirements	18,906	63,712	82,618
Interest and Fiscal Charges	-	7,263	7,263
<i>Total Expenditures</i>	<u>4,108,666</u>	<u>1,945,042</u>	<u>6,053,708</u>
<i>Excess of Revenues Over(Under) Expenditures</i>	<u>985,530</u>	<u>(525,608)</u>	<u>459,922</u>
<b>OTHER FINANCING SOURCES AND USES:</b>			
Transfers In	-	666,000	666,000
Proceeds from Sale of Capital Assets	5,851	-	5,851
Transfers Out	(665,000)	(1,000)	(666,000)
<i>Total Other Financing Sources and Uses</i>	<u>(659,149)</u>	<u>665,000</u>	<u>5,851</u>
<i>Net Change in Fund Balances</i>	326,381	139,392	465,773
<i>Fund Balances at Beginning of Year</i>	<u>2,244,764</u>	<u>1,732,928</u>	<u>3,977,692</u>
<i>Fund Balance at End of Year</i>	<u>\$ 2,571,145</u>	<u>\$ 1,872,320</u>	<u>\$ 4,443,465</u>

See accompanying notes to the basic financial statements.

**City of Hillsboro, Ohio**  
 Reconciliation of the Statement of Revenues, Expenditures and Changes  
 in Fund Balances of Governmental Funds to the Statement of Activities  
 For the Year Ended December 31, 2006

**Net Change in Fund Balances - Total Governmental Funds** \$ 465,773

**Amounts reported for governmental activities in the statement of activities are different because:**

Governmental funds report capital outlays as expenditures. However in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the difference between depreciation and capital outlays in the current period.

Capital Asset Additions	750,139	
Current Year Depreciation	(501,656)	
<b>Total</b>	<b>248,483</b>	<b>248,483</b>

Governmental funds only report the disposal of assets to the extent proceeds are received from the sale. In the statement of activities a gain or loss is reported for each disposal. This is the amount of the proceeds and gain on the disposal of fixed assets.

Proceeds from Sale of Capital Assets	(5,851)	
Gain on Disposal of Capital Assets	2,090	
<b>Total</b>	<b>(3,761)</b>	<b>(3,761)</b>

Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.

Taxes	(133,364)	
Intergovernmental	42,905	
<b>Total</b>	<b>(90,459)</b>	<b>(90,459)</b>

Repayments of bond principal are expenditures in the governmental funds, but the repayment reduces liabilities in the statement of net assets and does not result in an expense in the statement of activities.

50,000

Repayment of capital leases obligations are expenditures in the governmental funds, but the repayment reduces liabilities in the statement of net assets and does not result in an expense in the statement of activities.

32,618

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.

Increase in Compensated Absences	(96,133)	
<b>Total</b>	<b>(96,133)</b>	<b>(96,133)</b>

**Net Change in Net Assets of Governmental Activities** **\$ 606,521**

See accompanying notes to the basic financial statements.

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**City of Hillsboro, Ohio**  
Statement of Net Assets  
Proprietary Funds

as of December 31, 2006

	Water	Sewer	Total
<b>ASSETS:</b>			
<i>Current Assets</i>			
Equity in Pooled Cash and Cash Equivalents	\$ 450,439	\$ 399,745	\$ 850,184
Cash and Cash Equivalents in Segregated Accounts	-	434,300	434,300
Accounts Receivable	153,437	309,411	462,848
Deferred Expense on Refunding	-	23,069	23,069
Total Current Assets	<u>603,876</u>	<u>1,166,525</u>	<u>1,770,401</u>
<i>Noncurrent Assets</i>			
Non-Depreciable Capital Assets	3,462	3,080,200	3,083,662
Depreciable Capital Assets, net	7,952,713	4,287,857	12,240,570
Total Noncurrent Assets	<u>7,956,175</u>	<u>7,368,057</u>	<u>15,324,232</u>
Total Assets	<u>\$ 8,560,051</u>	<u>\$ 8,534,582</u>	<u>\$ 17,094,633</u>
<b>LIABILITIES:</b>			
<i>Current Liabilities</i>			
Accounts Payable	\$ 10,826	\$ 17,545	\$ 28,371
Accrued Wages and Benefits	12,036	7,306	19,342
Due to Other Governments	8,843	18,514	27,357
Accrued Interest Payable	34,429	2,257	36,686
OWDA Loans - Current Portion	-	42,893	42,893
Revenue Bonds Payable - Current Portion	105,000	270,000	375,000
Unamortized Charge - Current Portion	3,833	-	3,833
Total Current Liabilities	<u>174,967</u>	<u>358,515</u>	<u>533,482</u>
<i>Noncurrent Liabilities</i>			
Long Term Liabilities:			
OWDA Loans Payable - Net of Current Portion	-	1,600,741	1,600,741
Compensated Absences Payable	29,493	45,053	74,546
Revenue Bonds Payable - Net of Current Portion	5,925,333	285,000	6,210,333
Unamortized Charge - Refunding Bonds - Net of Current Portion	88,168	-	88,168
Total Noncurrent Liabilities	<u>6,042,994</u>	<u>1,930,794</u>	<u>7,973,788</u>
Total Liabilities	<u>6,217,961</u>	<u>2,289,309</u>	<u>8,507,270</u>
<b>NET ASSETS:</b>			
Invested in capital assets, net of related debt	1,833,841	5,442,123	7,275,964
Unrestricted	508,249	803,150	1,311,399
Total Net Assets	<u>\$ 2,342,090</u>	<u>\$ 6,245,273</u>	<u>\$ 8,587,363</u>

See accompanying notes to the basic financial statements.

**City of Hillsboro, Ohio**  
Statement of Revenues, Expenses and  
Changes in Net Assets  
Proprietary Funds

For the Year Ended December 31, 2006

	Water	Sewer	Total
Operating Revenues			
Charges for Services	\$ 1,128,400	\$ 1,545,118	\$ 2,673,518
Tap-In Fees	34,200	22,688	56,888
Other	78,312	19,619	97,931
<b>Total Operating Revenues</b>	<b>1,240,912</b>	<b>1,587,425</b>	<b>2,828,337</b>
Operating Expenses			
Salaries and Wages	349,122	427,376	776,498
Fringe Benefits	156,721	162,626	319,347
Contractual Services	132,311	108,950	241,261
Materials & Supplies	173,581	100,222	273,803
Utilities	78,126	89,542	167,668
Other	32,138	1,499	33,637
Amortization Expense	-	24,336	24,336
Depreciation Expense	219,996	174,500	394,496
<b>Total Operating Expenses</b>	<b>1,141,995</b>	<b>1,089,051</b>	<b>2,231,046</b>
Operating Income	98,917	498,374	597,291
Nonoperating Revenues (Expenses)			
Interest	-	17,252	17,252
Loss on Sale of Capital Assets	(2,022)	(12,388)	(14,410)
Interest & Fiscal Charges	(254,966)	(56,125)	(311,091)
<b>Total Nonoperating Revenues (Expenses)</b>	<b>(256,988)</b>	<b>(51,261)</b>	<b>(308,249)</b>
Changes in Net Assets Before Capital Contributions	(158,071)	447,113	289,042
Capital Contributions - Intergovernmental	-	900,000	900,000
Changes in Net Assets	(158,071)	1,347,113	1,189,042
Net Assets at Beginning of Year (Restated - See Note 3)	2,500,161	4,898,160	7,398,321
<b>Net Assets at End of Year</b>	<b>\$ 2,342,090</b>	<b>\$ 6,245,273</b>	<b>\$ 8,587,363</b>

See accompanying notes to the basic financial statements.

**City of Hillsboro, Ohio**  
**Statement of Cash Flows**  
**Proprietary Funds**  
**For the Year Ended December 31, 2006**

	Water	Sewer	Total
<b><i>Increase (Decrease) in Cash and Cash Equivalents:</i></b>			
<b><i>Cash Flows from Operating Activities:</i></b>			
Cash Received from Customers	\$ 1,129,683	\$ 1,438,192	\$ 2,567,875
Cash Received from Utility Deposits	34,200	22,688	56,888
Cash Received from Other Operating Sources	78,315	21,522	99,837
Cash Payments to Suppliers for Goods and Services	(388,472)	(322,375)	(710,847)
Cash Payments to Employees for Services and Benefits	(496,345)	(566,490)	(1,062,835)
Cash Payments for Other Operating Expenses	(32,138)	(1,499)	(33,637)
<i>Net Cash Provided by (Used for) Operating Activities</i>	<u>325,243</u>	<u>592,038</u>	<u>917,281</u>
<b><i>Cash Flows from Capital and Related Financing Activities:</i></b>			
Receipts from Capital Grants	-	900,000	900,000
Proceeds from OWDA Loan	-	638,699	638,699
Payments for Capital Acquisitions	(64,220)	(2,046,324)	(2,110,544)
Principal Payments	(105,000)	(340,355)	(445,355)
Interest Payments	(258,554)	(49,995)	(308,549)
<i>Net Cash Used for Capital and Related Financing Activities</i>	<u>(427,774)</u>	<u>(897,975)</u>	<u>(1,325,749)</u>
<b><i>Cash Flows from Investing Activities:</i></b>			
Interest on Investments	-	14,771	14,771
<i>Net Cash Provided by (Used for) Investing Activities</i>	<u>-</u>	<u>14,771</u>	<u>14,771</u>
Net Increase/(Decrease) in Cash and Cash Equivalents	(102,531)	(291,166)	(393,697)
Cash and Cash Equivalents at Beginning of Year	552,970	1,125,211	1,678,181
Cash and Cash Equivalents at End of Year	<u>\$ 450,439</u>	<u>\$ 834,045</u>	<u>\$ 1,284,484</u>
<b><i>Reconciliation of Operating Income (Loss) to Net Cash Provided by (Used for) Operating Activities:</i></b>			
Operating Income	\$ 98,917	\$ 498,374	\$ 597,291
<b><i>Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided by (Used for) Operating Activities:</i></b>			
Depreciation	219,996	174,500	394,496
Amortization	-	24,336	24,336
Changes in Assets and Liabilities:			
(Increase)/Decrease in Accounts Receivable	1,283	(106,926)	(105,643)
Increase/(Decrease) in Accounts Payable	(4,451)	(24,358)	(28,809)
Increase/(Decrease) in Accrued Wages and Benefits	58	(460)	(402)
Increase/(Decrease) in Compensated Absences Payable	5,156	20,053	25,209
Increase/(Decrease) in Due to Other Governments	4,284	6,519	10,803
Total Adjustments	<u>226,326</u>	<u>93,664</u>	<u>319,990</u>
Net Cash Provided by (Used for) Operating Activities	<u>\$ 325,243</u>	<u>\$ 592,038</u>	<u>\$ 917,281</u>

See accompanying notes to the basic financial statements.

**City of Hillsboro, Ohio**  
Statement of Fiduciary Assets and Liabilities  
Agency Funds  
As of December 31, 2006

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	<u>Agency</u>
<b>ASSETS</b>	
Cash and Cash Equivalents in Segregated Accounts	\$ 45,042
Receivables:	
Accounts	<u>59,035</u>
Total Assets	<u>\$ 104,077</u>
 <b>LIABILITIES</b>	
Due to Other Governments	\$ 34,831
Undistributed Monies	24,083
Deposits Held and Due to Others	<u>45,163</u>
Total Liabilities	<u>\$ 104,077</u>

See accompanying notes to the basic financial statements.

**City of Hillsboro, Ohio**  
Statement of Revenues, Expenditures and Changes  
In Fund Balance - Budget (Non-GAAP Budgetary Basis) and Actual

General Fund  
For the Year Ended December 31, 2006

	Budgeted Amounts		Actual	Variance With Final Budget Positive (Negative)
	Original	Final		
<b>REVENUES:</b>				
Property Taxes	\$ 232,850	\$ 641,714	\$ 646,154	\$ 4,440
Income Taxes	3,520,746	3,281,246	3,303,947	22,701
Charges for Services	445,077	414,800	497,785	82,985
Licenses and Permits	26,288	24,500	30,651	6,151
Fines and Forfeitures	216,208	201,500	227,154	25,654
Intergovernmental	21,460	20,000	18,403	(1,597)
Interest	69,744	65,000	105,608	40,608
Rent	8,584	8,000	8,000	-
Other	11,803	11,000	85,194	74,194
<b>Total Revenues</b>	<b>4,552,760</b>	<b>4,667,760</b>	<b>4,922,896</b>	<b>255,136</b>
<b>EXPENDITURES:</b>				
<b>Current:</b>				
<b>General Government:</b>				
Legislative and Executive	1,873,162	1,323,150	996,104	327,046
Judicial System	285,238	316,750	237,248	79,502
Security of Persons and Property	2,836,250	2,879,750	2,880,601	(851)
Public Health	25,000	25,000	23,993	1,007
Community Environment	42,950	37,950	25,358	12,592
<b>Total Expenditures</b>	<b>5,062,600</b>	<b>4,582,600</b>	<b>4,163,304</b>	<b>419,296</b>
<b>Excess of Revenues Over(Under) Expenditures</b>	<b>(509,840)</b>	<b>85,160</b>	<b>759,592</b>	<b>674,432</b>
<b>OTHER FINANCING SOURCES AND USES:</b>				
Advances In	-	100,000	60,000	(40,000)
Transfers Out	(150,000)	(665,000)	(665,000)	-
<b>Total Other Financing Sources and Uses</b>	<b>(150,000)</b>	<b>(565,000)</b>	<b>(605,000)</b>	<b>(40,000)</b>
<b>Net Change in Fund Balance</b>	<b>(659,840)</b>	<b>(479,840)</b>	<b>154,592</b>	<b>634,432</b>
Fund Balance at Beginning of Year	791,371	791,371	791,371	-
Prior Year Encumbrances Appropriated	216,615	216,615	216,615	-
<b>Fund Balance (Deficit) at End of Year</b>	<b>\$ 348,146</b>	<b>\$ 528,146</b>	<b>\$ 1,162,578</b>	<b>\$ 634,432</b>

The notes to the basic financial statements are an integral part of this statement.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006

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**1. FINANCIAL REPORTING ENTITY**

The financial statements of the City of Hillsboro have been prepared in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP) as applied to local governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial principles. The City also applies Financial Accounting Standards Board (FASB) Statements and Interpretations issued after November 30, 1989, to its proprietary activities provided they do not conflict with or contradict GASB pronouncements. The most significant of the City's accounting policies are described below.

**CITY GOVERNMENT AND REPORTING ENTITY**

The City of Hillsboro (the "City"), is a body politic and corporate established for the purpose of exercising the rights and privileges conveyed to it by the constitution and laws of the State of Ohio. The City was named in honor of Lord Hillsborough, was founded in 1807 by David Hayes and was named the county seat of Highland County. On January 1, 1952, Hillsboro was first organized as a city under the laws of the State of Ohio.

The City of Hillsboro is a home rule municipal corporation established under the laws of the State of Ohio. The legislative authority is vested in a seven member council three of whom are elected at-large and four by ward for four year terms. The presiding officer is the president, who is elected by the Council for a two year term. Council enacts ordinances and resolutions relating to tax levies, city services, and licensing, appropriates and borrows money, and accepts bids for materials and services and other municipal purposes. The mayor is elected at-large and is the Chief Executive Officer of the City. The Mayor supervises the administration of all departments and appoints their directors and all other employees in accordance with civil service requirements.

The reporting entity is comprised of the primary government, component units and other organizations that are included to ensure that the financial statements of the City are fairly presented and completed. The primary government consists of all funds, departments, boards and commissions that are not legally separate from the City. The City departments include a public safety department, a public service department, a parks and recreation department, a planning and zoning department, income tax department, utility departments including sewer and water, and staff to provide support to service providers.

Component units are legally separate organizations for which the City is financially accountable. The City is financially accountable for an organization if the City appoints a voting majority of the organization's governing board and (1) the City is able to significantly influence the programs or services performed or provided by the organization; or (2) the City is legally entitled to or can otherwise access the organization's resources; the City is legally obligated or has otherwise assumed the responsibility to finance the deficits of, or provide financial support to, the organization; or the City is obligated for the debt of the organization. Component units may also include organizations for which the City approves the budget, the issuance of debt or levying of taxes. The City has no blended or discretely presented component units.

The Hillsboro Municipal Court which provides judiciary services is included as an agency fund in the City's financial statements. The Municipal Court Judge is an elected City Official who has a fiduciary responsibility for the collection and distribution of the court fees and fines.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006

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**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**BASIS OF PRESENTATION**

The City's basic financial statements consist of government-wide statements, including a statement of net assets and statement of activities, and fund financial statements which provide a more detailed level of financial information.

Government-wide Financial Statements

The statement of net assets and the statement of activities display information about the City as a whole. These statements include the financial activities of the primary government, except for fiduciary funds. The statements distinguish between those activities of the City that are governmental in nature and those that are considered business-type.

The statement of net assets presents the financial condition of the governmental and business-type activities of the City at year-end. The statement of activities presents a comparison between direct expenses and program revenues for each program or function of the City's governmental activities and for the business-type activities of the City. Direct expenses are those that are specifically associated with a service, program or department and therefore are clearly identifiable to a particular function. Program revenues include charges paid by the recipient of the goods or services offered by the program, grants and contributions that are restricted to meeting the operational or capital requirements of a particular program and interest earned on grants that is required to be used to support a particular program. Revenues not classified as program revenues are presented as general revenues, with certain limited exceptions. The comparison of direct expenses with program revenues identifies that extent to which each governmental function or business segment is self-financing or draws from the general revenues of the City.

Fund Financial Statements

During the year, the City segregates transactions related to certain functions or activities in separate funds in order to assist financial management and to demonstrate legal compliance. Fund financial statements are designed to present financial information of the City at this more detailed level. The focus of governmental financial statements is on major funds. Each major fund is presented in a separate column. Nonmajor funds are aggregated and presented in a single column.

**FUND ACCOUNTING**

The City uses funds to maintain its financial records during the year. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts. There are three categories of funds: governmental, proprietary, and fiduciary.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006

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**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Governmental Funds - Governmental funds are those through which most governmental functions typically are financed. The acquisition, use and balances of the City's expendable financial resources and the related current liabilities are accounted for through governmental funds. The City maintains records showing revenues, actual and accrued expenditures, and encumbrances to assure legal and accounting compliance and to assure that budgetary authority is not exceeded. The difference between governmental fund assets and liabilities is reported as fund balance. The following is the City's major governmental fund:

*General Fund* - This fund is established to account for resources devoted to financing the general services that the City performs for its residents. Municipal income tax, general tax revenues, as well as other sources of revenue used to finance the fundamental operations of the City are included in this fund. The fund is charged with all costs of operating the government for which a separate fund has not been established.

The other governmental funds of the City account for grants and other resources that are generally restricted to use for a particular purpose.

Proprietary Funds - Proprietary fund reporting focuses on the determination of operating income, changes in net assets, financial position, and cash flows.

Enterprise Funds - Enterprise funds may be used to account for any activity for which a fee is charged to external users for goods or services. The following are the City's major enterprise funds:

*Water Fund* - This fund accounts for the provision of water treatment and distribution to residential and commercial users within the City.

*Sewer Fund* - This fund accounts for the provision of wastewater treatment services to residential and commercial users within the City.

Fiduciary Funds - Fiduciary funds are used to account for assets held by the City as a trustee or as an agent for individuals, private organizations, or other units of government. The fiduciary fund category is split into four classifications: agency funds, pension trust funds, investment trust funds, and private purpose trust funds. Agency funds are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations. Trust funds are used to account for assets held under a trust agreement for individuals, private organizations, or other governments and are therefore not available to support the City's own programs. The City's fiduciary fund consists only of an agency fund which is used to account for the activities of the Hillsboro Municipal Court.

**MEASUREMENT FOCUS**

Government-wide Financial Statements

The government-wide financial statements are prepared using the economic resources measurement focus. All assets and all liabilities associated with the operation of the City are included on the Statement of Net Assets.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006

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**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Fund Financial Statements

All governmental funds are accounted for using a flow of current financial resources measurement focus. With this measurement focus, only current assets and liabilities generally are included on the balance sheet. The statement of revenues, expenditures and changes in fund balances reports on the sources (i.e., revenues and other financial sources) and uses (i.e., expenditures and other financing uses) of current financial resources. This approach differs from the manner in which the governmental activities on the government-wide financial statements are prepared. Government fund financial statements therefore include a reconciliation with brief explanations to better identify the relationship between the government-wide statements and the statements of government funds.

Like the government-wide financial statements, all enterprise funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the statement of net assets. The statement of revenues, expenses, and changes in net assets presents increases (i.e., revenues) and decreases (i.e., expenses) in total net assets. The statement of cash flows reflects how the City finances and meets the cash flow needs of its enterprise activities.

**BASIS OF ACCOUNTING**

Accounting basis determines when transactions and economic events are reflected in its financial statements. Government-wide financial statements are prepared using the accrual basis of accounting. Government funds use the modified accrual basis of accounting; proprietary and fiduciary funds use the accrual basis of accounting. Differences in the accrual and modified accrual basis of accounting arise in the recognition of revenue, the recording of deferred revenue and in the presentation of expenses versus expenditures.

***Revenues-Exchange and Non-exchange Transactions*** Revenue resulting from exchange transactions, in which each party gives and receives essentially equal value, is recorded on the accrual basis when the exchange takes place. On a modified accrual basis, revenue is recorded in the fiscal year in which the resources are measurable and become available. Available means that the resources will be collected within the current fiscal year or are expected to be collected soon enough thereafter to be used to pay liabilities of the current fiscal year. For the City, available means expected to be received within sixty days of fiscal year end.

Non-exchange transactions, in which the City receives value without directly giving equal value in return, include property taxes, grants, entitlements and donations. Revenue from property taxes is recognized in the fiscal year for which taxes are levied. Revenue from grants is recognized in the fiscal year in which all eligibility requirements have been satisfied. Eligibility requirements include timing requirements, which specify the year when the resources are required to be used or the fiscal year when use is first permitted, matching requirements, in which the City must provide local resources to be used for a specified purpose, and expenditure requirements, in which the resources are provided to the City on a reimbursement basis. On a modified accrual basis, revenue from non-exchange transactions must also be available before it can be recognized.

Under the modified accrual basis, the following revenue sources are considered to be both measurable and available at fiscal year end: property taxes available as an advance, interest, and grants.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006

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**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Deferred Revenue** Deferred revenue arises when assets are recognized before revenue recognition criteria have been satisfied.

Property taxes for which there is an enforceable legal claim as of December 31, 2006, but which were levied to finance fiscal year 2007 operations, have been recorded as deferred revenue. Grants and entitlements received before the eligibility requirements were met have also been recorded as deferred revenue.

On governmental fund financial statements, receivables that were not collected with the available period are also reflected as deferred revenue.

**Expenses/Expenditures** On the accrual basis of accounting, expenses are recognized at the time they are incurred. The measurement focus of governmental fund accounting is on decreases in net financial resources (expenditures) rather than expenses. Expenditures are generally recognized in the accounting period in which the related fund liability is incurred, if measurable. Allocations of cost, such as depreciation and amortization, are not recognized in governmental funds.

**BUDGETS AND BUDGETARY ACCOUNTING**

The budgetary process is prescribed by provisions of the Ohio Revised Code and entails the preparation of budgetary documents within an established timetable. The major documents prepared are the tax budget, the certificate of estimated resources, and the appropriation resolution, all of which are prepared on the budgetary basis of accounting. The certificate of estimated resources and the appropriations resolution are subject to amendment throughout the year with the legal restriction that appropriations cannot exceed estimated resources, as certified. All funds, other than agency funds are legally required to be budgeted and appropriated. For the General fund, Council appropriations are budgeted for fund and function level. For all other funds, Council appropriations are budgeted to the fund level. Any budgetary modifications at this level may only be made by resolution of the members of Council. The City follows these procedures in establishing the budgetary data reported in the financial statements.

**Tax Budget:** By July 15, the Auditor submits an annual tax budget for the following fiscal year to City Council for consideration and passage. The adopted budget is submitted to the County Auditor, as secretary of the County Budget Commission, by July 20 of each year, for the period January 1 to December 31 of the following year.

**Estimated Resources:** The County Budget Commission certifies its actions to the City by September 1. As part of this certification, the City receives the official certificate of estimated resources which states the projected receipts of each fund. On or about January 1, this certificate is amended to include any unencumbered balances from the preceding year. Prior to December 31, the City must revise its budget so that the total contemplated expenditures from a fund during the ensuing fiscal year will not exceed the amount stated in the certificate of estimated resources.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006

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**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

The revised budget then serves as the basis for the annual appropriation measure. Further amendments may be made during the year if the Council determines that revenue to be collected will be greater than or less than prior estimates and the budget commission finds the revised estimate to be reasonable. The amounts set forth in the financial statements represent estimates from the final amended certificate issued in 2006.

**Appropriations:** A temporary appropriation measure to control cash disbursements may be passed on or about January 1 of each year for the period January 1 to March 31. An annual appropriation measure must be passed by April 1 of each year for the period January 1 to December 31. The appropriation measure may be amended or supplemented during the year as new information becomes available. Appropriations may not exceed estimated resources. Supplemental appropriations may be adopted by Council. Amounts shown in the financial statements represent the appropriated budgeted amounts and all supplemental appropriations. Supplemental appropriations were adopted during 2006 by the Council.

**Budgeted Level of Expenditure:** Administrative control is maintained through the establishment of budgets. Appropriated funds may not be expended for purposes other than those designated in the appropriation ordinance without authority from Council. Expenditures plus encumbrances may not legally exceed appropriations at the level of appropriation adopted by Council. The appropriations allocations may be made by the City Auditor as long as the allocations are within Council's appropriated amount.

**Encumbrances:** As part of formal budgetary control, purchase orders, contracts and other commitments for the expenditure of funds are recorded as the equivalent of expenditures on the non-GAAP budgetary basis in order to reserve the portion of the applicable appropriation and determine and maintain legal compliance. On the GAAP basis, encumbrances outstanding at year end are reported as a reservation of fund balance and subsequent year expenditures for governmental funds.

**Lapsing of Appropriations:** At the close of each fiscal year, the unencumbered balance of each appropriation reverts to the respective fund from which it was appropriated and becomes subject to future appropriation. Encumbered appropriations are carried forward to the succeeding fiscal year and are not reappropriated.

**CASH AND INVESTMENTS**

Cash balances of the City's funds, except cash held by a trustee or fiscal agent and in segregated accounts, are pooled and invested in short-term investments in order to provide improved cash management. Individual fund integrity is maintained through the City's records. Interest is distributed to various funds based upon the Ohio Revised Code requirements. Each fund's interest in the pool is presented as "Equity in Pooled Cash and Cash Equivalents" on the financial statements.

During the year 2006, investments were limited to repurchase agreements, money market accounts, and donated common stock.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006

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**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Except for nonparticipating investment contracts, investments are reported at fair value which is based on quoted market prices. Nonparticipating investment contracts such as repurchase agreements and nonnegotiable certificates of deposit are reported at cost.

For purposes of the statement of cash flows and for presentation on the statement of net assets and the balance sheet, funds included within the City's cash management pool and investments with original maturities of three months or less are considered to be cash and cash equivalents. Investments with an initial maturity of more than three months are reported as investments.

**CAPITAL ASSETS**

General capital assets are those assets not specifically related to activities reported in the enterprise funds. These assets generally result from expenditures in the governmental funds. These assets are reported in the governmental activities column of the government-wide statement of net assets but are not reported in the fund financial statements. Capital assets used by the enterprise funds are reported in both the government-wide statement of net assets and in the respective funds.

All capital assets are capitalized at cost (or estimated historical cost) and updated for additions and reductions during the year. Donated fixed assets are recorded at their fair market value on the date donated. The City maintains a capitalization threshold of five hundred dollars. The City's infrastructure consists of streets, bridges, storm and sanitary sewer lines and water lines. Improvements are capitalized. Interest incurred during the construction of fund capital assets is also capitalized.

All capital assets are depreciated, except for land and construction in progress. Improvements are depreciated over the remaining useful lives of the related capital assets. Depreciation has been provided on a straight-line basis over the following estimated useful lives for both governmental and business-type activities:

<u>Description</u>	<u>Estimated Lives</u>
Buildings and Improvements	30 years
Land Improvements	20 years
Furniture	10 years
Machinery and Equipment	10-20 years
Vehicles	8 years
Water/Sewer Lines	65 years
Infrastructure	10-40 years

**INTERFUND ASSETS AND LIABILITIES**

On fund financial statements, receivables and payables resulting from short-term inter-fund loans are classified as "Interfund Receivables/Payables". Inter-fund balances within governmental activities and within business-type activities are eliminated on the government-wide statement of net assets. The only inter-fund balances which remain on the government-wide statement of net assets are those between governmental and business-type activities. These amounts are reflected as "Internal Balances"; however, there were no internal balances at December 31, 2006.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006

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**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**COMPENSATED ABSENCES**

Vacation benefits are accrued as a liability as the benefits are earned if the employees' rights to receive compensation are attributable to services already rendered and it is probable that the employer will compensate the employees for the benefits through paid time off or some other means. Sick leave benefits are accrued as a liability using the termination method. The liability includes the employees who are currently eligible to receive termination benefits and by those employees for whom it is probable will become eligible to receive payment in the future. The amount is based on accumulated sick leave and employee's wage rates at year end. This item is discussed in Note 13 to the Basic Financial Statements.

The entire compensated absences liability is reported on the government-wide financial statements.

On fund financial statements for governmental funds, the current portion of unpaid compensated absences is the amount expected to be paid as a result of employee resignations and retirements. These amounts are recorded in the account "matured compensated absences payable" in the fund from which the employees who have accumulated unpaid leave are paid. The non-current portion of the liability is not reported. For enterprise funds, the entire amount of compensated absences is reported as a fund liability.

**ACCRUED LIABILITIES AND LONG-TERM OBLIGATIONS**

All payables, accrued liabilities, and long-term obligations are reported on the government-wide financial statements. All payables, accrued liabilities, and long-term obligations payable from the enterprise funds are reported on the enterprise fund financial statements. In general, governmental fund payables and accrued liabilities that, once incurred, are paid in a timely manner and in full from current financial resources are reported as obligations of the funds. Notes, capital leases, and bonds are recognized as liabilities on the fund financial statements when due.

**RESERVES OF FUND BALANCES**

The City records reservations for those portions of fund balance which are legally segregated for specific future use or which do not represent available, spendable resources and, therefore, are not available for expenditure. Undesignated fund balance indicates that portion of fund balance which is available for appropriation in future periods. Fund balance reserves have been established for encumbrances and for loans, which represent community development monies loaned to local businesses and homeowners.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006

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**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**NET ASSETS**

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any borrowing used for the acquisition, construction, or improvement of those assets. Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the City or through external restrictions imposed by creditors, grantors, or laws or regulations of other governments. Restricted for other purposes represents balances of state and federal grants and other restricted purposes in Special Revenue funds. The City's policy is to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

Of the City's \$2,340,084 restricted net assets, \$0 are restricted for enabling legislation.

**OPERATING REVENUES AND EXPENSES**

Operating revenue are those revenues that are generated directly from the primary activity of the enterprise funds. For the City, these revenues are charges for services for sewer and water utility services. Operating expenses are the necessary costs incurred to provide the service that is the primary activity of the fund.

**CAPITAL CONTRIBUTIONS**

Capital contributions in the enterprise fund financial statements arise from outside contributions of fixed assets or from grants or outside contributions of resources restricted to capital acquisition and construction.

**INTERFUND TRANSACTIONS**

Transfers between governmental and business-type activities on the government-wide financial statements are reported in the same manner as general revenues.

Exchange transactions between funds are reported as revenues in the seller funds and as expenditures/expenses in the purchaser funds. Flows of cash or goods from one fund to another without a requirement for repayment are reported as inter-fund transfers. Inter-fund transfers are reported as other financing sources/uses in governmental funds and after non-operating revenues/expenses in enterprise funds. Repayments from funds responsible for particular expenditures/expenses to the funds that initially paid for them are not presented on the financial statements. Transfers between governmental funds are eliminated on the statement of activities.

**ESTIMATES**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

**CITY OF HILLSBORO, OHIO**  
**NOTES TO THE BASIC FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED DECEMBER 31, 2006**

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**3. CHANGE IN ACCOUNTING PRINCIPLES AND RESTATEMENT OF FUND BALANCES/NET ASSETS**

For the fiscal year 2006, the City implemented Governmental Accounting Standards Board (GASB) Statement No. 46, *Net Assets Restricted by Enabling Legislation* and GASB Statement No. 47, *Accounting for Termination Benefits*. GASB Statement No. 46 requires that limitations on the use of net assets imposed by enabling legislation be reported as restricted net assets. GASB Statement No. 47 establishes accounting standards for termination benefits. The application of these new standards did not have a material effect on the financial statements, nor did their implementation require a restatement of prior year balances.

**Restatement of Net Assets:** During the previous fiscal year accounting errors were noted. There were some corrections to capital assets in both the Sewer fund and in governmental activities. These changes had the following affect on beginning net asset balances:

	Governmental Activities		
Net Assets, December 31, 2005	\$ 14,207,976		
Restatement	(48,561)		
Restated Net Assets, December 31, 2005	\$ 14,159,415		
	Water	Sewer	Business-Type Activities
Net Assets, December 31, 2005	\$ 2,500,161	\$ 4,667,301	\$ 7,167,462
Restatement	-	230,859	230,859
Restated Net Assets, December 31, 2005	\$ 2,500,161      \$ 4,898,160      \$ 7,398,321		

**4. DEPOSITS AND INVESTMENTS**

State statutes classify monies held by the City into three categories.

Active deposits are public deposits necessary to meet current demands on the treasury. Such monies must be maintained either as cash, in commercial accounts payable or withdrawable on demand, including negotiable order of withdrawal (NOW) accounts, or in money market deposit accounts.

Inactive deposits are public deposits that the City has identified as not required for use within the five year period of designation of depositories. Inactive deposits must be either evidenced by certificates of deposit maturing not later than the end of the current period of designation of depositories, or by savings or deposit accounts including, but not limited to, passbook accounts.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006

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**4. DEPOSITS AND INVESTMENTS (Continued)**

Interim deposits are deposits of interim moneys. Interim moneys are those moneys which are not needed for immediate use but which will be needed before the end of the current period of designation of depositories. Interim deposits must be evidenced by time certificates of deposit maturing not more than one year from the date of deposit or by savings or deposit accounts including passbook accounts.

State statute permits interim monies to be deposited or invested in the following securities:

1. United States treasury notes, bills, bonds, or other obligations of or security issued by the United States treasury or any other obligation guaranteed as to the payment of principal and interest by the United States;
2. Bonds, notes, debentures, or other obligations or securities issued by any federal government agency or instrumentality, including but not limited to, the federal national mortgage association, federal home loan bank, federal farm credit bank, federal home loan mortgage corporation, government national mortgage association, and student loan marketing association. All federal agency securities shall be direct issuances of federal government agencies or instrumentalities;
3. Written repurchase agreements in the securities listed above, provided that the market value of the securities subject to the repurchase agreement must exceed the principal value of the agreement by at least two percent and be marked to market daily, and that the term of the agreement must not exceed thirty days;
4. Bond and other obligations of the State of Ohio, its political subdivision, or other units or agencies of this State or its political subdivisions;
5. Time certificates of deposit or savings or deposit accounts, including, but not limited to, passbook accounts;
6. No-load money market mutual funds consisting exclusively of obligations described in division (1) or (2) and repurchase agreements secured by such obligations, provided that investments in securities described in this division are made only through eligible institutions;
7. The State Treasurer's investment pool (STAR Ohio);
8. Securities lending agreements in which the County lends securities and the eligible institution agrees to exchange either securities described in division (1) or (2), or cash, or both securities and cash, equal value for equal value;
9. High grade commercial paper in an amount not to exceed 5 percent of the County's total average portfolio; and
10. Bankers acceptances for a period not to exceed two hundred seventy days and in an amount not to exceed 10 percent of the County's total average portfolio.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006

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**4. DEPOSITS AND INVESTMENTS (Continued)**

Protection of the City's deposits is provided by the Federal Deposit Insurance Corporation (FDIC), by eligible securities pledged by the financial institution as security for repayment, by surety company bonds deposited with the Treasurer by the financial institution, or by a single collateral pool established by the financial institution to secure the repayment of all public money deposited with the institution.

Investments in stripped principal or interest obligations, reverse repurchase agreements and derivatives are prohibited. The issuance of taxable notes for the purpose of arbitrage, the use of leverage and short selling are also prohibited. An investment must mature within five years from the date of purchase unless matched to a specific obligation or debt of the City, and must be purchased with the expectation that it will be held to maturity.

Investments may only be made through specified dealers and institutions. Payment for investments may be made only upon delivery of the securities representing the investments to the treasurer or qualified trustee or, if the securities are not represented by a certificate, upon receipt of confirmation of transfer from the custodian.

***Deposits:***

Custodial credit risk is the risk that, in the event of a bank failure, the City's deposits may not be returned. According to state law, public depositories must give security for all public funds on deposit in excess of those funds that are insured by the federal deposit insurance corporation (FDIC) or by any other agency or instrumentality of the federal government. These institutions may either specifically collateralize individual accounts in lieu of amounts insured by the FDIC, or may pledge a pool of government securities valued at least 105% of the total value of public monies on deposit at the institution. The City's policy is to deposit money with financial institutions that are able to abide by the laws governing insurance and collateral of public funds.

The City's bank balance of \$3,771,352 is either covered by FDIC or collateralized by the financial institutions public entity deposit pools in the manner as described above.

**CITY OF HILLSBORO, OHIO**  
**NOTES TO THE BASIC FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED DECEMBER 31, 2006**

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**4. DEPOSITS AND INVESTMENTS (Continued)**

*Investments:*

<u>Investment type</u>	<u>Fair Value</u>	<u>Maturities</u> 6 months or less
Common Stock	\$ 6,234	\$ 6,234
U.S. Government Money Market Mutual Funds	<u>423,490</u>	<u>423,490</u>
	<u>\$ 429,724</u>	<u>\$ 429,724</u>

Interest rate risk – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The City has no policy specifically dealing with interest rate risk, in accordance with investment policy, the City manages its exposure to declines in fair values by limiting the weighted average maturity of its investment portfolio to five years or less.

Credit Risk – Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The City’s investment policy allows the City to invest in accordance with the Ohio Revised Code (Ohio Law). The City limits their investments to money market accounts, repurchase agreements, and stocks.

Concentration of credit risk – Concentration of credit risk is the risk of loss attributed to the magnitude of a government’s investment in a single issuer. The City places no limit on the amount the City may invest in any one issuer. The City does have an investment policy. More than 99 percent of the City’s investments are in money market funds as of December 31, 2006.

Custodial Credit Risk – Custodial credit risk is the risk that in the event of the failure of the counterparty, the City will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. All of the City’s securities are either insured and registered in the name of the City or at least registered in the name of the City. The City has no policy specifically related to custodial credit risk, but requires the City to conform to requirements of Ohio law.

**5. BUDGETARY BASIS OF ACCOUNTING**

While the City is reporting financial position, results of operations and changes in fund balance on the basis of accounting principles generally accepted in the United States of America (GAAP), the budgetary basis as provided by law and described above is based upon accounting for certain transactions on a basis of cash receipts, disbursements and encumbrances. The Statement of Revenues, Expenditures and Changes in Fund Balances - Budget (Non-GAAP Budgetary Basis) and Actual, for the General Fund are presented on the budgetary basis to provide a meaningful comparison of actual results with the budget. The major differences between the budget basis and GAAP basis are as follows:

**CITY OF HILLSBORO, OHIO**  
**NOTES TO THE BASIC FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED DECEMBER 31, 2006**

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**5. BUDGETARY BASIS OF ACCOUNTING (Continued)**

1. Revenues are recorded when received in cash (budget basis) as opposed to when susceptible to accrual (GAAP basis).
2. Expenditures are recorded when paid in cash (budget basis) as opposed to when the liability is incurred (GAAP basis).
3. Encumbrances are treated as expenditures for all funds (budget basis) rather than as a reservation of fund balance for governmental fund types (GAAP basis).

The following table summarizes the adjustments necessary to reconcile the GAAP and budgetary basis for the General Fund.

Net Change in Fund Balance	
	General
GAAP Basis	\$ 326,381
Adjustments:	
Revenue Accrual	(117,304)
Expenditure Accrual	53,535
Encumbrances	(108,173)
Budget Basis	\$ 154,439

**6. PROPERTY TAX**

Property taxes include amounts levied against all real, public utility, and tangible personal property located in the County. Taxes collected on real property (other than public utility) in one calendar year are levied in the preceding calendar year on assessed values as of January 1 of that preceding year, the lien date. Assessed values are established by the County Auditor at 35 percent of appraised market value. All property is required to be revalued every six years. The last revaluation was completed in 2000. Real property taxes are payable annually or semiannually. The first payment is due January 20, with the remainder payable by June 20.

Taxes collected from tangible personal property (other than public utility) in one calendar year are levied in the prior calendar year on assessed values during and at the close of the most recent fiscal year of the taxpayer that ended on or before March 31 of that calendar year, and at the tax rates determined in the preceding year. Tangible personal property used in business (except for public utilities) is currently assessed for ad valorem taxation purposes at 25 percent of its true value. Amounts paid by multi-county taxpayers are due September 20. Single county taxpayers may pay annually or semiannually. If paid annually, payment is due April 30; if paid semiannually, the first payment is due April 30, with the remainder payable by September 20.

Public utility real and tangible personal property taxes collected in one calendar year are levied in the preceding calendar year on assessed values determined as of December 31 of the second year preceding the tax collection year, the lien date. Certain public utility tangible personal property currently is assessed at 88 percent of its true value. Public utility property taxes are payable on the same dates as real property taxes described previously.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
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**6. PROPERTY TAX (Continued)**

The County Treasurer collects property tax on behalf of all taxing districts within the County. The County Auditor periodically remits to the City its share of the taxes collected. The City records receipt of these taxes in various funds.

Accrued property taxes receivable represent delinquent taxes outstanding and real, tangible personal, and public utility taxes which were measurable and unpaid as of December 31, 2006. Although total property tax collections for the next fiscal year are measurable, amounts to be received during the available period are not subject to reasonable estimation at December 31 and are not intended to finance 2006 operations. The receivable is therefore offset by a credit to deferred revenue.

The full tax rate for all City operations for the year ended December 31, 2006, was \$3.00 per \$1,000 of assessed value. The assessed values of real and tangible personal property upon which 2006 property tax receipts were based are as follows:

<u>Category</u>	<u>Assessed Value</u>
Real Estate	\$107,214,450
Public Utility Personal Property	3,742,890
Tangible Personal Property	<u>25,024,332</u>
Total Property Taxes	<u>\$135,981,672</u>

**7. LOCAL INCOME TAX**

This locally levied tax of one and one-half percent applies to gross salaries, wages and other personal service compensation earned by residents both in and out of the City of Hillsboro and to earnings of nonresidents earned in the City. It also applies to net income of business organizations conducted within the City. Proceeds of the tax are credited entirely to the General Fund.

**8. RECEIVABLES**

Receivables at December 31, 2006 consisted of taxes, accounts (billings for user charged services including unbilled utility services), and intergovernmental receivables arising from grants, entitlements and shared revenues. All receivables are considered fully collectible except accounts receivable related to utility services.

Loans receivable represents low interest loans for development projects and home improvements granted to eligible City residents and business under the Community Development Program.

Municipal Court receivables reported in the agency funds amount to \$1,421,446. Due to the age of many of these accounts, the amount of \$1,362,411 is considered uncollectable.

**CITY OF HILLSBORO, OHIO**  
**NOTES TO THE BASIC FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED DECEMBER 31, 2006**

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**8. RECEIVABLES (Continued)**

A summary of the amounts due from other governments are as follows:

<u>General</u>	
Local Government	\$152,625
Homestead & Rollback	8,777
 <u>Special Revenue</u>	
Street Constr., Maint. & Repair Fund	
Gasoline Tax	108,540
State Highway Fund	
Gasoline Tax	8,799
Police Pension Fund	
Homestead & Rollback	1,254
Fire Pension Fund	
Homestead & Rollback	1,254
Municipal Motor Vehicle Fund	
Permissive Tax	6,579
Rehab	121,761
 <u>Debt Service</u>	
Bond Retirement Fund	
Homestead & Rollback	<u>1,254</u>
 Total Governmental Activities	 <u>\$410,843</u>

**9. INTERFUND TRANSACTIONS**

Interfund balances at December 31, 2006, consist of the following individual fund receivables and payables:

	Interfund Receivable	Interfund Payable
General Fund	\$350,000	\$ 0
<i>Non-major Fund:</i>		
Tax Increment Capital Projects Fund	0	350,000
 Total All Funds	 <u>\$350,000</u>	 <u>\$350,000</u>

The above balance resulted from an advance to cover shortfalls which will be repaid with future revenues.

**CITY OF HILLSBORO, OHIO**  
**NOTES TO THE BASIC FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED DECEMBER 31, 2006**

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**9. INTERFUND TRANSACTIONS (Continued)**

Transfers are used to move revenues from the fund that statute or budget requires to collect them to the fund that statute or budget requires to expend them; to move receipts restricted to debt service from the funds collecting the receipts to the debt service fund as debt service payment become due, and use unrestricted revenues collected in the general fund to finance various programs accounted for in other funds in accordance with budgetary authorizations.

Transfers made during the year ended December 31, 2006, were as follows:

FUND	Transfer In	Transfer Out
General	\$ -	\$ 665,000
	-	665,000
<i>Non-Major Special Revenue Funds</i>		
Street C.M. & Repair	150,000	-
Police Pension	160,000	-
Fire Pension	185,000	-
Recreation	115,000	-
Rehab	1,000	-
Life Squad Improvement	55,000	-
House Revolving Loan	-	1,000
Total Non-Major Special Revenue	666,000	1,000
Total All Funds	\$ 666,000	\$ 666,000

**10. DEFINED BENEFIT RETIREMENT PLANS**

**Ohio Public Employees Retirement System:** The City participates in the Ohio Public Employees Retirement System (OPERS). OPERS administers three separate pension plans. The traditional plan is a cost-sharing, multiple-employer defined benefit pension plan. The member-directed plan is a defined contribution plan in which the member invests both member and employer contributions (employer contributions vest over five years at 20 percent per year). Under the member directed plan, members accumulate retirement assets equal to the value of the member and vested employer contributions plus any investment earnings. The combined plan is a cost-sharing, multiple-employer defined benefit pension plan that has elements of both a defined benefit and a defined contribution plan. Under the combined plan, employer contributions are invested by the retirement system to provide a formula retirement benefit similar to the traditional plan benefit. Member contributions, whose investment is self-directed by the member, accumulate retirement assets in a manner similar to the member directed plan.

OPERS provides retirement, disability, survivor and death benefits and annual cost of living adjustments to members of the traditional and combined plans. Members of the member directed plan do not qualify for ancillary benefits. Authority to establish and amend benefits is provided by Chapter 145 of the Ohio Revised Code. OPERS issues a stand-alone financial report that may be obtained by writing to OPERS, 277 East Town Street, Columbus, OH 43215-4642 or by calling (614) 222-6701 or (800) 222-7377.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006

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**10. DEFINED BENEFIT RETIREMENT PLANS (Continued)**

For the year ended December 31, 2006, the members of all three plans, except those in law enforcement or public safety participating in the traditional plan, were required to contribute 9 percent of their annual covered salaries. Members participating in the traditional plan who were in law enforcement contributed 10.1 percent of their annual covered salary; members in public safety contributed 10.1 percent. The employer contribution rate for pension benefits for 2006 was 13.7 percent, except for those plan members in law enforcement or public safety. For those classifications, the employer's pension contributions were 16.93 percent of covered payroll. The Ohio Revised Code provides statutory authority for member and employer contributions.

The City's contributions to the PERS of Ohio for the years ending December 31, 2004, 2005, and 2006 were \$228,234, \$228,461, and \$240,488 respectively. These contributions were equal to the required contributions for each of the years.

***Ohio Police and Fire Disability and Pension Fund:*** The City contributes to the Ohio Police and Fire Pension Fund (OP&F), a cost-sharing multiple-employer defined benefit pension plan. OP&F provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit provisions are established by the Ohio State Legislature and are codified in Chapter 742 of the Ohio Revised Code. OP&F issues a publicly available financial report that includes financial information and required supplementary information for the plan. That report may be obtained by writing to the Ohio Police and Fire Pension Fund, 140 East Town Street, Columbus, Ohio 43215-5164.

Plan members are required to contribute 10 percent of their annual covered salary to fund pension benefits while the employer is required to contribute 19.5 percent for police officers and 24 percent for firefighters. Contributions are authorized by State statute.

The City's contributions to OP&F for the years ended December 31, 2004, 2005, and 2006 were \$203,315, \$157,541, and \$151,149 for policemen and \$160,814, \$197,546, and \$200,489 for firefighters, respectively, equal to required contributions for each year.

**11. POSTEMPLOYMENT BENEFITS**

***Ohio Public Employees Retirement System:*** The Ohio Public Employees Retirement System (OPERS) provides postretirement health care coverage to age and service retirees with ten or more years of qualifying Ohio service credit with either the traditional or combined plans. Health care coverage for disability benefit recipients and qualified survivor benefit recipients is available. Members of the member-directed plan do not qualify for postretirement health care coverage. The health care coverage provided by the retirement system is considered an Other Postemployment Benefit as described in *GASB Statement No. 12*. A portion of each employer's contribution to the traditional or combined plans is set aside for the funding of postretirement health care based on authority granted by State statute. The 2006 local government employer contribution rate was 13.70 percent of covered payroll (16.7 percent for public safety and law enforcement); 4.5 percent of covered payroll was the portion that was used to fund health care.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006

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**11. POSTEMPLOYMENT BENEFITS (Continued)**

Benefits are advance-funded using the entry age normal actuarial cost method. Significant actuarial assumptions, based on OPERS's latest actuarial review performed as of December 31, 2005, include a rate of return on investments of 6.5 percent, an annual increase in active employee total payroll of 4 percent compounded annually (assuming no change in the number of active employees) and an additional increase in total payroll of between 0.50 percent and 6.3 percent based on additional annual pay increases. Health care premiums were assumed to increase at the projected wage inflation rate plus an additional factor ranging from 1 to 6 percent annually for the next nine years and 4 percent annually after nine years.

All investments are carried at market. For actuarial valuation purposes, a smoothed market approach is used. Assets are adjusted to reflect 25 percent of unrealized market appreciation or depreciation on investment assets annually.

The number of active contributing participants in the traditional and combined plans was 369,214. The number of active contributing participants for both plans used in the December 31, 2005 (the latest information available) actuarial valuation was 358,804. Actual City contributions for 2006 which were used to fund postemployment benefits were \$79,000. The actual contribution and the actuarially required contribution amounts are the same. The actuarial value of OPERS's net assets available for payment of benefits at December 31, 2005, (the latest information available) was \$11.1 billion. The actuarially accrued liability and the unfunded actuarial accrued liability were \$31.3 billion and \$20.2 billion, respectively.

On September 9, 2004, the OPERS Retirement Board adopted a Health Care Preservation Plan (HCPP) with an effective date of January 1, 2007. The HCPP restructures OPERS' health care coverage to improve the financial solvency of the fund in response to increasing health care costs. Member and employer contribution rates increased as of January 1, 2006 and January 1, 2007, which will allow additional funds to be allocated to the health care plan.

***Police and Fire Disability and Pension Fund:*** The Ohio Police and Fire Pension Fund (OP&F) provides postretirement health care coverage to any person who receives or is eligible to receive a monthly service, disability or survivor benefit check or is a spouse or eligible dependent child of such person. An eligible dependent child is any child under the age of 18 whether or not the child is attending school, or under the age of 22 if attending school full-time or on a 2/3 basis.

The health care coverage provided by the retirement system is considered an Other Postemployment Benefit (OPEB) as described in *GASB Statement No. 12*. The Ohio Revised Code provides the authority allowing the Ohio Police and Fire Pension Fund's board of trustees to provide health care coverage and states that health care costs paid from the funds of OP&F shall be included in the employer's contribution rate. Health care funding and accounting is on a pay-as-you-go basis. The total police employer contribution rate is 19.5 percent of covered payroll and the total firefighter employer contribution rate is 24 percent of covered payroll, of which 7.75 percent of covered payroll was applied to the postemployment health care program during 2006 and 2005. In addition, since July 1, 1992, most retirees and survivors have been required to contribute a portion of the cost of their health care coverage through a deduction from their monthly benefit payment. Beginning in 2001, all retirees and survivors have monthly health care contributions.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006

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**11. POSTEMPLOYMENT BENEFITS (Continued)**

The City's actual contributions for 2006 that were used to fund postemployment health care benefits were \$60,006 for police and \$64,874 for firefighters. The OP&F's total health care expense for the year ended December 31, 2005, (the latest information available) was \$108,039,449, which was net of member contributions of \$55,271,881. The number of OP&F participants eligible to receive health care benefits as of December 31, 2005, was 13,922 for police and 10,537 for firefighters.

**12. RISK MANAGEMENT**

The Government is exposed to various risks of property and casualty losses, and injuries to employees.

The Government insures against injuries to employees through the Ohio Bureau of Worker's Compensation.

The Government belongs to the Public Entities Pool of Ohio (PEP), a risk-sharing pool available to Ohio local governments. PEP provides property and casualty coverage for its members. PEP is a member of the American Public Entity Excess Pool (APEEP). Member governments pay annual contributions to fund PEP. PEP pays judgments, settlements and other expenses resulting from covered claims that exceed the members' deductibles.

Casualty Coverage

For an occurrence prior to January 1, 2006 PEP retains casualty risks up to \$250,000 per occurrence, including claim adjustment expenses. PEP pays a percentage of its contributions to APEEP. APEEP reinsures claims exceeding \$250,000, up to \$1,750,000 per claim and \$10,000,000 in the aggregate per year. For an occurrence on or subsequent to January 1, 2006, the Pool retains casualty risk up to \$350,000 per occurrence, including loss adjustment expenses. Claims exceeding \$350,000 are reinsured with APEEP in an amount not to exceed \$2,650,000 for each claim and \$10,000,000 in the aggregate per year. Governments can elect up to \$10,000,000 in additional coverage with the General Reinsurance Corporation, through contracts with PEP.

If losses exhaust PEP's retained earnings, APEEP provides *excess of funds available* coverage up to \$5,000,000 per year, subject to a per-claim limit of \$2,000,000 (for claims prior to January 1, 2006) or \$3,000,000 (for claims on or after January 1, 2006) as noted above.

Property Coverage

Through 2004, PEP retained property risks, including automobile physical damage, up to \$100,000 on any specific loss in any one occurrence. The Travelers Indemnity Company reinsured losses exceeding \$100,000 up to \$500 million per occurrence.

Beginning in 2005, Travelers reinsures specific losses exceeding \$250,000 up to \$600 million per occurrence. APEEP reinsures members for specific losses exceeding \$100,000 up to \$250,000 per occurrence, subject to an annual aggregate loss payment. Travelers provides aggregate stop-loss coverage based upon the combined members' total insurable values. If the stop loss is reached by payment of losses between \$100,000 and \$250,000, Travelers will reinsure specific losses exceeding \$100,000 up to their \$600 million per occurrence limit. The aggregate stop-loss limit for 2006 was \$1,901,127.

The aforementioned casualty and property reinsurance agreements do not discharge PEP's primary liability for claims payments on covered losses. Claims exceeding coverage limits are the obligation of the respective government.

Property and casualty settlements did not exceed insurance coverage for the past three fiscal years.

**CITY OF HILLSBORO, OHIO**  
**NOTES TO THE BASIC FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED DECEMBER 31, 2006**

**12. RISK MANAGEMENT (Continued)**

Financial Position

PEP's financial statements (audited by other accountants) conform with generally accepted accounting principles, and reported the following assets, liabilities and retained earnings at December 31, 2006 and 2005.

<u>Casualty Coverage</u>	<u>2006</u>	<u>2005</u>
Assets	\$30,997,868	\$29,719,675
Liabilities	(15,875,741)	(15,994,168)
Retained earnings	<u>\$15,122,127</u>	<u>\$13,725,507</u>

<u>Property Coverage</u>	<u>2006</u>	<u>2005</u>
Assets	\$5,125,326	\$4,443,332
Liabilities	(863,163)	(1,068,245)
Retained earnings	<u>\$4,262,163</u>	<u>\$3,375,087</u>

At December 31, 2006 and 2005, respectively, casualty coverage liabilities noted above include approximately \$14.4 million and \$14.3 million of estimated incurred claims payable. The Casualty Coverage assets and retained earnings above also include approximately \$14.4 million and \$14.3 million of unpaid claims to be billed to approximately 447 member governments in the future, as of December 31, 2006 and 2005, respectively. These amounts will be included in future contributions from members when the related claims are due for payment. The Government's share of these unpaid claims collectible in future years is approximately \$206,352. This payable includes the subsequent year's contribution due if the Government terminates participation, as described in the last paragraph below.

Based on discussions with PEP, the expected rates PEP charges to compute member contributions, which are used to pay claims as they become due, are not expected to change significantly from those used to determine the historical contributions detailed below. By contract, the annual liability of each member is limited to the amount of financial contributions required to be made to PEP for each year of membership.

<u>Contributions to PEP</u>	
2004	\$85,372
2005	\$92,712
2006	\$103,176

After completing one year of membership, members may withdraw on each anniversary of the date they joined PEP provided they give written notice to PEP 60 days in advance of the anniversary date. Upon withdrawal, members are eligible for a full or partial refund of their capital contributions, minus the subsequent year's budgetary contribution. Withdrawing members have no other future obligation to the pool. Also upon withdrawal, payments for all casualty claims and claim expenses become the sole responsibility of the withdrawing member, regardless of whether a claim occurred or was reported prior to the withdrawal.

**CITY OF HILLSBORO, OHIO**  
NOTES TO THE BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2006

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**12. RISK MANAGEMENT (Continued)**

The City also maintains a blanket crime bond in the amount of \$2,500. In addition the City carries employee dishonesty coverage in the amount of \$242,000. The City pays all elected officials' bonds by statute. The City insures an employee health benefits program through United Healthcare Insurance Company.

Settlement claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three years.

The City has not incurred significant reductions in insurance coverage from coverage in prior year by major category risk.

**13. OTHER EMPLOYEE BENEFITS**

*Deferred Compensation:* Employees of the City may elect to participate in the ING Deferred Compensation Program created in accordance with Internal Revenue Code Section 457. Participation is on a voluntary payroll deduction basis. The plan permits deferral of compensation until future years. According to the plan, the deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency. Assets of the plan are held in trust for the exclusive benefit of the participants and their beneficiaries.

*Compensated Absences:* Vacation leave is earned at rates that vary depending upon length of service and standard work week. Current policy credits vacation on the employee's anniversary date and is to be taken by the next anniversary date. Vacation time is not cumulative and must be taken during the year unless otherwise specified. City employees are paid for earned, unused vacation leave at the time of termination of employment if the employee has at least one year of service.

The Police Department earns sick leave at a rate of 4.6 hours per completed eighty hours of active pay status. Those employees with not less than 10 years of service at retirement shall be paid the value of his/her sick leave credit for up to one-third of the leave up to a maximum of 400 hours upon termination. The Fire Department earns sick leave at a rate of 6.44 hours for each completed pay period. Those employees with not less than 10 years of service at retirement shall be paid the value of his/her sick leave credit for up to one-fourth of their leave balance. All other City employees earn sick leave at a rate of 4.6 hours per completed eighty hours of active pay status. Those employees with at least ten years of service at the time of separation shall be paid the value of his/her sick credit for up to one-fourth of the leave up to 300 hours. Such payment shall be based on the employee's rate of pay at the time of separation, or the full balance may be transferred to another governmental agency.

**CITY OF HILLSBORO, OHIO**  
**NOTES TO THE BASIC FINANCIAL STATEMENTS**  
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**14. CAPITAL ASSETS**

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

	Beginning Balance 12/31/2005*	Additions	Deletions	Ending Balance 12/31/2006
<u>Governmental Activities</u>				
Capital Assets, Not Being Depreciated				
Land	\$ 384,072	\$ -	\$ -	\$ 384,072
Construction in Progress	102,295	-	-	102,295
Total Capital Assets, Not Being Depreciated	<u>486,367</u>	<u>-</u>	<u>-</u>	<u>486,367</u>
Capital Assets Being Depreciated				
Land Improvements	2,024,132	-	-	2,024,132
Buildings and Improvements	1,567,064	71,446	-	1,638,510
Furniture and Equipment	1,343,080	173,406	(53,140)	1,463,346
Vehicles	1,615,178	219,671	(17,722)	1,817,127
Infrastructure	8,980,827	285,616	-	9,266,443
Total Capital Assets Being Depreciated	<u>15,530,281</u>	<u>750,139</u>	<u>(70,862)</u>	<u>16,209,558</u>
Less Accumulated Depreciation				
Land Improvements	(910,977)	(36,449)	-	(947,426)
Buildings and Improvements	(468,882)	(45,786)	-	(514,668)
Furniture and Equipment	(746,645)	(117,260)	50,058	(813,847)
Vehicles	(1,048,068)	(113,713)	17,043	(1,144,738)
Infrastructure	(3,060,281)	(188,448)	-	(3,248,729)
Total Accumulated Depreciation	<u>(6,234,853)</u>	<u>(501,656)</u>	<u>67,101</u>	<u>(6,669,408)</u>
Total Capital Assets Being Depreciated, Net	<u>9,295,428</u>	<u>248,483</u>	<u>(3,761)</u>	<u>9,540,150</u>
Governmental Activities Capital Assets, Net	<u>\$ 9,781,795</u>	<u>\$ 248,483</u>	<u>\$ (3,761)</u>	<u>\$ 10,026,517</u>

\* As restated see note 3.

**CITY OF HILLSBORO, OHIO**  
**NOTES TO THE BASIC FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED DECEMBER 31, 2006**

**14. CAPITAL ASSETS (Continued)**

Depreciation expense was charged to governmental functions as follows:

General Government:

Legislative and Executive	\$ 67,621
Security of Persons & Property	114,918
Public Health	28,686
Leisure Time Activities	34,244
Transportation	<u>256,187</u>
Total Depreciation Expense	<u>\$ 501,656</u>

	Ending Balance 12/31/2005*	Additions	Deletions	Ending Balance 12/31/2006
<u>Business Type Activities</u>				
Capital Assets, Not Being Depreciated				
Construction in Progress	\$ 1,611,366	\$1,472,296	\$ -	\$ 3,083,662
Total Capital Assets, Not Being Depreciated	<u>1,611,366</u>	<u>1,472,296</u>	<u>-</u>	<u>3,083,662</u>
Capital Assets Being Depreciated				
Land Improvements	273,604	-	-	273,604
Buildings and Equipment	12,746,472	26,539	(16,237)	12,756,774
Mechanical Equipment	877,179	139,389	(23,216)	993,352
Vehicles	156,601	23,844	-	180,445
Water/Sewer Lines	<u>5,283,169</u>	<u>223,741</u>	<u>(30,526)</u>	<u>5,476,384</u>
Total Capital Assets Being Depreciated	19,337,025	413,513	(69,979)	19,680,559
Less Accumulated Depreciation				
Land Improvements	(164,137)	(9,052)	-	(173,189)
Buildings and Equipment	(3,998,075)	(134,392)	8,138	(4,124,329)
Mechanical Equipment	(587,510)	(62,341)	27,266	(622,585)
Vehicles	(117,750)	(13,858)	-	(131,608)
Water/Sewer Lines	<u>(2,231,361)</u>	<u>(174,853)</u>	<u>17,936</u>	<u>(2,388,278)</u>
Total Accumulated Depreciation	(7,098,833)	(394,496)	53,340	(7,439,989)
Total Capital Assets Being Depreciated, Net	<u>12,238,192</u>	<u>19,017</u>	<u>(16,639)</u>	<u>12,240,570</u>
Business Type Activities Capital Assets, Net	<u>\$13,849,558</u>	<u>\$1,491,313</u>	<u>\$ (16,639)</u>	<u>\$ 15,324,232</u>

\* As restated see note 3.

**CITY OF HILLSBORO, OHIO**  
**NOTES TO THE BASIC FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED DECEMBER 31, 2006**

**15. LONG-TERM OBLIGATIONS**

The City's long-term obligations at year end consisted of the following:

	Outstanding 12/31/2005	Issued	Retired	Outstanding 12/31/2006	Due In One Year
<b><i>Governmental Activities</i></b>					
Compensated Absences	\$ 268,622	\$ 364,755	\$ 268,622	\$ 364,755	\$ 19,687
1997 - 6.5% Street Improvement Bonds	100,000	-	50,000	50,000	50,000
Capital Lease	66,883	-	32,617	34,266	34,266
<b>Total Governmental Activities</b>	<b>\$ 435,505</b>	<b>\$ 364,755</b>	<b>\$ 351,239</b>	<b>\$ 449,021</b>	<b>\$ 103,953</b>
	Outstanding 12/31/2005	Issued	Retired	Outstanding 12/31/2006	Due In One Year
<b><i>Business Activities</i></b>					
Compensated Absences	\$ 49,337	\$ 74,546	\$ 49,337	\$ 74,546	\$ -
<b>Water</b>					
2004 - 2% Mortgage Revenue Bond	3,175,333	-	75,000	3,100,333	75,000
2005 - Water System Improvement Revenue Bonds - 4.25%	560,000	-	6,000	554,000	5,000
2005 - Water System Improvement Revenue Bonds - 4.25%	2,400,000	-	24,000	2,376,000	25,000
Unamortized Charge	95,834	-	3,833	92,001	3,833
<b>Total Water Fund</b>	<b>6,231,167</b>	<b>-</b>	<b>108,833</b>	<b>6,122,334</b>	<b>108,833</b>
<b>Sewer</b>					
2004 - OWDA Loan - 1%	389,700	-	22,194	367,506	11,180
2005 - OWDA Loan - 1%	427,890	911,399	63,161	1,276,128	31,713
1997 - 4.65% Mortgage Revenue Bond	810,000	-	255,000	555,000	270,000
<b>Total Sewer Fund</b>	<b>1,627,590</b>	<b>911,399</b>	<b>340,355</b>	<b>2,198,634</b>	<b>312,893</b>
<b>Total Business-Type Activities</b>	<b>\$ 7,908,094</b>	<b>\$ 985,945</b>	<b>\$ 498,525</b>	<b>\$ 8,395,514</b>	<b>\$ 421,726</b>

Mortgage revenue bonds were issued for payment of water system improvements, construction of a 150,000,000 gallon reservoir, and a water storage tank. Properties and revenues of the utility facilities have been pledged to repay these debts. Mortgage revenue bonds in the amount of \$3,385,000 were issued in 2004 to refund water mortgage revenue bonds of \$3,281,500 issued in 1991. Property and revenue of the utility facilities have been pledged to repay these debts.

**CITY OF HILLSBORO, OHIO**  
**NOTES TO THE BASIC FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED DECEMBER 31, 2006**

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**15. LONG-TERM OBLIGATIONS (Continued)**

Mortgage revenue bonds in the amount of \$560,000 and \$2,400,000 were issued in 2005 to improve the water system of the City. Property and revenue of the utility facilities have been pledged to repay these debts.

Compensated Absences (sick leave and vacation benefits) will be paid from the General Fund, Street Special Revenue Fund, and Sewer and Electric Enterprise Funds. Capital lease obligations will be paid from the fund that maintains custody of the related asset.

The 1997 Mortgage Revenue Bonds were issued in the amount of \$2,510,000. These bonds are special obligations of the City, payable solely from the net revenues of its wastewater treatment and sewer system and the revenue fund created under the trust indenture.

The Street Improvement Bonds in the amount of \$400,000 were issued for the improvement of city streets. General obligation bonds are direct obligations of the City for which its full faith, credit and resources are pledged and are payable from taxes levied on all taxable property in the City. Property tax monies will be received in and the debt will be repaid from a General Obligation Bond Retirement Fund.

The 2004 OWDA loan was issued at an interest rate of 1% during 2004 and 2005 to pay for the costs of sanitary sewer lining. The 2005 OWDA loan is to pay for the costs of lift station, equalization basin, and relief sewers. The sewer fund will be used to repay these loans.

Principal and interest requirements to retire Mortgage Revenue Bonds at December 31, 2006 were as follows:

	<u>Mortgage Revenue Bonds</u>	
	<u>Principal</u>	<u>Interest</u>
2007	\$375,000	\$288,204
2008	396,000	271,517
2009	114,000	260,252
2010	120,000	255,866
2011	121,000	251,244
2012-2016	695,000	1,175,872
2017-2021	853,000	1,013,452
2022-2026	1,061,000	799,881
2027-2031	1,338,000	516,884
2032-2036	471,000	304,547
2037-2041	581,000	195,211
2042-2045	560,000	60,724
Total	<u>\$6,685,000</u>	<u>\$5,393,654</u>

The amortization schedule does not match the outstanding debt amounts listed on page 47 in the amount of \$92,001 which is the unamortized charge.

The OWDA loans were still open as of December 31, 2006 and no amortization schedules had been established for these loans.

**CITY OF HILLSBORO, OHIO**  
**NOTES TO THE BASIC FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED DECEMBER 31, 2006**

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**15. LONG-TERM DEBT OBLIGATIONS (Continued)**

Principal and interest requirements to retire General Obligation Bonds at December 31, 2006 were as follows:

	<u>General Obligation Bonds</u>	
	<u>Principal</u>	<u>Interest</u>
2007	<u>50,000</u>	<u>2,375</u>
Total	<u><u>\$50,000</u></u>	<u><u>\$2,375</u></u>

The City's overall legal debt margin was \$3,109,966 at December 31, 2006.

**16. CONTINGENCIES**

Grants

The City received financial assistance from federal and state agencies in the form of grants. The expenditure of funds received under these programs generally requires compliance with terms and conditions specified in the grant agreements and is subject to audit by the grantor agencies. Any disallowed claims resulting from such audits could become liability of the General Fund or other applicable funds. However, in the opinion of management, any such disallowed claims will not have a material adverse effect on the overall financial position of the City at December 31, 2006.

Litigation

The City is currently party to legal proceedings. The City's management is of the opinion that ultimate disposition of claims will not have a material effect, if any, on the financial condition of the City.

**17. ACCOUNTABILITY**

The following fund had a fund balance deficit as of December 31, 2006:

<u>Capital Project Fund</u>	
Tax Increment Fund	292,151

This deficit is a result of the application of accounting principles generally accepted in the United States of America to the financial reporting of these funds. The General Fund is liable for any deficit in this fund and provides operating transfers when cash is required, not when accruals occur.

**CITY OF HILLSBORO, OHIO**  
**NOTES TO THE BASIC FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED DECEMBER 31, 2006**

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**18. CAPITALIZED LEASES - LESSEE DISCLOSURE**

During fiscal year 2005, the City entered into a capital lease for the purchase of a Ford Explorer and two police cruisers. In a previous fiscal year, the City entered into a capitalized lease for the acquisition of a backhoe. The terms of the agreements provide options to purchase the equipment. The leases meet the criteria of a capital lease as defined by Statement of Financial Accounting Standards No. 13 *Accounting for Leases*, which defines a capital lease generally as one which transfers benefits and risks of ownership to the lessee. Capital lease payments have been reclassified and are reflected as debt service in the Basic Financial Statements for the street fund. These expenditures are reflected as program/object expenditures on a budgetary basis.

The capital assets acquired by the leases have been capitalized in the statement of net assets for governmental activities in the amount of \$113,718 which is equal to the present value of the minimum lease payments at the time of acquisition. A corresponding liability was recorded on the statement of net assets for governmental activities. Principal payments in fiscal year 2006 totaled \$32,617 in the governmental funds.

The following is a schedule of the future minimum lease payments required under the capital leases and the present value of the minimum lease payments as of December 31, 2006.

<u>Year Ending</u> <u>December 31,</u> 2007	<u>Capitalized</u> <u>Lease</u> <u>Obligation</u>
Total Minimum Lease Payments	35,999
Less: Amount Representing Interest	(1,733)
Present Value of Minimum Lease Payments	\$34,266

**19. DONATED STOCK**

On October 23, 2003, the City received a donation of Proctor and Gamble Stock to be used for Life Squad improvements and related equipment. The market value of this stock at the time of donation was \$3,235. An investment firm holds the City's stock in book entry form in the City's name.

**20. RELATED PARTY TRANSACTION**

The City currently has an existing revolving loan with the Southern Ohio Economic Development Corporation (SOEDC), of which Dan Cowdrey is the current President. Dan Cowdrey is also under contract as the City's Loan Administrator for the City of Hillsboro, Revolving Loan Fund Committee (RLFC). However, at the time the loan was originated in 2001, Dan Cowdrey was not the President of the SOEDC.

**CITY OF HILLSBORO  
HIGHLAND COUNTY**

**FEDERAL AWARDS EXPENDITURES SCHEDULE  
FOR THE YEAR ENDED DECEMBER 31, 2006**

<b>FEDERAL GRANTOR</b> <i>Pass Through Grantor</i> Program Title	Pass Through Entity Number	Federal CFDA Number	Disbursements
<b><u>U.S. DEPARTMENT OF AGRICULTURE</u></b>			
<i>Direct from the Federal Government</i>			
Water & Waste Disposal Systems for Rural Communities	N/A	10.760	\$56,030
Total U.S. Department of Agriculture			<b><u>56,030</u></b>
<b><u>U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT</u></b>			
<i>Passed Through Ohio Department of Development</i>			
Community Development Block Grant			
Community Housing Improvement Program	A-C-06-131-1	14.228	91,105
Community Housing Improvement Program	A-C-04-131-1		20,345
Water and Sanitary Sewer Competitive Grant Program	A-W-04-131-1		500,000
			<u>611,450</u>
Home Investment Partnership Program			
Community Housing Improvement Program	A-C-06-131-2	14.239	37,243
Community Housing Improvement Program	A-C-04-131-2		102,827
			<u>140,070</u>
Total U.S. Department of Housing and Urban Development			<b><u>751,520</u></b>
<b><u>U.S. DEPARTMENT OF JUSTICE</u></b>			
<i>Passed Through Governor's Office of Criminal Justice Services</i>			
Victim-Witness/VOCA	2006VAGANE487	16.588	3,859
Victim-Witness/VOCA	2005VAGANE487		17,440
Total U.S. Department of Justice			<b><u>21,299</u></b>
<b><u>U.S. DEPARTMENT OF HOMELAND SECURITY</u></b>			
<i>Passed through Ohio Office of Criminal Justice Services</i>			
Technology Improvement	2005-GL-OIB-9261	97.074	15,241
Total U. S. Department of Homeland Security			<b><u>15,241</u></b>
<b>Total Federal Expenditures</b>			<b><u><u>\$844,090</u></u></b>

**CITY OF HILLSBORO, OHIO  
HIGHLAND COUNTY**

**NOTES TO THE FEDERAL AWARDS EXPENDITURES SCHEDULE  
FISCAL YEAR ENDED DECEMBER 31, 2006**

**NOTE A - SIGNIFICANT ACCOUNTING POLICIES**

The accompanying Federal Awards Expenditures Schedule (the Schedule) summarizes activity of the City's federal award programs. The schedule has been prepared on the cash basis of accounting.



# Mary Taylor, CPA

Auditor of State

## INDEPENDENT ACCOUNTANTS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS REQUIRED BY *GOVERNMENT AUDITING STANDARDS*

City of Hillsboro  
Highland County  
130 North Street  
Hillsboro, Ohio 45133

To the Member of Council:

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hillsboro, Highland County, Ohio (the City), as of and for the year ended December 31, 2006, which collectively comprise the City's basic financial statements and have issued our report thereon dated November 20, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the Comptroller General of the United States' *Government Auditing Standards*.

### **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 audit procedures for expressing our opinions on the financial statements, but not to opine on the effectiveness of the City's internal control over financial reporting. Accordingly, we have not opined on the effectiveness of the City's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the City's ability to initiate, authorize, record, process, or report financial data reliably in accordance with its applicable accounting basis, such that there is more than a remote likelihood that the City's internal control will not prevent or detect a more-than-inconsequential financial statement misstatement.

We consider the following deficiencies described in the accompanying schedule of findings to be significant deficiencies in internal control over financial reporting: 2006-001 through 2006-006.

A material weakness is a significant deficiency, or combination of significant deficiencies resulting in more than a remote likelihood that the City's internal control will not prevent or detect a material financial statement misstatement.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and accordingly, would not necessarily disclose all significant deficiencies that are also material weaknesses. However, of the significant deficiencies described above, we believe finding number 2006-004 is also a material weakness.

We also noted certain internal control matters that we reported to the City's management in a separate letter dated November 20, 2007.

### **Compliance and Other Matters**

As part of reasonably assuring whether the City's financial statements are free of material misstatement, we tested its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could directly and materially affect 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 an opinion. The results of our tests disclosed instances of noncompliance or other matters that we must report under *Government Auditing Standards* which are described in the accompanying schedule of findings as items 2006-001 and 2006-003.

We also noted certain noncompliance or other matters not requiring inclusion in this report that we reported to the City's management in a separate letter dated November 20, 2007.

The City's responses to the findings identified in our audit are described in the accompanying schedule of findings. We did not audit the City's responses and, accordingly, we express no opinion on them.

We intend this report solely for the information and use of the management, City Council and federal awarding agencies and pass-through entities. We intend it for no one other than these specified parties.



**Mary Taylor, CPA**  
Auditor of State

November 20, 2007



# Mary Taylor, CPA

## Auditor of State

### INDEPENDENT ACCOUNTANTS' REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR FEDERAL PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

City of Hillsboro  
Highland County  
130 North High Street  
Hillsboro, Ohio 45133

To the Members of Council:

#### Compliance

We have audited the compliance of the City of Hillsboro, Highland County, Ohio (the City), with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133, Compliance Supplement* that apply to its major federal program for the year ended December 31, 2006. The summary of auditor's results section of the accompanying schedule of findings identifies the City's major federal program. The City's management is responsible for complying with the requirements of laws, regulations, contracts, and grants applicable to each major federal program. 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 reasonably assure whether noncompliance occurred with the types of compliance requirements referred to above that could directly and materially affect a major federal program. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing other procedures we considered necessary in the circumstances. We believe 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 of Hillsboro, Highland County, Ohio complied, in all material respects, with the requirements referred to above that apply to its major federal program for the year ended December 31, 2006.

#### Internal Control Over Compliance

The City's management 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 requirements that could directly and materially affect a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, 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 *control deficiency* in internal control over compliance exists when the design or operation of a control does not allow management or employees, when performing their assigned functions, to prevent or detect noncompliance with a federal program compliance requirement on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that the entity's internal control will not prevent or detect more-than-inconsequential noncompliance with a federal program compliance requirement.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that the City's internal control will not prevent or detect material noncompliance with a federal program's compliance requirements.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be 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. However, we noted a matter involving the internal control over federal compliance not requiring inclusion in this report, that we reported to the City's management in a separate letter dated November 20, 2007.

We intend this report solely for the information and use of the management, City Council, federal awarding agencies, and pass-through entities. It is not intended for anyone other than these specified parties.



**Mary Taylor, CPA**  
Auditor of State

November 20, 2007

**CITY OF HILLSBORO  
HIGHLAND COUNTY**

**SCHEDULE OF FINDINGS  
OMB CIRCULAR A -133 § .505  
DECEMBER 31, 2006**

**1. SUMMARY OF AUDITOR'S RESULTS**

<i>(d)(1)(i)</i>	Type of Financial Statement Opinion	Unqualified
<i>(d)(1)(ii)</i>	Were there any material control weaknesses reported at the financial statement level (GAGAS)?	Yes
<i>(d)(1)(ii)</i>	Were there any other significant deficiencies in internal control reported at the financial statement level (GAGAS)?	Yes
<i>(d)(1)(iii)</i>	Was there any reported material noncompliance at the financial statement level (GAGAS)?	Yes
<i>(d)(1)(iv)</i>	Were there any material internal control weaknesses reported for major federal programs?	No
<i>(d)(1)(iv)</i>	Were there any other significant deficiencies in internal control reported for major federal programs?	No
<i>(d)(1)(v)</i>	Type of Major Programs' Compliance Opinion	Unqualified
<i>(d)(1)(vi)</i>	Are there any reportable findings under § .510?	No
<i>(d)(1)(vii)</i>	Major Programs (list):	CFDA # 14.228; Community Development Block grants.
<i>(d)(1)(viii)</i>	Dollar Threshold: Type A/B Programs	Type A: > \$ 300,000 Type B: all others
<i>(d)(1)(ix)</i>	Low Risk Auditee?	No

**2. FINDINGS RELATED TO THE FINANCIAL STATEMENTS  
REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS**

**FINDING NUMBER 2006-001**

**Noncompliance and Significant Deficiency**

**Ohio Rev. Code, Section 5705.10(D)** requires, in part all revenue derived from a source other than the general property tax and which the law prescribes shall be used for a particular purpose is to be paid into a special fund for such purpose.

During the conversion process, the City incorrectly posted several receipts to the financial statements. The City agreed with the following adjustments which they made to the accompanying financial statements.

**FINDING NUMBER 2006-001  
 (Continued)**

	<b>Intergovernmental</b>	<b>Taxes</b>	<b>Licenses and Permits</b>
Intergovernmental Receipts were posted incorrectly.	\$341,267	(\$330,407)	(\$10,861)

	<b>Intergovernmental</b>	<b>Taxes</b>	<b>Other Receipts</b>
Intergovernmental Receipts were posted incorrectly.	\$15,421	(\$63,000)	\$47,579

Failure to properly record all transactions reduces internal control over receipts and disbursements and increases the risk that misappropriation, errors or loss of public funds will not be detected in a timely manner. To improve internal control and accountability we recommend that the City Auditor post receipts correctly. We also recommend that the City Auditor review the statements received from the Independent Accountants performing the GAAP conversion to determine amounts are correctly taken to the financial statements.

**Officials' Response:**

City Auditor Gary Lewis responded as follows:

"In response to various findings in your Audit Report, please be advised of the following:

The City had correctly posted their receipts; however, during the GAAP conversion process the IPA reversed several of the postings. We will address this issue by providing to the IPA a copy of our audit report and management letter and we will aggressively pursue remedies that will prevent this from happening in the future."

**FINDING NUMBER 2006-002**

**Significant Deficiency**

Accurate and timely accounting and reconciliation procedures are key components of an effective accounting system and internal controls required to enable the Clerk of Courts to properly classify transactions, maintain accountability for funds, distribute funds accurately, and detect fraud and errors in a timely manner.

We noted the following deficiencies for the 2006 audit period over the Traffic/Criminal Account of the Municipal Court:

- Monthly reconciliations were not performed for the Traffic/Criminal Account of the Municipal Court for all of 2006. The balance in the Traffic/Criminal account could not be completely reconciled to the accounting records due to the lack of reconciliations and the significant activity in the accounts. Additional audit hours were needed to prepare a reconciliation for this account. A variance of \$159 was noted between the accounting records and auditor prepared reconciliation. Without reconciling monthly, the controls over the Court are greatly diminished and the controls of the accuracy of the accounting records are weakened.

**FINDING NUMBER 2006-002  
(Continued)**

- Duplicated receipt numbers were issued by the Court as evidenced by more than one case being found on the Courts computerized system for the same receipt number. Deposit or receipt information could be lost or incorrectly posted if duplicated receipts exist on the Courts system. Avoiding duplication of receipt numbers will help assure the Courts that the information recorded on the computerized system is complete and accurate for each receipt posted.
- Duplicate ticket books have been issued by the Court to the City Police Department as evidenced by more than one case being filed under the same ticket number. Critical information could be lost or incorrectly posted to the wrong defendant if duplicate tickets exist on the Court's system. Avoiding duplication of ticket numbers will help assure the Courts that the information recorded on the computerized system is complete and accurate for each citation issued.

We recommend that the Clerk of Courts prepare an accurate, timely written reconciliation between the bank and the accounting records on a monthly basis. Also, all receipt books and ticket books should be used in sequential order with no duplication of receipt and ticket numbers.

**Officials' Response:**

Judge David McKenna responded as follows:

"Please include the following response with the final audit report regarding finding number 2006-002 for the Hillsboro Municipal Court.

1. Reconciliations for the Traffic/Criminal Account have now been completed for 2006. This problem is related to changes in personnel in 2006 and monthly reconciliation is now being addressed.
2. Duplicate receipt numbers were identified as an issue of re-numbering receipts at the beginning of each year. The problem has been reviewed with Henschen and Associates to modify the accounting software to eliminate this problem for 2008. An internal check has not identified any duplicate receipts issued for 2007.
3. Duplicate traffic tickets are traceable to 1998 when tickets were re-numbered. It appears that Hillsboro Police issued a ticket in 2006 with a number used in 1996. Both tickets received their own case numbers and have remained separate in Court records. A review with the Hillsboro Police Department to inventory numbers of tickets in their possession and to reconcile with the clerk of courts records is scheduled. This should eliminate this problem in the future."

**FINDING NUMBER 2006-003**

**Noncompliance and Significant Deficiency**

Per **Ohio Revised Code, Section 705.08**, the treasurer shall be the custodian of all moneys of the municipal corporation, and shall keep the moneys in such manner and in such place as is determined by the legislative authority thereof. He shall pay out money only on warrants issued by the auditor.

Contrary to the above ORC Section, the City of Hillsboro's Elected Treasurer does not act as the custodian of all monies of the City. The Treasurer performs no accounting functions for the City. The City Auditor performs all cash reconciliations and accounts for City's investments.

**FINDING NUMBER 2006-003  
(Continued)**

Separating the duties of the Auditor and Treasurer keeps duties segregated and is an excellent form of protection from fraud or abuse. The lack of participation of the Treasurer in the accounting functions of the City greatly weakens the adequacy of the internal controls in place at the City.

We recommend that the Treasurer properly perform their duties as enumerated in the Ohio Revised Code, including accounting for City investments and performing monthly reconciliations.

**Officials' Response:**

City Auditor Gary Lewis responded as follows:

"With the election of a new treasurer, who will take office in 2008, the deficiencies as noted in this finding will be addressed in the following manner:

1. The treasurer will make all manual deposits on a daily basis.
2. The treasurer will maintain a record of all deposits for the city. On a monthly basis the treasurer will reconcile his deposit records with those of the auditor to check for accuracy.
3. The treasurer will review all warrants issued by the auditor prior to signing.
4. On a monthly basis the treasurer will review account reconciliations performed by the auditor prior to balancing and closing the prior month's books. He shall then sign off on each account after it has been balanced.
5. The treasurer also acts as the chairperson of the investment advisory committee consisting of the treasurer, auditor, mayor and the law director. He shall have no fewer than two meetings per year.

It should be noted that the treasurer in 2007 was appointed to the position in 2006 and that she had merely carried on with the policies of previous treasurers. Had she been elected to the position, she intended to follow the duties of treasurer as prescribed by ORC Section 705.08."

**FINDING NUMBER 2006-004**

**Material Weakness**

Policies and procedures are essential to monitor loan repayments and ensure independence of those involved in the revolving loan program. The City of Hillsboro, Revolving Loan Fund Committee (RLFC) has contracted with a third party to serve as Loan Administrator; however, as fiduciary agent for the revolving loan program, the City has a responsibility to oversee all aspects of the revolving loan program.

**FINDING NUMBER 2006-004  
(Continued)**

We noted the following deficiencies for the 2006 audit period over the City's revolving loan program:

- Loan repayments required by the agreements were not made for certain loans.
- Files did not always contain necessary information and the City did not collect payments on several loans. No action was shown on the city's part to collect the outstanding monies.
- Several "interest only" payments were accepted that were not in accordance with the loan agreements, and the City did not document a modification of the loan terms.
- No original agreement was found for CDBG or UDAG loans.
- Minutes for the Revolving Loan committee were not presented for audit.
- The administrator, Dan Cowdrey, the City hired to administer the loans also has a loan in his business' name (SOEDC) that has not been paid on since April 2003. He is the only one to monitor this account. He is paid \$15/hour not to exceed \$8,400 per year by the City. The City also pays SOEDC for office expenses relating to the Revolving Loan. There is no written contract stating that the City is to pay the expenses for SOEDC.
- Kenneth Captain, a board member, recently received an UDAG loan for the purchase of a mower for his mowing business. He did abstain from all voting.
- The City files and the Administrator's files are not reconciled.
- Duplicate receipts are not issued to individuals upon payment of loans.

Without adequate monitoring and oversight of the revolving loan program, the risk of loss or misappropriation of City funds is greatly increased. To reduce the risk of undetected errors and omissions occurring which could result in a loss of assets, we recommend the following procedures:

- The RLFC should regularly review each individual revolving loan file to ensure that accurate accounting records are being maintained.
- The RLFC should regularly review each individual revolving loan file to ensure that payments are being made timely and agree to the original loan agreements.
- The RLFC should regularly review all outstanding balances and determine that steps are being taken to actively collect past due amounts and that these steps are documented in each individual file.
- The RLFC should document minutes of their meetings and provide these to City management on a timely basis. Management should document their review of these minutes.
- The Loan Administrator and the City Auditor should regularly reconcile their records to determine that all amounts are accurately accounted for.
- The City should obtain the original grant agreements that provided the funding for the revolving loan program and keep these agreements on file.
- The Loan Administrator should issue duplicate receipts for all loan payments received.

**FINDING NUMBER 2006-004  
(Continued)**

- We recommend the City consult with their legal counsel to review the requirements of Revised Code Sections 2921.42 and 102.03 to ensure that all public officials and employees are transacting City business in accordance with Ohio Ethics Laws.

These procedures will help assure that all loans are independent, properly monitored, properly documented and accounted for in the City's accounting records.

**Officials' Response:**

Mayor Richard Zink responded as follows:

"In reference to Finding Number 2006-004, the following actions have been taken as a result of your Auditor Report:

- The City Administration has sought legal opinion from the City Law Director as a result of the allegation as set forth in the finding and subsequent Noncompliance Citation.
- Mr. Cowdrey was asked to tender his resignation effective immediate in lieu of direct termination by the appointing authority. Mr. Cowdrey elected to resign his position as the Revolving Loan Fund Administrator effective immediately.
- Kenneth Captain, one of the board members was also asked to convey his resignation in light of the recent audit and subsequent citation as a result of the UDAG loan that was taken out during his tenure as a Board Member. Mr. Captain tendered his resignation from the board.
- . . . this matter has been forwarded to the Hillsboro Police Department for investigation and prosecution should Probable Cause be found to substantiate the allegations as outlined in your report.
- My office is currently preparing an RFQ/RFP for the position of Revolving Loan Fund Administrator to fill the vacancy as evidenced by the above resignation. Once filled, due diligence will be exercised to ensure that proper record keeping and reconciliations occur by and between the Revolving Loan Administrator and the City Auditor. We will require that the new Revolving Loan Administrator provide a report that will outline the activities of each loan for the reporting period subject of the report. Any discrepancies will be addressed in a timely manner.
- Steps will be taken to address the lack of duplicate receipts and will enact procedures that will provide for receipt duplication for accountability.
- All documents and files pertaining to the Revolving Loan Fund will be moved from their current location of 135 N. High Street to the City Administration Building, located at 130 N. High Street forthwith. The relocating of these files will ensure that they are properly safeguarded in a secure, security monitored environment."

## FINDING NUMBER 2006-005

### Significant Deficiency

Organizations that use service organizations to process certain transactions should gain assurance that the service organization has controls in place and operating effectively to reduce the risk that transactions are not processed correctly.

During the 2005 fiscal year, the City of Hillsboro Fire and Rescue (HFD) entered into an agreement with HealthServe, LLC to receive, use, obtain, access or create Protected Health Information from or on behalf of HFD in the course of providing services. HealthServe, LLC service includes claims processing and payment posting for emergency medical service customers served by the HFD which is a significant accounting function for the City. The City of Hillsboro (City) has not established procedures to determine whether the service organization, HealthServe, LLC, has sufficient controls in place and operating effectively to ensure that emergency medical service claims processed on behalf of the HFD have been completely and accurately processed in accordance with their service contract.

HealthServe, LLC obtained a Tier I SAS 70 report "Independent Service Auditor's Report Provided by Service Auditor" dated June 30, 2005. However, a Tier I SAS 70 report is of limited benefit to the City because it only provides assurance that: 1) the description of the controls are fairly described; 2) that the controls are suitably designed to meet control objectives specified in the description; and 3) that the controls are in place and operating as of the opinion date. A Tier I SAS 70 report provides no opinion on the operating effectiveness of the controls.

A failure by the City to ensure, on an on-going basis, that emergency medical service claims processed on behalf of the HFD are completely and accurately processed in accordance with their specific service contract could result in the City incurring emergency medical service charges that are not billed or collected, thus resulting in lost revenues.

The City should implement procedures to assure the completeness, and accuracy of emergency medical service claims processed by its third party administrator. Statement on Auditing Standards (SAS) No. 70, as amended, prescribes standards for reporting on the processing (i.e. control design and operation) of transactions by service organizations. An unqualified Tier II "Report on Policies and Procedures Placed in Operation and Tests of Operating Effectiveness" in accordance with SAS No. 70 should provide the City with an appropriate level of assurance that emergency medical service claims are being processed in conformance with the contract.

We recommend that the City work with HealthServe, LLC to specify in their contract that an annual Tier II SAS 70 audit report be performed. The City should be provided a copy of the Tier II SAS 70 report in a timely manner and should review the report's content. A SAS 70 audit report should be conducted in accordance with American Institute of Certified Public Accountants' (AICPA) standards by a firm registered and considered in "good standing" with the Accountancy Board of the respective State. If the third-party administrator refuses to provide the City with a Tier II SAS 70 report, we recommend that the City only contract with a third-party administrator that will provide such a report. If HealthServe, LLC provides a Tier II SAS 70 report, we recommend that the City establish procedures to review on a monthly basis a Run Activity Report and the Fee and Receipt Analysis Report to ensure all runs have completely and accurately processed for billing, and that all collected receipts have been deposited to the City's bank account.

In the absence of a Tier II SAS 70 audit report, the District should establish procedures to strictly monitor claims processed by HealthServe, LLC to ensure that all emergency medical run claims were processed and collected in accordance with the contract. The claims information received, used, obtained, access or created by HealthServe, LLC on behalf of the HFD should be considered confidential and should be used by the City in compliance with the Health Insurance Portability and Accountability Act.

**FINDING NUMBER 2006-005  
(Continued)**

**Officials' Response:**

We did not receive a response from Officials to this finding.

**FINDING NUMBER 2006-006**

**Significant Deficiency**

Accurate and timely accounting and reconciliation procedures are key components of an effective accounting system and internal controls required to enable the Emergency Medical Services (EMS) to properly classify transactions, maintain accountability for funds, distribute funds accurately, and detect fraud and errors in a timely manner.

We noted the following deficiencies for the 2006 audit period over the emergency medical services:

- A reconciliation of monthly deposits of emergency medical services billing receipts to the receipt summary report from the third party billing service is not being performed.
- A reconciliation of run reports prepared by the emergency medical service personnel is not being reconciled to the billing reports from the third party billing service.

Without complete and timely reconciliation of emergency medical services provided, to the information entered and processed for billing, could result in services being provided which are not being billed, or not being billed at the appropriate rate. To reduce the risk of undetected errors and omissions occurring which could result in a negative fund balance situation, we recommend the following procedures:

- The Consolidated Reports from the 911 dispatch system which are faxed to the fire department after each run should be attached to the run report from the Firehouse Software system after entry.
- The Fire Chief should verify that all runs have been completely and accurately entered into the *Firehouse Software* system and have been processed for billing by matching the run reports to the monthly *EMS Run Activity Reports* from HealthServe, LLC.
- The City Auditor should reconcile the direct deposit amounts from the Lockbox Account to the monthly net receipts from the *Monthly Executive Summary Report* from HealthServe, LLC.

These procedures will help assure that all emergency medical service runs have been entered for processing, have been entered completely and accurately, have been downloaded to the third party billing service for processing, and that all receipts collected from billings are being received.

**Officials' Response:**

City Auditor Gary Lewis responded as follows:

"While the contract with HealthServe LLC (now known as Med3000) is the responsibility of the City Administration, it should be noted that the procedures recommended in the absence of a Tier II SAS 70 report was reviewed with the fire chief in February 2007 and implementation was recommended. The Auditor has reconciled the direct deposit amounts from the lockbox account to the monthly net reports from the Monthly Executive Summary Report for 2007."

**FINDING NUMBER 2006-006  
(Continued)**

Mayor Richard Zink responded as follows:

“The Consolidation Reports from the 911 dispatch system will be filed with the FireHouse run number affixed in a manner as to allow for monthly reconciliation with HealthServe LLC, nka Med 3000. Med 3000 allows access to all billing activity via their Web enabled Internet Portal. Said reconciliation can be conducted by both the City Auditor and the Fire Chief. I am directing my Fire Chief to complete a reconciliation report no less frequent than once per calendar month. Once completed, the Fire Chief shall reconcile his reports with that of the City Auditor in order to ensure consistent and accurate billing of EMS services.”

<b>3. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARDS</b>
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**None.**

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**CITY OF HILLSBORO  
HIGHLAND COUNTY**

**SCHEDULE OF PRIOR AUDIT FINDINGS  
OMB CIRCULAR A -133 § .315 (b)  
DECEMBER 31, 2006**

Finding Number	Finding Summary	Fully Corrected?	Not Corrected, Partially Corrected; Significantly Different Corrective Action Taken; or Finding No Longer Valid; <b><i>Explain</i></b>
2005-001	Entity did not obtain a SAS 70 report for HealthServe, LLC for their service of claims processing and payment posting for emergency medical service customers.	No	Repeated as Finding 2006-005
2005-002	ORC Section 5705.39 appropriations exceeding estimated resources.	No	Partially corrected, moved to management letter.





**Mary Taylor, CPA**  
Auditor of State

**CITY OF HILLSBORO**

**HIGHLAND COUNTY**

**CLERK'S CERTIFICATION**

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

*Susan Babbitt*

**CLERK OF THE BUREAU**

**CERTIFIED  
JANUARY 3, 2008**