



**Auditor of State
Betty Montgomery**

**CITY OF EAST PALESTINE
COLUMBIANA COUNTY**

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Auditor of State Betty Montgomery

INDEPENDENT ACCOUNTANTS' REPORT

City of East Palestine
Columbiana County
82 Garfield Avenue
East Palestine, Ohio 44413

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 East Palestine, Columbiana County, Ohio (the City), as of and for the year ended December 31, 2004, 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 East Palestine, Columbiana County, Ohio, as of December 31, 2004, and the respective changes in financial position and cash flows, where applicable, thereof and the respective budgetary comparisons for the General and Electric Trust funds 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 August 23, 2005, 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.

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

Betty Montgomery
Auditor of State

August 23, 2005

CITY OF EAST PALESTINE, OHIO

***Management's Discussion and Analysis
For the Year Ended December 31, 2004***

Unaudited

The discussion and analysis of the City of East Palestine's financial performance provides an overall review of the City's financial activities for the fiscal year ended December 31, 2004. The intent of this discussion and analysis is to look at the City's financial performance as a whole; readers should also review the notes to the basic financial statements and financial statements to enhance their understanding of the City's financial performance.

FINANCIAL HIGHLIGHTS

Key financial highlights for 2004 are as follows:

- ❑ In total, net assets decreased \$262,331. Net assets of governmental activities decreased \$358,036 which represents a 8% decrease from 2003. Net assets of business-type activities increased \$95,705 or 6% from 2003.
- ❑ General revenues accounted for \$1,453,685 in revenue or 36% of all revenues. Program specific revenues in the form of charges for services and grants and contributions accounted for \$2,548,722, 64% of total revenues of \$4,002,407.
- ❑ The City had \$2,695,352 in expenses related to governmental activities; only \$1,074,858 of these expenses were offset by program specific charges for services, grants or contributions. General revenues of \$1,262,458 were not adequate to provide for these programs.
- ❑ Among major funds, the general fund had \$1,741,489 in revenues and other financing sources and \$1,738,806 in expenditures and other financing uses. The general fund's fund balance increased from a deficit of \$531,233 to a deficit of \$528,550.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of two parts – *management's discussion and analysis* and the *basic financial statements*. The basic financial statements include two kinds of statements that present different views of the City:

These statements are as follows:

The Government-Wide Financial Statements – These statements provide both long-term and short-term information about the City's overall financial status.

The Fund Financial Statements – These statements focus on individual parts of the City, reporting the City's operations in more detail than the government-wide statements.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data.

CITY OF EAST PALESTINE, OHIO

***Management's Discussion and Analysis
For the Year Ended December 31, 2004***

Unaudited

Government-wide Statements

The government-wide statements report information about the City as a whole using accounting methods similar to those used by private-sector companies. The statement of net assets includes all of the government's assets and liabilities. All of the current year's revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two government-wide statements report the City's net assets and how they have changed. Net-assets (the difference between the City's assets and liabilities) are one way to measure the City's financial health or position.

- Over time, increases or decreases in the City's net assets are an indicator of whether its financial health is improving or deteriorating, respectively.
- To assess the overall health of the City you need to consider additional nonfinancial factors such as the City's tax base and the condition of the City's capital assets

The government-wide financial statements of the City are divided into two categories:

- *Governmental Activities* – Most of the City's program's and services are reported here including security of persons and property, public health and welfare services, leisure time activities, community environment, transportation and general government.
- *Business-Type Activities* – These services are provided on a charge for goods or services basis to recover all of the expenses of the goods or services provided. The City's water and wastewater services are reported as business-type activities.

Fund Financial Statements

Funds are accounting devices that the City uses to keep track of specific sources of funding and spending for particular purposes. The fund financial statements provide more detailed information about the City's most significant funds, not the City as a whole.

Governmental Funds – Most of the City's activities are reported in governmental funds, which focus on how money flows into and out of those funds and the balances left at year-end available for spending in future periods. These funds are reported using an accounting method called modified accrual 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 government operations and the basic services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance programs. The relationship (or differences) between governmental activities (reported in the Statement of Net Assets and the Statement of Activities) and governmental funds is reconciled in the financial statements.

CITY OF EAST PALESTINE, OHIO

**Management's Discussion and Analysis
For the Year Ended December 31, 2004**

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Proprietary Funds – Proprietary funds use the same basis of accounting as business-type activities; therefore, these statements will essentially match. The proprietary fund financial statements provide separate information for the Water and Wastewater funds, both of which are considered major funds.

Fiduciary Funds – Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are *not* reflected in the government-wide financial statement because the resources of those funds are *not* available to support the City's own programs. All of the City's fiduciary activities are reported in a separate Statement of Fiduciary Net Assets.

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

This is the first year for government-wide financial statements using the full accrual basis of accounting, therefore a comparison with prior year's information is not available. A comparative analysis will be provided in future years when prior year's information is available.

	Governmental Activities	Business-type Activities	Total
	2004	2004	2004
Current and other assets	\$1,907,135	\$228,073	\$2,135,208
Capital assets, Net	3,203,625	7,139,945	10,343,570
Total assets	5,110,760	7,368,018	12,478,778
Long-term debt outstanding	560,623	5,501,068	6,061,691
Other liabilities	595,650	198,419	794,069
Total liabilities	1,156,273	5,699,487	6,855,760
Net assets			
Invested in capital assets, net of related debt	2,804,256	1,760,539	4,564,795
Restricted	3,541,296	0	3,541,296
Unrestricted	(2,391,065)	(92,008)	(2,483,073)
Total net assets	\$3,954,487	\$1,668,531	\$5,623,018

CITY OF EAST PALESTINE, OHIO

**Management's Discussion and Analysis
For the Year Ended December 31, 2004**

Unaudited

Changes in Net Assets – The following table shows the changes in net assets for the fiscal year 2004:

	Governmental Activities	Business-type Activities	Total
	2004	2004	2004
Revenues			
Program revenues:			
Charges for Services and Sales	\$444,804	\$1,473,864	\$1,918,668
Operating Grants and Contributions	524,933		524,933
Capital Grants and Contributions	105,121	0	105,121
General revenues:			
Property Taxes	244,853	0	244,853
Income Taxes	833,631	0	833,631
Other Local Taxes	515	0	515
Grants and Entitlements not restricted to Specific Programs	256,745	0	256,745
Investment Earnings	13,217	0	13,217
Miscellaneous	104,724	0	104,724
Total revenues	<u>2,528,543</u>	<u>1,473,864</u>	<u>4,002,407</u>
Program Expenses			
Security of Persons and Property	1,331,317	0	1,331,317
Leisure Time Activities	252,351	0	252,351
Community Environment	179,414	0	179,414
Public Health and Welfare	56,424	0	56,424
Transportation	382,472	0	382,472
General Government	479,108	0	479,108
Debt Service:			
Interest and Fiscal Charges	14,266	0	14,266
Water	0	367,308	367,308
Sewer	0	1,202,078	1,202,078
Total expenses	<u>2,695,352</u>	<u>1,569,386</u>	<u>4,264,738</u>
Change in Net Assets before transfers	<u>(166,809)</u>	<u>(95,522)</u>	<u>(262,331)</u>
Transfers	<u>(191,227)</u>	<u>191,227</u>	<u>0</u>
Total Change in Net Assets	<u>(358,036)</u>	<u>95,705</u>	<u>(262,331)</u>
Beginning Net Assets	<u>4,312,523</u>	<u>1,572,826</u>	<u>5,885,349</u>
Ending Net Assets	<u><u>\$3,954,487</u></u>	<u><u>\$1,668,531</u></u>	<u><u>\$5,623,018</u></u>

Governmental Activities

Net assets of the City's governmental activities decreased 8% from the previous year. Although increases occurred in both income tax revenues and charges for services, expenses continued to outpace revenues.

The City receives an income tax, which is based on 1% of all salaries, wages, commissions and other compensation and on net profits earned from residents living within the City.

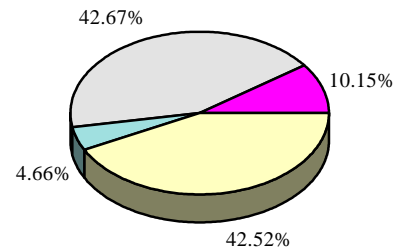
CITY OF EAST PALESTINE, OHIO

**Management's Discussion and Analysis
For the Year Ended December 31, 2004**

Unaudited

Income taxes and property taxes made up 33% and 10% respectively of revenues for governmental activities for the City in fiscal year 2004. The City's reliance upon tax revenues is demonstrated by the following graph indicating 43% of total revenues from general tax revenues:

Revenue Sources	2004	Percent of Total
General Tax Revenues	\$1,078,999	42.67%
Shared Revenue	256,745	10.15%
Program Revenues	1,074,858	42.52%
General Other	117,941	4.66%
Total Revenue	\$2,528,543	100.00%



Business-Type Activities

Net assets of the business-type activities increased by \$95,705. This increase was mainly the result of capital contributions received from the City's Governmental Activities.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

The City's governmental funds reported a combined fund balance of \$788,725, which is a decrease from last year's balance of \$917,909. The schedule below indicates the fund balance and the total change in fund balance by fund type as of December 31, 2003 and 2004:

	Fund Balance/Deficit December 31, 2004	Fund Balance/Deficit December 31, 2003	Increase (Decrease)
General	(\$528,550)	(\$531,233)	\$2,683
Electric Trust	3,040,000	3,005,000	35,000
Capital Improvement	(2,031,292)	(1,889,231)	(142,061)
Other Governmental	308,567	333,373	(24,806)
Total	\$788,725	\$917,909	(\$129,184)

CITY OF EAST PALESTINE, OHIO

**Management's Discussion and Analysis
For the Year Ended December 31, 2004**

Unaudited

General Fund – The City's General Fund balance increase is due to several factors. The tables that follow assist in illustrating the financial activities of the General Fund:

	2004 Revenues	2003 Revenues	Increase (Decrease)
Taxes	\$924,235	\$813,093	\$111,142
Intergovernmental Revenue	249,041	205,874	43,167
Charges for Services	231,169	144,066	87,103
Licenses and Permits	128,975	63,746	65,229
Investment Earnings	13,217	33,834	(20,617)
Fines and Forfeitures	11,643	9,513	2,130
All Other Revenue	19,222	79,951	(60,729)
Total	\$1,577,502	\$1,350,077	\$227,425

General Fund revenues in 2004 increased approximately 17% compared to revenues in fiscal year 2003. Contributing to this increase was a substantial increase in income tax receipts. This increase in income taxes was the result of the City no longer allowing a credit for those individuals who pay income taxes to outside municipalities. In addition, charges for services increased as a result of increases in ambulance services provided.

	2004 Expenditures	2003 Expenditures	Increase (Decrease)
Security of Persons and Property	\$1,041,889	\$1,058,638	(\$16,749)
Public Health and Welfare Services	56,424	52,753	3,671
General Government	488,485	469,280	19,205
Total	\$1,586,798	\$1,580,671	\$6,127

General Fund expenditures remained very stable, increasing by \$6,127, or less than 1%.

	2004 Other Financing Sources (Uses)	2003 Other Financing Sources (Uses)	Increase (Decrease)
Sale of Capital Assets	\$425	\$0	\$425
Transfers In	163,562	163,000	562
Transfers Out	(152,008)	(179,526)	27,518
Total	\$11,979	(\$16,526)	\$28,505

CITY OF EAST PALESTINE, OHIO

***Management's Discussion and Analysis
For the Year Ended December 31, 2004***

Unaudited

Electric Trust Fund – The City's Electric Trust Fund balance remained very stable, increasing by approximately 1%.

Capital Improvement Fund - The Capital Improvement Fund balance decreased approximately 7.5%. The fund reported increases in revenues due to Ohio Public Works Commission loan proceeds received, however, expenditures continued to exceed revenues.

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 fiscal year 2004 the City amended its General Fund budget several times, none significant.

For the General Fund, final budget basis revenue of \$1,513,998 did not significantly change from original budget estimates of \$1,563,998. The General Fund had an adequate fund balance to cover expenditures.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At the end of fiscal 2004 the City had \$10,343,570 net of accumulated depreciation invested in land, buildings, equipment and vehicles. Of this total, \$3,203,625 was related to governmental activities and \$7,139,945 to the business-type activities. The following table shows fiscal year 2004 and 2003 balances:

	Governmental Activities		Increase (Decrease)
	2004	2003	
Land	\$175,335	\$175,335	\$0
Construction In Progress	5,150	0	5,150
Buildings	1,847,192	1,798,265	48,927
Improvements Other than Buildings	127,501	69,171	58,330
Infrastructure	154,879	3,285	151,594
Machinery and Equipment	2,136,414	2,101,598	34,816
Less: Accumulated Depreciation	(1,242,846)	(1,140,922)	(101,924)
Totals	<u>\$3,203,625</u>	<u>\$3,006,732</u>	<u>\$196,893</u>

CITY OF EAST PALESTINE, OHIO

**Management's Discussion and Analysis
For the Year Ended December 31, 2004**

Unaudited

The primary increases occurred in infrastructure, which consisted of routine street improvement projects.

	Business-Type Activities		Increase (Decrease)
	2004	2003	
Land	\$177,511	\$177,511	\$0
Construction in Progress	504,169	194,168	310,001
Buildings and Improvements	2,423,457	2,343,095	80,362
Infrastructure	6,585,147	6,582,635	2,512
Machinery and Equipment	1,326,634	1,440,318	(113,684)
Less: Accumulated Depreciation	(3,876,973)	(3,653,809)	(223,164)
Totals	\$7,139,945	\$7,083,918	\$56,027

The primary increase occurred in construction in progress, which can be attributed to the addition of clarifiers at the sewage plant. Additional information on the City's capital assets can be found in Note 9.

Debt

At December 31, 2004, the City had \$4,030,000 in general obligation bonds outstanding, \$145,000 due within one year. The following table summarizes the City's debt outstanding as of December 31, 2004 and 2003:

	2004	2003
Governmental Activities:		
Ohio Public Works Commission Loans	\$286,752	\$0
Capital Leases	121,824	141,261
Compensated Absences	152,047	162,676
Total Governmental Activities	560,623	303,937
Business-Type Activities:		
General Obligation Bonds	4,030,000	4,165,000
Ohio Public Works Commission Loans	13,140	16,060
Ohio Water Development Authority Loans	1,336,266	1,431,614
Compensated Absences	121,662	111,773
Total Business-Type Activities	5,501,068	5,724,447
Totals	\$6,061,691	\$6,028,384

Under current state statutes, the City's general obligation bonded debt issues are subject to a legal limitation based on 10.5% of the total assessed value of real and personal property. In addition, the unvoted net debt of municipal corporations cannot exceed 5.5% of the total assessed value of property. At December 31, 2004, the City's outstanding debt was below the legal limit. Additional information on the City's long-term debt can be found in Note 12.

CITY OF EAST PALESTINE, OHIO

***Management's Discussion and Analysis
For the Year Ended December 31, 2004***

Unaudited

ECONOMIC FACTORS

At one time, the City of East Palestine was known for its pottery production with the potteries being the largest employers in the City. Currently the City has only one pottery left. A recycling company has purchased one of the closed potteries and the other one was torn down years ago. The City has five industrial plants with the remaining businesses being mainly sole-proprietor businesses. Two annexations were completed in 2004 and a fifty two lot housing development was started in 2003. The Claybrooke Condo Development has almost completed Phase I, and is ready to start Phase II with fifty condos in each phase.

The City's 2005 budget is very conservative. The only exceptions are a Wastewater Treatment Plant Improvement Project and a FEMA Flood Prevention Project.

The City's school district has just completed two years of building additions and improvements. The school district is the City's largest withholding employer of City Income Tax.

REQUESTS FOR INFORMATION

This financial report is designed to provide our citizens, taxpayers, investors and creditors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have questions about this report or need additional financial information contact Ms. Connie Robinson, Finance Director of the City of East Palestine.

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CITY OF EAST PALESTINE, OHIO

Statement of Net Assets
December 31, 2004

	<u>Governmental</u> <u>Activities</u>	<u>Business-Type</u> <u>Activities</u>	<u>Total</u>
Assets:			
Cash and Cash Equivalents	\$ 160,611	\$ 42,559	\$ 203,170
Investments	436,310	0	436,310
Receivables:			
Accounts	60,219	165,613	225,832
Intergovernmental	587,984	0	587,984
Interest	8,724	0	8,724
Taxes	596,632	0	596,632
Special Assessments	439	0	439
Loans	17,164	0	17,164
Inventory of Supplies at Cost	7,619	15,464	23,083
Prepaid Items	31,433	4,437	35,870
Capital Assets, Net	3,203,625	7,139,945	10,343,570
Total Assets	<u>5,110,760</u>	<u>7,368,018</u>	<u>12,478,778</u>
Liabilities:			
Accounts Payable	131,000	15,540	146,540
Accrued Wages and Benefits	114,204	34,439	148,643
Intergovernmental Payable	308	5,693	6,001
Deferred Revenue	350,138	0	350,138
Accrued Interest Payable	0	142,747	142,747
Noncurrent liabilities:			
Due within one year	94,149	264,473	358,622
Due in more than one year	466,474	5,236,595	5,703,069
Total Liabilities	<u>1,156,273</u>	<u>5,699,487</u>	<u>6,855,760</u>
Net Assets:			
Invested in Capital Assets, Net of Related Debt	2,804,256	1,760,539	4,564,795
Restricted For:			
Debt Service	23,782	0	23,782
Other Purposes	3,517,514	0	3,517,514
Unrestricted (Deficit)	(2,391,065)	(92,008)	(2,483,073)
Total Net Assets	<u>\$ 3,954,487</u>	<u>\$ 1,668,531</u>	<u>\$ 5,623,018</u>

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

Statement of Activities
For the Year Ended December 31, 2004

	Expenses	Program Revenues		
		Charges for Services and Sales	Operating Grants and Contributions	Capital Grants and Contributions
Governmental Activities:				
Security of Persons and Property	\$ 1,331,317	\$ 243,540	\$ 263,776	\$ 50,794
Leisure Time Activities	252,351	48,092	0	54,327
Community Environment	179,414	62,746	0	0
Public Health and Welfare	56,424	37,902	0	0
Transportation	382,472	0	261,157	0
General Government	479,108	52,524	0	0
Interest and Fiscal Charges	14,266	0	0	0
Total Governmental Activities	<u>2,695,352</u>	<u>444,804</u>	<u>524,933</u>	<u>105,121</u>
Business-Type Activities:				
Water	367,308	484,610	0	0
Sewer	1,202,078	989,254	0	0
Total Business-Type Activities	<u>1,569,386</u>	<u>1,473,864</u>	<u>0</u>	<u>0</u>
Totals	<u>\$ 4,264,738</u>	<u>\$ 1,918,668</u>	<u>\$ 524,933</u>	<u>\$ 105,121</u>

General Revenues

- Property Taxes Levied for:
 - General Purposes
 - Special Purposes
- Income Tax
- Other Local Taxes
- Grants and Entitlements not Restricted to Specific Programs
- Investment Earnings
- Miscellaneous
- Transfers
- Total General Revenues and Transfers

- Change in Net Assets
 - Net Assets Beginning of Year
 - Net Assets End of Year

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

Net (Expense) Revenue
and Changes in Net Assets

Governmental Activities	Business-Type Activities	Total
\$ (773,207)	\$ 0	\$ (773,207)
(149,932)	0	(149,932)
(116,668)	0	(116,668)
(18,522)	0	(18,522)
(121,315)	0	(121,315)
(426,584)	0	(426,584)
(14,266)	0	(14,266)
<u>(1,620,494)</u>	<u>0</u>	<u>(1,620,494)</u>
0	(213,695)	(213,695)
<u>0</u>	<u>118,173</u>	<u>118,173</u>
<u>0</u>	<u>(95,522)</u>	<u>(95,522)</u>
<u>(1,620,494)</u>	<u>(95,522)</u>	<u>(1,716,016)</u>
106,738	0	106,738
138,115	0	138,115
833,631	0	833,631
515	0	515
256,745	0	256,745
13,217	0	13,217
104,724	0	104,724
<u>(191,227)</u>	<u>191,227</u>	<u>0</u>
<u>1,262,458</u>	<u>191,227</u>	<u>1,453,685</u>
(358,036)	95,705	(262,331)
<u>4,312,523</u>	<u>1,572,826</u>	<u>5,885,349</u>
<u>\$ 3,954,487</u>	<u>\$ 1,668,531</u>	<u>\$ 5,623,018</u>

CITY OF EAST PALESTINE, OHIO

**Balance Sheet
Governmental Funds
December 31, 2004**

	General	Electric Trust	Capital Improvement	Other Governmental Funds	Total Governmental Funds
Assets:					
Cash and Cash Equivalents	\$ 1,526	\$ 20,487	\$ 2,419	\$ 136,179	\$ 160,611
Investments	15,833	212,505	25,092	182,880	436,310
Receivables:					
Taxes	342,818	0	0	253,814	596,632
Accounts	59,754	0	0	465	60,219
Intergovernmental	91,034	0	24,464	472,486	587,984
Interest	8,048	0	0	676	8,724
Special Assessments	0	0	0	439	439
Loans	0	0	0	17,164	17,164
Interfund Loans Receivables	0	2,807,008	0	0	2,807,008
Inventory of Supplies, at Cost	0	0	0	7,619	7,619
Prepaid Items	31,433	0	0	0	31,433
Total Assets	\$ 550,446	\$ 3,040,000	\$ 51,975	\$ 1,071,722	\$ 4,714,143
Liabilities:					
Accounts Payable	\$ 26,389	\$ 0	\$ 48,841	\$ 55,770	\$ 131,000
Accrued Wages and Benefits Payable	93,955	0	0	20,249	114,204
Intergovernmental Payable	308	0	0	0	308
Interfund Loans Payable	710,000	0	2,009,962	87,046	2,807,008
Deferred Revenue	248,344	0	24,464	600,090	872,898
Total Liabilities	1,078,996	0	2,083,267	763,155	3,925,418
Fund Balances:					
Reserved for Encumbrances	240	0	148	89,674	90,062
Reserved for Prepaid Items	31,433	0	0	0	31,433
Reserved for Supplies Inventory	0	0	0	7,619	7,619
Reserved for Endowments	0	0	0	48,624	48,624
Undesignated, Unreserved in:					
General Fund	(560,223)	0	0	0	(560,223)
Special Revenue Funds	0	3,040,000	0	72,758	3,112,758
Debt Service Fund	0	0	0	23,343	23,343
Capital Project Funds	0	0	(2,031,440)	66,549	(1,964,891)
Total Fund Balances	(528,550)	3,040,000	(2,031,292)	308,567	788,725
Total Liabilities and Fund Balances	\$ 550,446	\$ 3,040,000	\$ 51,975	\$ 1,071,722	\$ 4,714,143

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

***Reconciliation Of Total Governmental Fund Balances
To Net Assets Of Governmental Activities
December 31, 2004***

Total Governmental Fund Balances \$ 788,725

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

Capital Assets used in governmental activities are not
resources and therefore are not reported in the funds. 3,203,625

Other long-term assets are not available to pay for current-
period expenditures and therefore are deferred in the funds. 522,760

Long-term liabilities, including bonds payable, are not due
and payable in the current period and therefore are not
reported in the funds.

Compensated Absences Payable	(152,047)	
OPWC Loan Payable	(286,752)	
Capital Leases	(121,824)	(560,623)

Net Assets of Governmental Activities **\$ 3,954,487**

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

**Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
For the Year Ended December 31, 2004**

	General	Electric Trust	Capital Improvement	Other Governmental Funds	Total Governmental Funds
Revenues:					
Taxes	\$ 924,235	\$ 0	\$ 0	\$ 141,987	\$ 1,066,222
Intergovernmental Revenues	249,041	0	34,463	784,935	1,068,439
Charges for Services	231,169	0	0	72,366	303,535
Licenses and Permits	128,975	0	0	0	128,975
Investment Earnings	13,217	0	0	0	13,217
Special Assessments	0	0	0	119	119
Fines and Forfeitures	11,643	0	0	728	12,371
All Other Revenue	19,222	35,000	0	50,502	104,724
Total Revenue	1,577,502	35,000	34,463	1,050,637	2,697,602
Expenditures:					
Current:					
Security of Persons and Property	1,041,889	0	0	221,208	1,263,097
Public Health and Welfare	56,424	0	0	0	56,424
Leisure Time Activities	0	0	0	218,127	218,127
Community Environment	0	0	0	179,414	179,414
Transportation	0	0	0	348,078	348,078
General Government	488,485	0	0	52,815	541,300
Capital Outlay	0	0	706,854	98,800	805,654
Debt Service:					
Interest & Fiscal Charges	0	0	0	14,266	14,266
Total Expenditures	1,586,798	0	706,854	1,132,708	3,426,360
Excess (Deficiency) of Revenues Over Expenditures	(9,296)	35,000	(672,391)	(82,071)	(728,758)
Other Financing Sources (Uses):					
Sale of Capital Assets	425	0	0	0	425
OPWC Loan Proceeds	0	0	286,752	0	286,752
Other Financing Sources - Capital Lease	0	0	37,609	0	37,609
Transfers In	163,562	0	205,969	89,400	458,931
Transfers Out	(152,008)	0	0	(32,557)	(184,565)
Total Other Financing Sources (Uses)	11,979	0	530,330	56,843	599,152
Net Change in Fund Balances	2,683	35,000	(142,061)	(25,228)	(129,606)
Fund Balances (Deficit) at Beginning of Year	(531,233)	3,005,000	(1,889,231)	333,373	917,909
Increase in Inventory Reserve	0	0	0	422	422
Fund Balances (Deficit) End of Year	\$ (528,550)	\$ 3,040,000	\$ (2,031,292)	\$ 308,567	\$ 788,725

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

***Reconciliation Of The Statement Of Revenues, Expenditures
And Changes In Fund Balances Of Governmental Funds
To The Statement Of Activities
For The Fiscal Year Ended December 31, 2004***

Net Change in Fund Balances - Total Governmental Funds \$ (129,606)

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 amount by which capital outlays exceeded depreciation in the current period.

Capital Outlay	374,406	
Depreciation Expense	(177,513)	196,893

Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds. (169,059)

The issuance of long-term debt (e.g. notes, leases) provides current financial resources to government funds, while the repayment of the principal of long-term debt consumes the current financial resources of government funds. Neither transaction, however, has any effect on net assets. This amount is the net effect of these differences in the treatment of long-term debt and related items.

OPWC Loan	(286,752)	
Capital Leases	(37,609)	(324,361)

Repayment of bond and loan principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets.

Capital Lease Payment		57,046
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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 the governmental funds.

Compensated Absences	10,629	
Change in Inventory	422	11,051

Change in Net Assets of Governmental Activities \$ (358,036)

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

**Statement of Revenues, Expenditures and Changes in
Fund Balance – Budget and Actual (Non-GAAP Budgetary Basis)
General Fund
For the Year Ended December 31, 2004**

	Original Budget	Final Budget	Actual	Variance with Final Budget Positive (Negative)
Revenues:				
Taxes	\$ 996,705	\$ 964,841	\$ 925,147	\$ (39,694)
Intergovernmental Revenue	195,314	189,070	181,292	(7,778)
Charges for Services	249,837	241,848	231,899	(9,949)
Licenses and Permits	77,963	75,471	72,366	(3,105)
Investment Earnings	12,932	12,519	12,004	(515)
Fines and Forfeitures	12,118	11,731	11,248	(483)
All Other Revenues	19,129	18,518	17,756	(762)
Total Revenues	<u>1,563,998</u>	<u>1,513,998</u>	<u>1,451,712</u>	<u>(62,286)</u>
Expenditures:				
Current:				
Security of Persons and Property	1,132,474	1,105,505	1,072,173	33,332
Public Health and Welfare	60,562	59,119	57,337	1,782
General Government	514,319	502,071	486,933	15,138
Total Expenditures	<u>1,707,355</u>	<u>1,666,695</u>	<u>1,616,443</u>	<u>50,252</u>
Excess (Deficiency) of Revenues Over (Under) Expenditures	(143,357)	(152,697)	(164,731)	(12,034)
Other Financing Sources (Uses):				
Sale of Capital Assets	425	425	425	0
Transfers In	163,562	163,562	163,562	0
Transfers Out	(152,008)	(152,008)	(152,008)	0
Advances In	100,000	100,000	100,000	0
Total Other Financing Sources (Uses):	<u>111,979</u>	<u>111,979</u>	<u>111,979</u>	<u>0</u>
Net Change in Fund Balance	(31,378)	(40,718)	(52,752)	(12,034)
Fund Balance at Beginning of Year	22,255	22,255	22,255	0
Prior Year Encumbrances	37,605	37,605	37,605	0
Fund Balance at End of Year	<u>\$ 28,482</u>	<u>\$ 19,142</u>	<u>\$ 7,108</u>	<u>\$ (12,034)</u>

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

**Statement of Revenues, Expenditures and Changes in
Fund Balance – Budget and Actual (Non-GAAP Budgetary Basis)
Special Revenue Fund - Electric Trust Fund
For the Year Ended December 31, 2004**

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>	Variance with Final Budget Positive (Negative)
Revenues:				
All Other Revenues	\$ 80,000	\$ 40,000	\$ 35,000	\$ (5,000)
Total Revenues	<u>80,000</u>	<u>40,000</u>	<u>35,000</u>	<u>(5,000)</u>
Expenditures:				
Total Expenditures	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Excess (Deficiency) of Revenues Over (Under) Expenditures	80,000	40,000	35,000	(5,000)
Other Financing Sources (Uses):				
Advances Out	<u>(100,000)</u>	<u>(100,000)</u>	<u>(100,000)</u>	<u>0</u>
Total Other Financing Sources (Uses):	<u>(100,000)</u>	<u>(100,000)</u>	<u>(100,000)</u>	<u>0</u>
Net Change in Fund Balance	(20,000)	(60,000)	(65,000)	(5,000)
Fund Balance at Beginning of Year	<u>297,992</u>	<u>297,992</u>	<u>297,992</u>	<u>0</u>
Fund Balance at End of Year	<u>\$ 277,992</u>	<u>\$ 237,992</u>	<u>\$ 232,992</u>	<u>\$ (5,000)</u>

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

Statement of Net Assets
Proprietary Funds
December 31, 2004

	Business-Type Activities		
	Enterprise Funds		
	Water	Sewer	Total
ASSETS			
Current assets:			
Cash and Cash Equivalents	\$ 11,805	\$ 30,754	\$ 42,559
Receivables:			
Accounts	53,789	111,824	165,613
Inventory of Supplies at Cost	14,125	1,339	15,464
Prepaid Items	1,805	2,632	4,437
Total current assets	81,524	146,549	228,073
Noncurrent assets:			
Capital Assets, Net	1,189,055	5,950,890	7,139,945
Total noncurrent assets	1,189,055	5,950,890	7,139,945
Total assets	1,270,579	6,097,439	7,368,018
LIABILITIES			
Current liabilities:			
Accounts Payable	4,902	10,638	15,540
Accrued Wages and Benefits	10,782	23,657	34,439
Intergovernmental Payable	232	5,461	5,693
Accrued Interest Payable	4,311	138,436	142,747
General Obligation Bonds Payable - Current	6,300	138,700	145,000
OWDA Loans Payable - Current	41,525	55,013	96,538
OPWC Loans Payable - Current	2,920	0	2,920
Total Current Liabilities	70,972	371,905	442,877
Noncurrent Liabilities:			
General Obligation Bonds Payable	112,095	3,772,905	3,885,000
OWDA Loans Payable	290,671	949,057	1,239,728
OPWC Loans Payable	10,220	0	10,220
Compensated Absences Payable	34,485	87,177	121,662
Total noncurrent liabilities	447,471	4,809,139	5,256,610
Total Liabilities	518,443	5,181,044	5,699,487
NET ASSETS			
Invested in Capital Assets, Net of Related Debt	725,324	1,035,215	1,760,539
Unrestricted	26,812	(118,820)	(92,008)
Total Net Assets	\$ 752,136	\$ 916,395	\$ 1,668,531

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

Statement of Revenues, Expenses and Changes in Fund Net Assets
Proprietary Funds
For the Year Ended December 31, 2004

	Business-Type Activities		
	Enterprise Funds		
	Water	Sewer	Total
Operating Revenues:			
Charges for Services	\$ 483,864	\$ 986,095	\$ 1,469,959
Total Operating Revenues	<u>483,864</u>	<u>986,095</u>	<u>1,469,959</u>
Operating Expenses:			
Personal Services	149,600	363,114	512,714
Contractual Services	23,781	53,351	77,132
Materials and Supplies	46,989	24,945	71,934
Utilities	51,985	70,976	122,961
Depreciation	73,169	284,094	357,263
Total Operating Expenses	<u>345,524</u>	<u>796,480</u>	<u>1,142,004</u>
Operating Income	138,340	189,615	327,955
Non-Operating Revenue (Expenses):			
Interest and Fiscal Charges	(21,784)	(337,522)	(359,306)
Capital Contributions	134,596	330,997	465,593
Loss on Sale of Capital Assets	0	(67,818)	(67,818)
Other Nonoperating Revenue	746	3,159	3,905
Other Nonoperating Expense	0	(258)	(258)
Total Non-Operating Revenues (Expenses)	<u>113,558</u>	<u>(71,442)</u>	<u>42,116</u>
Income Before Transfers	251,898	118,173	370,071
Transfers:			
Transfers-In	0	16,610	16,610
Transfers-Out	(195,764)	(95,212)	(290,976)
Total Transfers	<u>(195,764)</u>	<u>(78,602)</u>	<u>(274,366)</u>
Change in Net Assets	56,134	39,571	95,705
Net Assets Beginning of Year	696,002	876,824	1,572,826
Net Assets End of Year	<u>\$ 752,136</u>	<u>\$ 916,395</u>	<u>\$ 1,668,531</u>

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

**Statement of Cash Flows
Proprietary Funds
For the Year Ended December 31, 2004**

	Business-Type Activities		Totals
	Enterprise Funds		
	Water	Sewer	
<u>Cash Flows from Operating Activities:</u>			
Cash Received from Customers	\$451,220	\$921,542	\$1,372,762
Cash Payments for Goods and Services	(115,419)	(141,261)	(256,680)
Cash Payments to Employees	(146,527)	(353,066)	(499,593)
Net Cash Provided by Operating Activities	189,274	427,215	616,489
<u>Cash Flows from Noncapital Financing Activities:</u>			
Transfers Out to Other Funds	(179,154)	(95,212)	(274,366)
Net Cash Used by Noncapital Financing Activities	(179,154)	(95,212)	(274,366)
<u>Cash Flows from Capital and Related Financing Activities:</u>			
Acquisition and Construction of Assets	(13,340)	(2,175)	(15,515)
Principal Paid on General Obligation Bond	(14,250)	(120,750)	(135,000)
Principal Paid on Ohio Public Works Commission Loan	(2,920)	0	(2,920)
Principal Paid on Ohio Water Development Authority Loan	(41,525)	(53,823)	(95,348)
Interest Paid on All Debt	(41,374)	(198,539)	(239,913)
Net Cash Used for Capital and Related Financing Activities	(113,409)	(375,287)	(488,696)
<u>Cash Flows from Investing Activities:</u>			
Sale of Investments	112,845	72,591	185,436
Net Cash Provided by Investing Activities	112,845	72,591	185,436
Net Increase in Cash and Cash Equivalents	9,556	29,307	38,863
Cash and Cash Equivalents at Beginning of Year	2,249	1,447	3,696
Cash and Cash Equivalents at End of Year	\$11,805	\$30,754	\$42,559
<u>Reconciliation of Operating Income to Net Cash Provided by Operating Activities:</u>			
Operating Income	\$138,340	\$189,615	\$327,955
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:			
Depreciation Expense	73,169	284,094	357,263
Miscellaneous Nonoperating Revenue	746	3,159	3,905
Miscellaneous Nonoperating Expense	0	(258)	(258)
Changes in Assets and Liabilities:			
Increase in Accounts Receivable	(33,390)	(67,755)	(101,145)
Decrease in Intergovernmental Receivable	0	43	43
Decrease in Inventory	10,706	361	11,067
Decrease in Prepaid Items	257	671	928
Increase (Decrease) in Accounts Payable	(3,754)	1,970	(1,784)
Increase in Accrued Wages and Benefits	1,420	1,585	3,005
Increase in Intergovernmental Payable	160	5,461	5,621
Increase in Compensated Absences	1,620	8,269	9,889
Total Adjustments	50,934	237,600	288,534
Net Cash Provided by Operating Activities	\$189,274	\$427,215	\$616,489

See accompanying notes to the basic financial statements

CITY OF EAST PALESTINE, OHIO

***Statement of Net Assets
Fiduciary Funds
December 31, 2004***

	<u>Agency Fund</u>
Assets:	
Cash and Cash Equivalents	\$ 311
Total Assets	<u>311</u>
Liabilities:	
Due to Others	<u>311</u>
Total Liabilities	<u>311</u>
Total Net Assets	<u>\$ 0</u>

See accompanying notes to the basic financial statements

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CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The City of East Palestine, Ohio (the "City") is a home rule municipal corporation created under the laws of the State of Ohio. East Palestine was first incorporated as a village on February 27, 1876. The City currently operates under and is governed by its own Charter. The current Charter, which provides for a Council-City Manager form of government, was adopted in 1990.

The accompanying basic financial statements comply with the provisions of Governmental Accounting Standards Board (the "GASB") Statement No. 14, "*The Financial Reporting Entity*," in that the financial statements include all organizations, activities, functions and component units for which the City (the reporting entity) is financially accountable. Financial accountability is defined as the appointment of a voting majority of a legally separate organization's governing body and either the City's ability to impose its will over the organization, or the possibility that the organization will provide a financial benefit to or impose a financial burden on the City. There were no potential component units that met the criteria imposed by GASB Statement No. 14 to be included in the City's reporting entity. Based on the foregoing, the reporting entity of the City includes the following services: police and fire protection, emergency medical, parks, recreation, planning, zoning, street maintenance and other governmental services. In addition, the City owns and operates a water treatment and distribution system and a wastewater treatment and collection system, which are reported as enterprise funds.

The accounting policies and financial reporting practices of the City conform to generally accepted accounting principles as applicable to governmental units. The following is a summary of its significant accounting policies:

B. Basis of Presentation - Fund Accounting

The accounting system is organized and operated on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues and expenditures (expenses). The various funds are summarized by type in the basic financial statements. The following fund types are used by the City:

Governmental Funds - The governmental funds are those funds through which most governmental functions are typically financed. The acquisition, use and balances of the City's expendable financial resources and the related current liabilities (except those accounted for in the proprietary funds) are accounted for through governmental funds. The measurement focus is upon determination of "financial flow" (sources, uses and balances of financial resources). The following are the City's major governmental funds:

General Fund - This fund is used to account for all financial resources except those resources accounted for in another fund. The general fund balance is available to the City for any purpose provided it is expended or transferred according to the general laws of Ohio and the provisions of the City Charter.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Basis of Presentation - Fund Accounting (Continued)

Electric Trust Fund - This fund was created to account for proceeds received by the City from the sale of the City Electric Plant. These proceeds may be used by the City for purposes approved by city council.

Capital Improvement Fund - This fund is used to account for the financial resources used for the major capital projects undertaken by the City.

Proprietary Funds - The proprietary funds are accounted for on an "economic resources" measurement focus. This measurement focus provides that all assets and liabilities associated with the operation of the proprietary funds are included on the balance sheet. The proprietary fund operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total assets.

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

Water Fund - This fund is used to account for the operation of the City's water service.

Wastewater Fund - This fund is used to account for the operation of the City's sanitary sewer service.

Fiduciary Funds - Trust and Agency Funds - These funds are used to account for assets held by a government unit in a trustee capacity or as an agent for individuals, private organizations, other governmental units and/or other funds. The City maintains one agency fund. Agency funds are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations.

C. Basis of Presentation - Financial Statements

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 and those that are considered business-type activities.

The government-wide statements are prepared using the economic resources measurement focus. This is the same approach used in the preparation of the proprietary fund financial statements but differs from the manner in which governmental fund financial statements are prepared. Governmental fund financial statements therefore include a reconciliation with brief explanations to better identify the relationship between the government-wide statements and the statements for governmental funds.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

C. Basis of Presentation – Financial Statements (Continued)

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

Fund Financial Statements – Fund financial statements report detailed information about the City. The focus of governmental fund financial statements is on major funds rather than reporting funds by type. Each major fund is presented in a separate column. Nonmajor funds are aggregated and presented in a single column. Fiduciary funds are reported by fund type.

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental fund types are accounted for using a flow of current financial resources measurement focus. The financial statements for governmental funds are a balance sheet, which generally includes only current assets and current liabilities, and a statement of revenues, expenditures and changes in fund balances, which reports on the sources (i.e., revenues and other financing sources) and uses (i.e., expenditures and other financing uses) of current financial resources.

All proprietary fund types 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 changes in fund net assets presents increases (i.e., revenues) and decreases (i.e., expenses) in net total assets. The statement of cash flows provides information about how the City finances and meets the cash flow needs of its proprietary activities.

D. Basis of Accounting

Basis of accounting represents the methodology utilized in the recognition of revenues and expenditures or expenses reported in the financial statements. The accounting and reporting treatment applied to a fund is determined by its measurement focus.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

D. Basis of Accounting (Continued)

The modified accrual basis of accounting is followed by the governmental funds. Under the modified accrual basis of accounting, revenues are recorded when susceptible to accrual, i.e., both measurable and available. The term "available" means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period, which for the City is 60 days after year end. Expenditures are recognized in the accounting period in which the fund liability is incurred, if measurable, except for unmatured interest on general long-term debt which is recognized when due.

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

Revenues considered susceptible to accrual at year end include income taxes withheld by employers, interest on investments, special assessments and state levied locally shared taxes (including motor vehicle license fees and local government assistance). Other revenues, including licenses, permits, certain charges for services, income taxes other than those withheld by employers and miscellaneous revenues, are recorded as revenues when received in cash because generally these revenues are not measurable until received.

Property taxes measurable as of December 31, 2004 but which are not intended to finance 2004 operations and delinquent property taxes, whose availability is indeterminate, are recorded as deferred revenue as further described in Note 5.

The accrual basis of accounting is utilized for reporting purposes by the proprietary and agency funds. Revenues are recognized when earned and expenses are recognized when they are incurred.

Pursuant to GASB Statement No. 20, *"Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting,"* the City follows GASB guidance as applicable to proprietary funds and FASB Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins issued on or before November 30, 1989 that do not conflict with or contradict GASB pronouncements. The City has elected not to apply FASB statements and interpretations issued after November 30, 1989 to its business-type activities and enterprise funds.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

E. Budgetary Process

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 ordinance, all of which are prepared on the budgetary basis of accounting. The certificate of estimated resources and the appropriation ordinance are subject to amendment throughout the year.

All funds other than agency funds are legally required to be budgeted and appropriated; however, only governmental funds are required to be reported. The primary level of budgetary control is at the object level within each department. Budgetary modifications may only be made by ordinance of the City Council.

1. Tax Budget

By July 15, the City Manager 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.

2. Estimated Resources

The County Budget Commission reviews estimated revenue and determines if the budget substantiates a need to levy all or part of previously authorized taxes. The Budget Commission then certifies its actions to the City by September 1 of each year. As part of the certification process, the City receives an official certificate of estimated resources stating the projected receipts by fund. Prior to December 31, the City must revise its budget so that the total contemplated expenditures from any fund during the ensuing fiscal year do not exceed the amount available as stated in the certificate of estimated resources. The revised budget then serves as the basis for the annual appropriations measure. On or about January 1, the certificate of estimated resources is amended to include any unencumbered fund balances from the preceding year. The certificate may be further amended during the year if a new source of revenue is identified or actual receipts exceed current estimates. The amounts reported on the budgetary statement reflect the amounts in the final amended official certificate of estimated resources issued during 2004.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

E. Budgetary Process (Continued)

3. Appropriations

A temporary appropriation ordinance to control expenditures may be passed on or about January 1 of each year for the period January 1 through March 31. An annual appropriation ordinance must be passed by April 1 of each year for the period January 1 through December 31. The appropriation ordinance establishes spending controls at the fund, department and object level. The appropriation ordinance may be amended during the year as additional information becomes available, provided that total fund appropriations do not exceed the current estimated resources as certified. The allocation of appropriations among departments and objects within a fund may be modified during the year by an ordinance of City Council. During 2004, several supplemental appropriations were necessary to budget the use of contingency funds. Administrative control is maintained through the establishment of more detailed line-item budgets. The budgetary figures which appear in the "Statement of Revenues, Expenditures, and Changes in Fund Balances--Budget and Actual—for the General and Major Special Revenue Funds" are provided on the budgetary basis to provide a comparison of actual results to the final budget, including all amendments and modifications.

4. Encumbrances

As part of formal budgetary control, purchase orders, contracts and other commitments for expenditures are encumbered and recorded as the equivalent of expenditures (budget basis) in order to reserve that portion of the applicable appropriation and to determine and maintain legal compliance. However, on the GAAP basis of accounting, encumbrances do not constitute expenditures or liabilities and are reported as reservations of fund balances for governmental funds in the accompanying basic financial statements.

5. 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 appropriations. The encumbered appropriation balance is carried forward to the subsequent fiscal year and need not be reappropriated.

6. Budgetary Basis of Accounting

The City's budgetary process accounts for certain transactions on a basis other than generally accepted accounting principles (GAAP). The major differences between the budgetary basis and the GAAP basis lie in the manner in which revenues and expenditures are recorded. Under the budgetary basis, revenues and expenditures are recognized on a cash basis. Utilizing the cash basis, revenues are recorded when received in cash and expenditures when paid. Under the GAAP basis, revenues and expenditures are recorded on the modified accrual basis of accounting.

CITY OF EAST PALESTINE, OHIO

***Notes to the Basic Financial Statements
For the Year Ended December 31, 2004***

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

E. Budgetary Process (Continued)

6. Budgetary Basis of Accounting (Continued)

The following table summarizes the adjustments necessary to reconcile the GAAP basis statements to the budgetary basis statements for the General and Major Special Revenue funds:

	Net Change in Fund Balances	
	General Fund	Electric Trust Fund
GAAP Basis (as reported)	\$2,683	\$35,000
Increase (Decrease):		
Accrued Revenues at December 31, 2004 received during 2005	(153,310)	(2,807,008)
Accrued Revenues at December 31, 2003 received during 2004	127,520	2,707,008
Accrued Expenditures at December 31, 2004 paid during 2005	120,652	0
Accrued Expenditures at December 31, 2003 paid during 2004	(138,126)	0
2003 Prepays for 2004	29,513	0
2004 Prepays for 2005	(31,433)	0
Outstanding Encumbrances	(10,251)	0
Budget Basis	(\$52,752)	(\$65,000)

F. Cash and Cash Equivalents

Cash and cash equivalents include amounts in demand deposits, the State Treasurer's Asset Reserve (STAR Ohio), repurchase agreements and certificates of deposit. The repurchase agreements and STAR Ohio are considered cash equivalents because of their highly liquid nature.

The City pools a majority of its cash for investment and resource management purposes. Each fund's equity in pooled cash and investments represents the balance on hand as if each fund maintained its own cash and investment account. For purposes of the statement of cash flows, the proprietary funds' shares of equity in pooled repurchase agreements and certificates of deposit are considered to be cash equivalents. See Note 4, "Cash, Cash Equivalents and Investments."

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

G. Investments

Investment procedures and interest allocations are restricted by provisions of the Ohio Constitution and the Ohio Revised Code. In accordance with GASB Statement No. 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools", the City reports its investments at fair value, except for nonparticipating investment contracts (certificates of deposit and repurchase agreements) which are reported at cost.

The City has invested funds in the STAR Ohio during 2004. STAR Ohio is an investment pool managed by the State Treasurer's Office which allows governments within the State to pool their funds for investment purposes. STAR Ohio is not registered with the SEC as an investment company, but does operate in a manner consistent with Rule 2a7 of the Investment Company Act of 1940. Investments in STAR Ohio are valued at STAR Ohio's share price which is the price the investment could be sold for on December 31, 2004. See Note 4, "Cash, Cash Equivalents and Investments."

H. Inventory

Inventory is stated at cost (first-in, first-out) in the governmental funds and at the lower of cost or market in the proprietary funds. The costs of inventory items are recorded as expenditures in the governmental funds when purchased and as expenses in the proprietary funds when used.

I. Capital Assets and Depreciation

Capital assets are defined by the City as assets with an initial, individual cost of more than \$1,000.

1. Property, Plant and Equipment - Governmental Activities

Governmental activities capital assets are those not directly related to the business type funds. These generally are acquired or constructed for governmental activities and are recorded as expenditures in the governmental funds and are capitalized at cost (or estimated historical cost for assets not purchased in recent years). These assets are reported in the Governmental Activities column of the Government-wide Statement of Net Assets, but they are not reported in the Fund Financial Statements.

Contributed capital assets are recorded at fair market value at the date received. Capital assets include land, buildings, building improvements, machinery, equipment and infrastructure. Infrastructure is defined as long-lived capital assets that normally are stationary in nature and normally can be preserved for a significant number of years. Examples of infrastructure include roads, bridges, curbs and gutters, streets and sidewalks, drainage systems and lighting systems.

Estimated historical costs for governmental activities capital asset values were initially determined by identifying historical costs when such information was available. In cases where information supporting original cost was not obtainable, estimated historical costs were developed. For certain capital assets, the estimates were arrived at by indexing estimated current costs back to the estimated year of acquisition.

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2004**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

I. Capital Assets and Depreciation (Continued)

2. Property, Plant and Equipment – Business Type Activities

Property, plant and equipment acquired by the proprietary funds are stated at cost (or estimated historical cost), including interest capitalized during construction and architectural and engineering fees where applicable. Contributed capital assets are recorded at fair market value at the date received. These assets are reported in both the Business-Type Activities column of the Government-wide Statement of Net Assets and in the respective funds.

3. Depreciation

All capital assets are depreciated, excluding land and construction in progress. Depreciation has been provided using the straight-line method over the following estimated useful lives:

Description	Governmental and Business-Type Activities Estimated Lives (in years)
Buildings	30 - 40
Improvements other than Buildings	50
Machinery, Equipment, Furniture and Fixtures	5 – 15
Infrastructure	50 – 100

J. Long-Term Obligations

Long-term liabilities are being repaid from the following funds:

Obligation	Fund
Ohio Water Development Authority Loans	Water Fund Wastewater Fund
General Obligation Bond	Wastewater Fund
Ohio Public Works Commission Loan	General Bond Retirement Fund
Compensated Absences	General Fund Street Construction, Maintenance and Repair Fund Water Fund Wastewater Fund
Capital Leases	General Fund Capital Improvement Fund

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

K. Compensated Absences

In accordance with GASB Statement No. 16, "Accounting for Compensated Absences," vacation and compensatory time are accrued as liabilities when an employee's right to receive compensation is attributable to services already rendered and it is probable that the employee will be compensated through paid time off or some other means, such as cash payments at termination or retirement. Leave time that has been earned but is unavailable for use as paid time off or as some other form of compensation because an employee has not met the minimum service time requirement, is accrued to the extent that it is considered to be probable that the conditions for compensation will be met in the future.

Sick leave is accrued using the vesting method, whereby the liability is recorded on the basis of leave accumulated by employees who are eligible to receive termination payments as of the balance sheet date, and on leave balances accumulated by other employees who are expected to become eligible in the future to receive such payments.

For governmental funds, that portion of unpaid compensated absences that is expected to be paid using expendable, available resources is reported as an expenditure in the fund from which the individual earning the leave is paid, and a corresponding liability is reflected in the account "Compensated Absences Payable." In the government wide statement of net assets, "Compensated Absences Payable" is recorded within the "Due within one year" account and the long-term portion of the liability is recorded within the "Due in more than one year" account.

Compensated absences are expensed in the Water and Wastewater Funds when earned, and the related liability is reported within the fund.

L. 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 balances of any borrowings used for the acquisition, construction of 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.

The City applies restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

M. Pensions

The provision for pension costs is recorded when the related payroll is accrued and the obligation is incurred.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

N. Interfund Activity

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 interfund transfers. Interfund transfers are reported as other financing sources/uses in governmental funds and after nonoperating revenues/expenses in proprietary funds. Repayments from funds responsible for particular expenditures/expenses to the funds that initially paid for them are not presented on the financial statements.

O. Reservations of Fund Balance

Reserves indicate that a portion of fund balance is not available for expenditure or is legally segregated for a specific future use. Fund balances are reserved for supplies inventory, prepaid items, debt service, endowments and encumbered amounts which have not been accrued at year end.

P. Operating Revenues and Expenses

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues are those revenues that are generated directly from the primary activity of the proprietary funds. For the City, these revenues are charges for services for water treatment and distribution and wastewater collection and treatment. Operating expenses are necessary costs incurred to provide the goods or services that are the primary activity of the fund. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Q. Extraordinary and Special Items

Extraordinary items are transactions or events that are both unusual in nature and infrequent in occurrence. Special items are transactions or events that are within the control of the City and that are either unusual in nature or infrequent in occurrence. The City had no special items to report during fiscal year 2004.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 2 – CHANGES IN ACCOUNTING PRINCIPLE AND RESTATEMENT OF FUND BALANCE

A. Changes in Accounting Principles

For fiscal year 2004, the City has implemented GASB Statement No. 34, “*Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*”; GASB Statement No. 37, “*Basic Financial Statements for State and Local Governments: Omnibus*”; GASB Statement No. 38, “*Certain Financial Statement Note Disclosures*”; and GASB Interpretation No. 6, “*Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statement.*” At December 31, 2003, there was no effect on fund balance as a result of implementing GASB Statements 36, 37 and 38, or Interpretation No. 6.

GASB 34 creates new basic financial statements for reporting on the City’s financial activities. The financial statements now include government-wide financial statements prepared on an accrual basis of accounting and fund financial statements which present information for individual major funds rather than by fund type. Nonmajor funds are presented in total in one column.

The government-wide financial statements split the City’s programs between business-type and governmental activities. Except for the restatement explained below, the beginning net asset amount for the business-type activities equals fund equity of the enterprise funds from last year. The beginning net asset amount for governmental programs reflects the change in fund balance for governmental funds at December 31, 2003 caused by the conversion to the accrual basis of accounting.

B. Prior Period Adjustments

For the year ended December 31, 2004, the City has implemented a policy of capitalizing all capital assets based on a capitalization threshold of \$1,000. This change resulted in the restatement of the net assets at December 31, 2003 for the enterprise funds as presented in item C of this note.

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2004**

NOTE 2 – CHANGES IN ACCOUNTING PRINCIPLE AND RESTATEMENT OF FUND BALANCE (Continued)

C. Restatement of Fund Balance/Retained Earnings

In addition, The changes to the beginning fund balance, as well as the transition from fund balance to net assets of the governmental activities and the business-type activities are as follows:

	General	Electrict Trust	Capital Improvement	Other Governmental Funds	Total Governmental Activities
Fund Balance December 31, 2003	(\$531,233)	\$3,005,000	(\$1,889,231)	\$279,425	\$863,961
Adjustments to Fund Structure:					
Reclassified fund from Non-Expendable Trust					
Fund to Permanent Fund	0	0	0	53,948	53,948
Adjusted Fund Balance	(531,233)	3,005,000	(1,889,231)	333,373	917,909
GASB 34 Adjustments:					
Capital Assets					3,006,732
Long-Term Liabilities					(303,937)
Long-Term (Deferred) Assets					691,819
Net Assets, December 31, 2003					\$4,312,523

	Water	Sewer	Total Business-Type Activities
Fund Balance December 31, 2003	\$236,462	(\$908,114)	(\$671,652)
GASB 34 Adjustments:			
Contributed Capital	129,813	1,568,224	1,698,037
Adjusted Fund Balance	366,275	(908,114)	1,026,385
Capital Assets			546,441
Net Assets, December 31, 2003			\$1,572,826

NOTE 3 - COMPLIANCE AND ACCOUNTABILITY

Fund Deficits - The fund deficits at December 31, 2004 of \$528,550 in the General Fund, \$86,141 in the Downtown Revitalization Fund (special revenue funds) and \$2,031,292 in the Capital Improvement Fund (capital projects fund) arise from the recognition of expenditures on the modified accrual basis which are greater than expenditures recognized on the budgetary/cash basis. The general fund provides transfers when cash is required, not when accruals occur.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 4 - CASH, CASH EQUIVALENTS AND INVESTMENTS

Cash resources of several individual funds are combined to form a pool of cash, cash equivalents and investments. In addition, investments are separately held by a number of individual funds. Statutes require the classification of funds held by the City into three categories:

Category 1 consists of "active" funds - those funds required to be kept in "cash" or "near cash" status for immediate use by the City. Such funds must be maintained either as cash in the City Treasury or in depository accounts payable or withdrawable on demand, including negotiable order of withdrawal (NOW) accounts.

Category 2 consists of "inactive" funds - those funds not required for use within the current five year period of designation of depositories. Inactive funds may be deposited or invested only as certificates of deposit maturing no later than the end of the current period of designation of depositories.

Category 3 consists of "interim" funds - those funds not needed for immediate use but needed before the end of the current period of designation of depositories. Interim funds may be invested or deposited in the following securities:

- United States treasury notes, bills, bonds, or any other obligation or security issued by the United States treasury or any other obligation guaranteed as to principal or interest by the United States;
- Bonds, notes, debentures, or any 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;
- 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;
- Interim deposits in eligible institutions applying for interim funds;
- Bonds and other obligations of the State of Ohio;
- No-load money market mutual funds consisting exclusively of obligations described in the first two bullets of this section and repurchase agreements secured by such obligations, provided that investments in securities described in this division are made only through eligible institutions, and
- The State Treasury Asset Reserve of Ohio (STAR Ohio).

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 4 - CASH, CASH EQUIVALENTS AND INVESTMENTS (Continued)

Ohio Law requires that deposits be placed in eligible banks or savings and loan associations located in Ohio. Any public depository in which the City places deposits must pledge as collateral eligible securities of aggregate market value equal to the excess of deposits not insured by the Federal Deposit Insurance Corporation (FDIC). The securities pledged as collateral are pledged to a pool for each individual financial institution in amounts equal to at least 105% of the carrying value of all public deposits held by each institution. Obligations that may be pledged as collateral are limited to obligations of the United States and its agencies and obligations of any state, county, municipal corporation or other legally constituted authority of any other state, or any instrumentality of such county, municipal corporation or other authority. Based upon criteria described in GASB Statement No. 3, "*Deposits With Financial Institutions, Investments (including Repurchase Agreements) and Reverse Repurchase Agreements*," collateral held in single financial institution collateral pools with securities being held by the pledging financial institution's agent in the pool's name are classified as Category 3.

The GASB has established risk categories for deposits and investments as follows:

Deposits:

- Category 1 Insured or collateralized with securities held by the City or by its agent in the City's name.
- Category 2 Collateralized with securities held by the pledging financial institution's trust department or agent in the City's name.
- Category 3 Collateralized with securities held by the pledging financial institution's trust department or agent but not in the City's name.

Investments:

- Category 1 Insured or registered with securities held by the City or its agent in the City's name.
- Category 2 Uninsured and unregistered with securities held by the counterparty's trust department or agent in the City's name.
- Category 3 Uninsured and unregistered with securities held by the counterparty or by its trust department or agent but not in the City's name.

A. Deposits

At year end the carrying amount of the City's deposits was \$525,886 and the bank balance \$553,616. The Federal Deposit Insurance Corporation (FDIC) covered \$200,000 of the bank balance. All remaining deposits were classified as Category 3.

Investment earnings of \$12,710 earned by other funds were credited to the General Fund as required by state statute.

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2004**

NOTE 4 - CASH, CASH EQUIVALENTS AND INVESTMENTS (Continued)

B. Investments

The City's investments at December 31, 2004 are summarized below:

<u>Categorized Investments</u>	<u>Category 2</u>	<u>Fair Value</u>
Repurchase Agreement	\$103,599	\$103,599
<u>Non-Categorized Investments</u>		
STAR Ohio	N/A	10,306
Total Investments	<u>\$103,599</u>	<u>\$113,905</u>

C. Reconciliation of Cash, Cash Equivalents and Investments

The classification of cash, cash equivalents and investments on the financial statements is based on criteria set forth in GASB Statement No. 9. STAR Ohio and certificates of deposit with an original maturity of three months or less are treated as cash equivalents. The classification of cash and cash equivalents (deposits) for purposes of this note are based on criteria set forth in GASB Statement No. 3.

	<u>Cash and Cash Equivalents</u>	<u>Investments</u>
Per Balance Sheet	\$203,481	\$436,310
Certificates of Deposit (with maturities of more than 3 months)	436,310	(436,310)
Investments:		
STAR Ohio	(10,306)	10,306
Repurchase Agreement	<u>(103,599)</u>	<u>103,599</u>
Per GASB Statement No. 3	<u>\$525,886</u>	<u>\$113,905</u>

NOTE 5 - PROPERTY TAXES

Property taxes include amounts levied against all real estate and public utility property, and tangible personal property used in business and located in the City. Real property taxes (other than public utility) collected during 2004 were levied after October 1, 2003 on assessed values as of January 1, 2003 the lien date. Assessed values were 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 2004. Real property taxes are payable annually or semi-annually. The first payment is due January 20; the remainder is payable by June 20.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 5 - PROPERTY TAXES (Continued)

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 of the year assessed. Single county taxpayers may pay annually or semi-annually. The first payment is due April 30; the remainder is 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 is currently assessed at 100 percent of its true value. Public utility property taxes are payable on the same dates as real property taxes described previously.

The County Treasurer collects property taxes on behalf of all taxing districts in the County including the City of East Palestine. The County Auditor periodically remits to the City its portion of the taxes collected.

The full property tax rate for all City operations for the year ended December 31, 2004 was \$5.40 per \$1,000 of assessed value. The assessed value upon which the 2004 tax receipts was based was \$57,314,615. This amount constitutes \$49,188,880 in real property assessed value, \$2,791,330 in public utility assessed value, and \$5,334,405 in tangible personal property assessed value.

Ohio law prohibits taxation of property from all taxing authorities in excess of 1% of assessed value without a vote of the people. Under current procedures, the City's share is .54% (5.4 mills) of assessed value.

The City levies a tax of 1.0% on all salaries, wages, commissions and other compensation, on net profits earned within the City and on incomes of residents earned outside the City. Employers within the City are required to withhold income tax on employee compensation and remit the tax to the City either monthly or quarterly, as required. Corporations and other individual taxpayers are required to pay their estimated tax quarterly and file a declaration annually.

NOTE 6 - RECEIVABLES

Receivables at December 31, 2004 consisted of taxes, interest, accounts receivable, CDBG loans, special assessments, interfund receivables and intergovernmental receivables.

CITY OF EAST PALESTINE, OHIO

***Notes to the Basic Financial Statements
For the Year Ended December 31, 2004***

NOTE 7 - TRANSFERS

Following is a summary of transfers in and out for all funds for 2004:

Fund	Transfer In	Transfer Out
General Fund	\$163,562	\$152,008
Capital Improvement Fund	205,969	0
Other Governmental Funds	89,400	32,557
Total Governmental Funds	458,931	184,565
Water Fund	0	195,764
Wastewater Fund	16,610	95,212
Total Proprietary Funds	16,610	290,976
Totals	\$475,541	\$475,541

NOTE 8 - INTERFUND RECEIVABLES AND PAYABLES

The following is a summary of interfund loans receivable and payable for all funds for 2004:

Fund	Interfund Loans Receivable	Interfund Loans Payable
General Fund	\$0	\$710,000
Electric Trust Fund	2,807,008	0
Capital Improvement Fund	0	2,009,962
Other Governmental Funds	0	87,046
Totals	\$2,807,008	\$2,807,008

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2004**

NOTE 9 - CAPITAL ASSETS

A. Governmental Activities Capital Assets

Summary by category of changes in governmental activities capital assets at December 31, 2004:

<i>Historical Cost:</i>	Restated December 31, 2003	Additions	Deletions	December 31, 2004
Class	2003	Additions	Deletions	2004
<i>Capital assets not being depreciated:</i>				
Land	\$175,335	\$0	\$0	\$175,335
Construction in Progress	0	5,150	0	5,150
Subtotal	175,335	5,150	0	180,485
<i>Capital assets being depreciated:</i>				
Buildings	1,798,265	48,927	0	1,847,192
Improvements Other than Buildings	69,171	58,330	0	127,501
Machinery and Equipment	2,101,598	110,405	(75,589)	2,136,414
Infrastructure	3,285	151,594	0	154,879
Subtotal	3,972,319	369,256	(75,589)	4,265,986
Total Cost	\$4,147,654	\$374,406	(\$75,589)	\$4,446,471
 <i>Accumulated Depreciation:</i>				
Class	Restated December 31, 2003	Additions	Deletions	December 31, 2004
Buildings	(\$487,962)	(\$36,737)	\$0	(\$524,699)
Improvements Other than Buildings	(10,345)	(4,277)	0	(14,622)
Machinery and Equipment	(641,950)	(133,678)	75,589	(700,039)
Infrastructure	(665)	(2,821)	0	(3,486)
Total Depreciation	(\$1,140,922)	(\$177,513) *	\$75,589	(\$1,242,846)
<i>Net Value:</i>	\$3,006,732			\$3,203,625

* Depreciation expenses were charged to governmental functions as follows:

Security of Persons and Property	\$81,596
Leisure Time Activities	37,762
Transportation	33,461
General Government	24,694
Total Depreciation Expense	\$177,513

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2004**

NOTE 9 - CAPITAL ASSETS (Continued)

B. Business-Type Activities Capital Assets

Summary by Category at December 31, 2004:

<i>Historical Cost:</i>	Restated			
Class	December 31, 2003	Additions	Deletions	December 31, 2004
<i>Capital assets not being depreciated:</i>				
Land	\$177,511	\$0	\$0	\$177,511
Construction in Progress	194,168	310,001	0	504,169
Subtotal	371,679	310,001	0	681,680
<i>Capital assets being depreciated:</i>				
Buildings and Improvements	2,343,095	80,362	0	2,423,457
Machinery and Equipment	1,440,318	88,233	(201,917)	1,326,634
Infrastructure	6,582,635	2,512	0	6,585,147
Subtotal	10,366,048	171,107	(201,917)	10,335,238
Total Cost	\$10,737,727	\$481,108	(\$201,917)	\$11,016,918
 <i>Accumulated Depreciation:</i>				
Class	Restated December 31, 2003	Additions	Deletions	December 31, 2004
Buildings and Improvements	(\$1,214,738)	(\$56,106)	\$0	(\$1,270,844)
Machinery and Equipment	(789,123)	(148,311)	134,099	(803,335)
Infrastructure	(1,649,948)	(152,846)	0	(1,802,794)
Total Depreciation	(\$3,653,809)	(\$357,263)	\$134,099	(\$3,876,973)
<i>Net Value:</i>	\$7,083,918			\$7,139,945

NOTE 10 – DEFINED BENEFIT PENSION PLANS

All of the City’s full-time employees participate in one of two separate retirement systems which are cost-sharing multiple employer defined benefit pension plans.

A. Ohio Public Employees Retirement System (the “Ohio PERS”)

The following information was provided by the Ohio PERS to assist the City in complying with GASB Statement No. 27, “Accounting for Pensions by State and Local Government Employers.”

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 10 – DEFINED BENEFIT PENSION PLANS (Continued)

A. Ohio Public Employees Retirement System (the “Ohio PERS”) (Continued)

All employees of the City, except full-time uniformed police officers and full-time firefighters, participate in one of the three pension plans administered by the Ohio PERS: the Traditional Pension Plan (TP), the Member-Directed Plan (MD), and the Combined Plan (CO). The TP Plan is a cost-sharing multiple employer defined benefit pension plan. The MD Plan is a defined contribution plan in which the member invests both member and employer contributions (employer contributions vest over five years at 20% per year). Under the MD Plan members accumulate retirement assets equal to the value of member and (vested) employer contributions plus any investment earnings thereon. The CO Plan is a cost-sharing multiple-employer defined benefit pension plan that has elements of both a defined benefit and defined contribution plan. Under the CO Plan employer contributions are invested by the retirement system to provide a formula retirement benefit similar in nature to the TP Plan. Member contributions, the investment of which is self-directed by the members, accumulate retirement assets in a manner similar to the MD Plan.

The Ohio PERS provides retirement, disability, survivor and death benefits and annual cost-of-living adjustments to members of the TP Plan and CO Plan. Members of the MD Plan do not qualify for ancillary benefits. Chapter 145 of the Ohio Revised Code provides statutory authority to establish and amend benefits. The Ohio Public Employees Retirement System issues a stand-alone financial report that includes financial statements and required supplementary information for the Ohio PERS. Interested parties may obtain a copy by making a written request to 277 East Town Street, Columbus, Ohio 43215-4642 or by calling (614) 222-6701 or 1-800-222-7377.

The Ohio Revised Code provides statutory authority for employee and employer contributions. For 2004, employee and employer contribution rates were consistent across all three plans (TP, MD and CO). The employee contribution rate is 8.5%. The 2004 employer contribution rate for local government employer units was 13.55%, of covered payroll, 9.55% to fund the pension and 4.0% to fund health care. The contribution requirements of plan members and the City are established and may be amended by the Public Employees Retirement Board. The City's contributions to the Ohio PERS for the years ending December 31, 2004, 2003 and 2002 were \$149,520, \$149,228 and \$153,216, respectively, which were equal to the required contributions for each year.

The Ohio PERS provides postemployment health care benefits to age and service retirees with ten or more years of qualifying Ohio service credit and to primary survivor recipients of such retirees. Health care coverage for disability recipients is also available. The health care coverage provided by the Ohio PERS is considered an Other Postemployment Benefit (OPEB) as described in GASB Statement No. 12. A portion of each employer's contribution to the Ohio PERS is set aside for the funding of post retirement health care. The Ohio Revised Code provides statutory authority requiring public employers to fund postemployment health care through their contributions to the Ohio PERS. The portion of the 2004 employer contribution rate (identified above) that was used to fund health care for the year 2004 was 4.0% of covered payroll which amounted to \$44,139.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 10 – DEFINED BENEFIT PENSION PLANS (Continued)

A. Ohio Public Employees Retirement System (the “Ohio PERS”) (Continued)

The significant actuarial assumptions and calculations relating to postemployment health care benefits were based on the Ohio Public Employees Retirement System’s latest actuarial review performed as of December 31, 2003. An entry age normal actuarial cost method of valuation is used in determining the present value of OPEB. The difference between assumed and actual experience (actuarial gains and losses) becomes part of unfunded actuarial accrued liability. All investments are carried at market value. For actuarial valuation purposes, a smoothed market approach is used. Under this approach assets are adjusted annually to reflect 25% of unrealized market appreciation or depreciation on investment assets. The investment assumption rate for 2003 was 8.0%. An annual increase of 4.0% compounded annually, is the base portion of the individual pay increase assumption. This assumes no change in the number of active employees. Additionally, annual pay increases, over and above the 4.0% base increase, were assumed to range from 0.5% to 6.3%. Health care costs were assumed to increase 4.0% annually plus an additional factor ranging from 1% to 6% for the next 8 years. In subsequent years (9 and beyond) health care costs were assumed to increase 4% (the projected wage inflation rate).

Benefits are advanced-funded on an actuarially determined basis. The number of active contributing participants was 369,885. The actuarial value of the Ohio PERS net assets available for OPEB at December 31, 2003 is \$10.5 billion. The actuarially accrued liability and the unfunded actuarial accrued liability, based on the actuarial cost method used, were \$26.9 billion and \$16.4 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 Ohio PERS’ health care coverage to improve the financial solvency of the fund in response to skyrocketing health care costs.

Under the HCPP, retirees eligible for health care coverage will receive a graded monthly allocation based on their years of service at retirement. The Plan incorporates a cafeteria approach, offering a broad range of health care options that allow benefit recipients to use their monthly allocation to purchase health care coverage customized to meet their individual needs. If the monthly allocation exceeds the cost of the options selected, the excess is deposited into a Retiree Medical Account that can be used to fund future health care expenses.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 10 – DEFINED BENEFIT PENSION PLANS (Continued)

B. Ohio Police and Fire Pension Fund (the “OP&F Fund”)

All City full-time police officers and full-time firefighters participate in the OP&F Fund, a cost-sharing multiple-employer defined benefit pension plan. The OP&F Fund provides retirement and disability benefits, annual cost of living adjustments and death benefits to plan members and beneficiaries. Contribution requirements and benefit provisions are established by the Ohio State Legislature and are codified in Chapter 742 of the Ohio Revised Code. The Ohio Police and Fire Pension Fund issues a stand-alone financial report that includes financial statements and required supplementary information for the OP&F Fund. Interested parties may obtain a copy by making a written request to 140 East Town Street, Columbus, Ohio 43215-5164 or by calling (614) 228-2975.

Plan members are required to contribute 10.0% of their annual covered salary, while employers are required to contribute 19.5% and 24.0% respectively for police officers and firefighters. The City's contributions to the OP&F Fund for the years ending December 31, 2004, 2003 and 2002 were \$56,184, \$57,685 and \$60,727 for police and \$11,319, \$10,982 and \$10,867 for firefighters, respectively, which were equal to the required contributions for each year.

The OP&F Fund provides postemployment health care coverage to any person who received or is eligible to receive a monthly 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 on a full-time or two-thirds basis. The health care coverage provided by the OP&F Fund is considered an Other Postemployment Benefit (OPEB) as described in GASB Statement No. 12. The Ohio Revised Code provides that health care costs paid from the funds of the OP&F Fund shall be included in the employer's contribution rate. The Ohio Revised Code also provides statutory authority allowing the Fund's Board of Trustees to provide postemployment health care coverage to all eligible individuals from the employer's contributions to the OP&F Fund.

The portion of the 2004 covered payroll that was used to fund postemployment health care benefits was \$22,330 representing 7.75% of covered payroll for police and \$3,655 representing 7.75% of covered payroll for fire. Health care funding and accounting was on a pay-as-you-go basis. In addition, since July 1, 1992 most retirees 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. As of December 31, 2003, the date of the last actuarial evaluation available, the number of participants eligible to receive health care benefits was 13,662 for police and 10,474 for firefighters. The OP&F Fund does not provide separate data on the funded status and funding progress of postemployment health care benefits. The Fund's total health care expenses for the year ended December 31, 2003 were \$150,853,148, which was net of member contributions of \$17,207,506.

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2004**

NOTE 11 - CAPITAL LEASES

The City leases several pieces of equipment under capital leases. The original cost of the equipment and the related liability are reported on the Government – wide Statement of Net Assets.

The following is a schedule of future minimum lease payments under the capital lease together with the present value of the net minimum lease payments as of December 31, 2004:

Year Ending December 31,	Capital Leases
2005	\$64,742
2006	50,336
2007	15,275
Minimum Lease Payments	130,353
Less amount representing interest at the City's incremental borrowing rate of interest	(8,529)
Present value of minimum lease payments	\$121,824

NOTE 12 - LONG-TERM OBLIGATIONS

Long-term debt and other long-term obligations of the City at December 31, 2004 were as follows:

	Balance December 31, 2003	Additions	Deductions	Balance December 31, 2004	Amount Due Within One Year
Governmental Activities:					
Ohio Public Works Commission Loan:					
Waterline Improvement	2004	\$0	\$286,752	\$0	\$286,752
Capital Leases		141,261	37,609	(57,046)	121,824
Compensated Absences Payable		162,676	152,047	(162,676)	152,047
Total Governmental Activities		303,937	476,408	(219,722)	560,623
Business-Type Activities:					
General Obligation Bonds:					
Various Purpose Bond	1999	1,980,000	0	(95,000)	1,885,000
Sewerage System Refunding Bond	2003	2,185,000	0	(40,000)	2,145,000
Total General Obligation Bonds:		4,165,000	0	(135,000)	4,030,000
Ohio Public Works Commission Loan:					
Waterline Improvement	2000	16,060	0	(2,920)	13,140
Ohio Water Development Authority Loans:					
Water Treatment Plant	1992	373,721	0	(41,525)	332,196
Sewer Project - Phase Two	1999	1,057,893	0	(53,823)	1,004,070
Total OWDA Loans:		1,431,614	0	(95,348)	1,336,266
Compensated Absences		111,773	121,662	(111,773)	121,662
Total Business-Type Activities		5,724,447	121,662	(345,041)	5,501,068
Totals		\$6,028,384	\$598,070	(\$564,763)	\$6,061,691

CITY OF EAST PALESTINE, OHIO

**Notes to the Basic Financial Statements
For the Year Ended December 31, 2004**

NOTE 12 - LONG-TERM OBLIGATIONS (Continued)

A. Principal and Interest Requirements

A summary of the City's future long-term debt funding requirements, including principal and interest payments as of December 31, 2004, follows:

Years	OPWC Loan		OWDA Loans	
	Principal	Interest	Principal	Interest
2005	\$17,258	\$0	\$96,538	\$44,483
2006	17,258	0	97,755	40,246
2007	17,258	0	98,999	35,982
2008	17,258	0	100,269	31,691
2009	15,798	0	101,569	28,383
2010-2014	71,686	0	445,320	80,702
2015-2019	71,686	0	357,827	26,182
2020-2024	71,690	0	37,989	411
2025-2031	0	0	0	0
Totals	<u>\$299,892</u>	<u>\$0</u>	<u>\$1,336,266</u>	<u>\$288,080</u>

Years	General Obligation Bond		Total	
	Principal	Interest	Principal	Interest
2005	\$145,000	\$205,460	\$258,796	\$249,943
2006	150,000	199,760	265,013	240,006
2007	150,000	193,678	266,257	229,660
2008	160,000	187,595	277,527	219,286
2009	165,000	178,480	282,367	206,863
2010-2014	975,000	761,975	1,492,006	842,677
2015-2019	1,035,000	497,525	1,464,513	523,707
2020-2024	475,000	296,500	584,679	296,911
2025-2031	775,000	117,850	775,000	117,850
Totals	<u>\$4,030,000</u>	<u>\$2,638,823</u>	<u>\$5,666,158</u>	<u>\$2,926,903</u>

B. Defeased Debt

In February 2003, the City defeased \$2,236,000 of FHA Loans for Sewer Improvements through the issuance of \$2,235,000 of General Obligation Bonds for Sewer System Improvement. The net proceeds of the 2003 Bonds have been invested in obligations guaranteed as to both principal and interest by the United States and placed in irrevocable escrow accounts which, including interest earned, will be used to pay the principal and interest on the refunded bonds. The refunded bonds, which have an outstanding balance of \$2,170,000 at December 31, 2004, are not included in the City's outstanding debt since the City has in-substance satisfied its obligations through the advance refunding. The refunding was undertaken to reduce total debt service payments over the next 26 years by \$363,369 and resulted in an economic gain of \$205,434. The acquisition price exceeded the net carrying amount of the old debt by \$30,054.

CITY OF EAST PALESTINE, OHIO

Notes to the Basic Financial Statements For the Year Ended December 31, 2004

NOTE 13 - INSURANCE AND RISK MANAGEMENT

The City is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees and natural disasters. The City is a participant in the Public Entities Pool of Ohio (the "Pool"). The Pool was established in 1987 and is administered under contract by American Risk Pooling Consultants Inc. to provide a program of property and casualty insurance for its member organizations throughout the State of Ohio.

The Pool's general objectives are to formulate, develop and administer a program of insurance, to obtain lower costs for that coverage, and to develop a comprehensive loss control program on behalf of the member political subdivisions. Political subdivisions joining the Pool may withdraw at the end of any coverage period upon 60 days prior written notice to the Pool. Under agreement, members who terminate participation in the Pool as well as current members are subject to a supplemental assessment or a refund, at the discretion of the Board of Trustees, depending on the ultimate loss experience of all the entities it insures for each coverage year. To date, there has been no assessments or refunds, due to the limited period of time that the Pool has been in existence and the nature of the coverage that is afforded to the participants.

The City of East Palestine obtained insurance coverage from the Pool for the years 2000 through 2005 for losses related to general liability, public officials liability, automobile, law enforcement liability, medical malpractice liability, and employee benefits liability.

Each participant makes an annual "contribution" to the Pool for the coverage they are provided, based on rates established by the Pool, using anticipated and actual results of operation for the various coverages provided. Participants are also charged for a "surplus contribution" that is used to build the Pool's retained earning account to fund the activities of the Pool. During 2004, the City of East Palestine made contributions to the Pool totaling \$71,534.

In the ordinary course of business, the Pool cedes a portion of its exposure to other insurers. These arrangements limit the Pool's maximum net loss on individual risks.

Treaty basis casualty excess of loss contracts in force at December 31, 2004 generally protect the Pool against individual losses over \$250,000.

Losses exceeding \$250,000 are reinsured with American Public Entity Excess Pool (APEEP) in an amount not to exceed \$2,000,000 per claim and \$5,000,000 in aggregate per year.

The Pool is, and ultimately the participants are, contingently liable should any reinsurer become unable to meet its obligations under the reinsurance agreements.

There has been no significant reduction in insurance coverages from coverages in the prior year. In addition, settled claims resulting from these risks have not exceeded commercial insurance coverages in any of the past three fiscal years.

Worker's Compensation claims are covered through the City's participation in the State of Ohio's program. The City pays the State Worker's Compensation System a premium based upon a rate per \$100 of payroll. The rate is determined based on accident history and administrative costs.

CITY OF EAST PALESTINE, OHIO

***Notes to the Basic Financial Statements
For the Year Ended December 31, 2004***

NOTE 14 - CONTINGENCIES

The City is a party to various legal proceedings which seek damages or injunctive relief generally incidental to its operations and pending projects. The City's management is of the opinion that the ultimate disposition of various claims and legal proceedings will not have a material effect, if any, on the financial condition of the City.

NOTE 15 - CONSTRUCTION COMMITMENTS

The City had the following contractual commitments at December 31, 2004:

<u>Project</u>	<u>Remaining Contractual Commitment</u>	<u>Expected Date of Completion</u>
Phase V - WWTP Improvements	\$2,580,225	2005
Grant St, East St & N. Avenue Repaving	48,640	2005
Leslie Run Creek Restoration Project	111,980	2006
Walking and Bike Trail Phase II	14,250	2005
Flood Damage - Sewer Plant	67,335	2005

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**Auditor of State
Betty Montgomery**

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

City of East Palestine
Columbiana County
82 Garfield Avenue
East Palestine, Ohio 44413

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 East Palestine (the City) as of and for the year ended December 31, 2004, which collectively comprise the City's basic financial statements and have issued our report thereon dated August 23, 2005. 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 to determine our auditing procedures in order to express our opinions on the financial statements and not to opine on the internal control over financial reporting. Our consideration of the internal control would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts material to the financial statements we audited may occur and not be timely detected by employees when performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider material weaknesses. In a separate letter to the City's management dated August 23, 2005, we reported other matters involving internal control over financial reporting we did not deem reportable conditions.

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 no instances of noncompliance or other matters we must report under *Government Auditing Standards*. In a separate letter to the City's management dated August 23, 2005, we reported other matters related to noncompliance we deemed immaterial.

City of East Palestine
Columbiana County
Independent Accountants' Report on Internal Control over Financial Reporting and on
Compliance and Other Matters Required by Government Auditing Standards
Page 2

We intend this report solely for the information and use of the audit committee, management, and City Council. It is not intended for anyone other than these specified parties.

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

Betty Montgomery
Auditor of State

August 23, 2005



**Auditor of State
Betty Montgomery**

88 East Broad Street
P.O. Box 1140
Columbus, Ohio 43216-1140
Telephone 614-466-4514
800-282-0370
Facsimile 614-466-4490

CITY OF EAST PALESTINE

COLUMBIANA 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
OCTOBER 18, 2005**