

Report of Independent Certified Public Accountants
on Financial Statements, Supplementary Information, and
Schedule of Expenditures of Federal and State Awards

To the Honorable Mayor and
Members of the City Council
City of Chattanooga, Tennessee

We have audited the accompanying financial statements of the governmental activities, business-type activities, the aggregate discretely-presented component units, each major fund, and the aggregate remaining fund information of the City of Chattanooga, Tennessee, as of and for the year ended June 30, 2006, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City of Chattanooga, Tennessee's management. Our responsibility is to express an opinion on these financial statements based on our audit. We did not audit the financial statements of the Chattanooga Metropolitan Airport Authority and the Chattanooga Area Regional Transit Authority, which represent 42 percent and 64 percent, respectively, of the assets and revenues of the discretely presented component units. Those financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for the Chattanooga Metropolitan Airport Authority and the Chattanooga Area Regional Transit Authority, is based solely on the report of the other auditors.

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 Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audit and the reports of the other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Chattanooga, Tennessee, as of June 30, 2006, and the respective changes in financial position and cash flows, where applicable, thereof and the respective budgetary comparison for the general fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated October 31, 2006, 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. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Management's discussion and analysis on pages iii through xiv of the Financial Section and the required supplementary information on pages 53-54 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Chattanooga, Tennessee's basic financial statements. The accompanying schedule of expenditures of federal and state awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is not a required part of the basic financial statements. The introductory section, combining and individual nonmajor fund and component unit financial statements, the budgetary comparison schedules included as other supplementary information, financial schedules, and statistical tables are presented for purposes of additional analysis and are not a required part of the basic financial statements. The combining and individual nonmajor fund and component unit financial statements, the budgetary comparison schedules included as other supplementary information, and financial schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory section and statistical tables have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

Haylett, Lewis & Bieter, PLLC

Chattanooga, Tennessee
October 31, 2006

In this section of the City of Chattanooga's annual financial report we offer readers a narrative overview and analysis of the City's financial activities for the fiscal year ended June 30, 2006. Please consider the information presented here in conjunction with the transmittal letter found at the front of this report and with the City's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

- The assets of the City of Chattanooga exceeded its liabilities at the close of the fiscal year by \$1.87 billion (net assets), an increase of \$22.7 million. Of this amount, \$81.3 million may be used to meet the government's ongoing obligations to citizens and creditors (unrestricted net assets), a \$1.3 million decrease over last year.
- While the net assets of our business-type activities increased \$12.0 million, or 2.5 percent, the net assets of our governmental activities increased \$10.7 million, or .8 percent. During the year, the City generated \$227.4 million in taxes and other revenues for governmental programs. This compares with \$219.1 million of expenses for these programs.
- The City of Chattanooga has opted to use depreciation rather than the maintenance method to report infrastructure assets. During the current fiscal year our governmental activities recognized depreciation expense of \$36.4 million including \$23.4 million on infrastructure assets alone.
- As of the close of the fiscal year, the City's governmental funds reported combined ending fund balances of \$88.1 million, an increase of \$4.3 million in comparison to last year. This increase is the result of several factors.
 - o Property tax and sales tax revenues were higher than expected reflecting a strong real estate and retail environment and the return of the second half of the a nine percent cut in state shared revenues in 2002. The hotel-motel tax was fully phased-in for the first time. Income from the use of property increased tremendously due to the sale of the old TB Hospital property and rising interest rates.
 - o All areas of government felt the impact of increased cost of fuel, utilities and pension contributions. These rising costs were offset by salaries savings due to vacancy control and a 52.5 percent decrease in capital expenditures due to substantial completion of the 21st Century Waterfront project.
- At the end of the current fiscal year, unreserved, undesignated fund balance for the General Fund was \$45.1 million, up \$6.2 million or 15.8 percent over prior year. This represents 26.8 percent of total General Fund expenditures and transfers out.
- The City's primary governmental debt decreased \$12.2 million (2.6 percent) during the current fiscal year. Business-type activity debt decreased from \$206.4 million to \$191.7 million, retiring more debt than was issued while governmental activities debt increased slightly from \$257.8 million to \$260.3 million due to draw down of previously authorized but unissued debt with the Tennessee Municipal League bond fund.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the City of Chattanooga's financial statements. The basic financial statements consist of three parts: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the financial statements. This report also contains supplementary information in addition to the basic financial statements.

GOVERNMENT-WIDE FINANCIAL STATEMENTS. The first two statements are government-wide financial statements. They are designed to provide readers with a broad overview of the City's finances in a manner similar to a private-sector business.

The government-wide financial statements are:

- **Statement Of Net Assets** – presents information about the City's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City is improving or deteriorating.
- **Statement Of Activities** – presents information showing how the City's net assets changed during the most recent fiscal year. All current year revenues and expenses are taken into account regardless of the timing of related cash flows. Thus revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal years (e.g., uncollected taxes and earned but unused vacation leave).

Both of the government-wide financial statements distinguish between functions of the City that are principally supported by taxes and intergovernmental revenues (governmental activities) and other functions that are intended to recover all, or a significant portion, of their costs through user fees and charges (business-type activities). The governmental activities of the City include general government, public safety, public works, parks and recreation and social services. The business-type activities include the City's electric, sewer and storm water systems, as well as solid waste disposal and housing management operations.

The government-wide financial statements include not only the City itself (known as the primary government) but also three legally separate entities (known as component units). The Chattanooga Metropolitan Airport Authority, the Chattanooga Area Regional Transportation Authority (CARTA) and the Chattanooga Downtown Redevelopment Corporation, although legally separate from the City, are important because the City is financially accountable for them.

Complete financial statements of the component units may be obtained from: (1) Chattanooga Metropolitan Airport Authority, P. O. Box 22444, Chattanooga, TN 37422; (2) CARTA, 1617 Wilcox Boulevard, Chattanooga, TN 37406 and (3) The Chattanooga Downtown Redevelopment Corporation, 427 City Hall Annex, 100 East 11th Street, Chattanooga, Tennessee 37402.

The government-wide financial statements begin on page 1 of this report.

FUND FINANCIAL STATEMENTS. The fund financial statements provide more detailed information about the most significant funds—not the City as a whole. Some funds are required by State

or Federal law or by bond covenants; other funds are established by the City to help it manage money for specific purposes (i.e. economic development projects) or to show that it is meeting legal responsibilities for how certain taxes, grants and other monies are used (i.e. grants received from the U. S Department of Housing and Urban Development).

All the funds of the City can be divided into three types of funds: (1) governmental funds, (2) proprietary funds, and (3) fiduciary funds.

- **Governmental Funds** – The City’s basic services are included in governmental funds. The focus of these funds is on (1) how cash and other financial assets that can readily be converted to cash were received and used and (2) what remains at the end of the fiscal year for future spending. This detailed short-term view helps in determining whether there are more or fewer financial resources that can be spent in the near future to finance the City’s programs. Because this information does not include the additional long-term focus of the government-wide statements, we provide additional information after the governmental fund statements that explain the differences between the long-term view and the short-term view.

The City maintains a general fund, multiple special revenue funds, a debt service fund, a capital projects fund and two permanent funds as governmental funds. Information is presented separately in the governmental statements for the General Fund and the capital projects fund since both of these are considered major funds. Data for the other funds is combined into a single column with individual fund data for each of these nonmajor governmental funds provided in the other supplementary information section of this report.

The City of Chattanooga adopts an annual budget for the General Fund, special revenue funds and the debt service fund. Budgetary comparisons are provided for these funds to demonstrate compliance with the budget: the General Fund budgetary comparison is found in the fund statements of this report and comparisons for special revenue funds and the debt service fund are provided in the other supplementary information section of this report. Both the capital projects fund and the permanent funds are excluded from budgetary reporting since neither adopts an annual budget.

The governmental fund financial statements begin on page 4 of this report.

- **Proprietary Funds** – Services for which the City charges customers a fee are generally reported in proprietary funds. Proprietary funds, like the government-wide statements, provide both long-term and short-term financial information. The City of Chattanooga maintains two different types of proprietary funds: enterprise funds and an internal service fund.

Enterprise funds are the same as business-type activities in the government-wide financial statements but provide more detail and additional information, such as cash flows. The Electric Power Board (EPB), Interceptor Sewer System, Storm Water Management and Solid Waste are considered major funds. The only other fund, Housing Management, is also shown on the face of the proprietary fund financial statements.

Internal service fund provides services for other City activities. The City of Chattanooga accounts for maintenance of City vehicles and risk financing in the internal service fund. Because these services predominantly benefit governmental rather than business-type functions, they have been included in governmental activities in the government-wide financial statements.

The proprietary fund statements begin on page 9 of this report.

- **Fiduciary Funds** – These funds are used to account for resources held for the benefit of others outside the government. The City maintains two pension trust funds for pension plans as the only fiduciary funds. The City is responsible for ensuring that the assets are used for their intended purposes, however, we exclude these activities from the City’s government-wide financial statements since these assets cannot be used to finance City operations. The City’s fiduciary activities are reported in statements of fiduciary net assets and changes in fiduciary net assets in the fund financial statements.

The fiduciary fund financial statements begin on page 14 of this report.

As previously stated, the City includes three legally separate component units in the government-wide financial statements. Financial information is provided for each component unit beginning on page 16 of this report.

NOTES TO THE FINANCIAL STATEMENTS. The financial statements also include notes that provide additional information that is essential to a full understanding of the government-wide and fund financial statements.

The notes to the financial statements begin on page 18 of this report.

SUPPLEMENTARY INFORMATION. In addition to the basic financial statements discussed above, this report also contains supplementary information.

- **Required Supplementary Information** – Information about the City’s progress in funding its obligation to provide pension benefits to its employees.
- **Other Supplementary Information** – This includes the combining statements for nonmajor governmental funds, private-purpose trust funds and discretely presented component units. It also includes a more detailed budget to actual comparison for General Fund and budget to actual comparisons for special revenue funds and the debt service fund.

Both the required and other supplementary information can be found following the notes to the financial statements.

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

NET ASSETS. Net assets may serve over time as a useful indicator of a government’s financial position. Assets exceeded liabilities by \$1.87 billion at the close of the most recent fiscal year, an increase of \$22.7 million, or 1.2 percent, from last year.

By far the largest portion of the City’s net assets (94 percent) reflects its investment in capital assets (land, buildings, equipment, infrastructure, etc), less any related debt used to acquire those assets. Because

capital assets are used to provide services to citizens the assets are not available for future spending. It should be noted that although the City reports capital assets net of related debt, the resources needed to repay the debt must be provided from other sources.

A portion of the City's net assets, \$24.3 million or 1.3 percent, represents resources that are restricted in how they may be used. The remaining balance of \$81.3 million may be used to meet the City's ongoing obligations, a \$1.3 million decrease.

At the end of the fiscal year, the City of Chattanooga is able to report a positive net asset balance for the government as a whole, as well as for its governmental and business-type activities.

City of Chattanooga's Net Assets (in thousands)

	Governmental Activities		Business-type Activities		Total	
	2006	2005	2006	2005	2006	2005
Current and other assets	\$ 223,630	\$ 211,607	\$ 160,667	\$ 165,759	\$ 384,297	\$ 377,366
Capital assets	1,527,771	1,530,278	664,829	647,845	2,192,600	2,178,123
Total assets	<u>1,751,401</u>	<u>1,741,885</u>	<u>825,496</u>	<u>813,604</u>	<u>2,576,897</u>	<u>2,555,489</u>
Long-term debt outstanding	276,855	273,948	193,624	208,376	470,479	482,324
Other liabilities	104,870	109,003	134,717	120,073	239,587	229,076
Total liabilities	<u>381,725</u>	<u>382,951</u>	<u>328,341</u>	<u>328,449</u>	<u>710,066</u>	<u>711,400</u>
Net assets:						
Invested in capital assets, net of debt	1,269,926	1,277,884	491,352	457,613	1,761,278	1,735,497
Restricted	6,313	7,713	17,945	18,301	24,258	26,014
Unrestricted	93,438	73,337	(12,142)	9,241	81,296	82,578
Total net assets	<u>\$ 1,369,677</u>	<u>\$ 1,358,934</u>	<u>\$ 497,155</u>	<u>\$ 485,155</u>	<u>\$ 1,866,832</u>	<u>\$ 1,844,089</u>

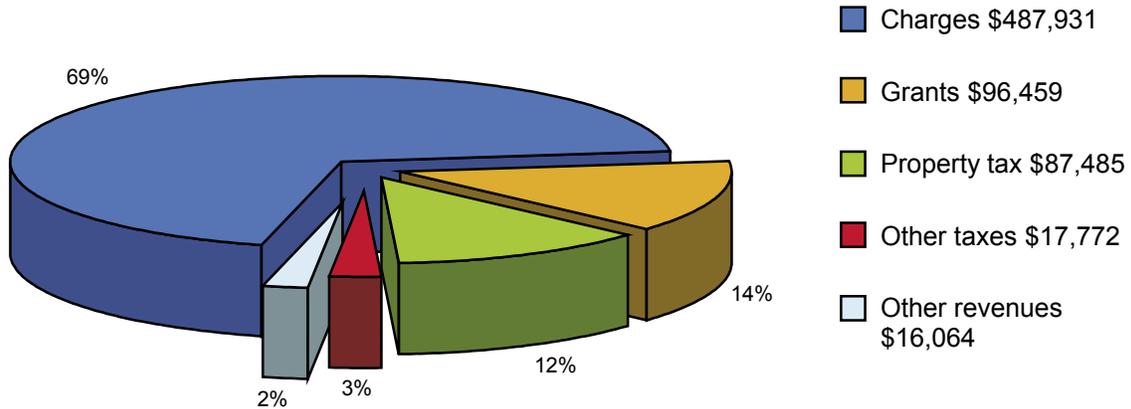
CHANGES IN NET ASSETS. Net assets of the City's governmental activities were \$1.4 billion, a \$10.7 million increase from the prior year. Of that balance \$1.28 billion are either restricted as to how they may be used or are invested in capital assets (buildings, roads, bridges, and so on). Therefore \$93.4 million remains to meet the City's ongoing obligations to citizens and creditors, a \$20.1 million increase.

During the current year the net assets of the business-type activities increased \$12.0 million or 2.5 percent to \$497.2 million. These net assets are dedicated solely to finance the continuing operations of the electric, sewer, and storm water systems, and solid waste disposal and housing management operations.

The following graphs summarize the sources of the City's total revenues of \$705.7 million and total program expenses of \$683.0 million. These graphs combine governmental and business-type information.

City Wide Sources of Revenue

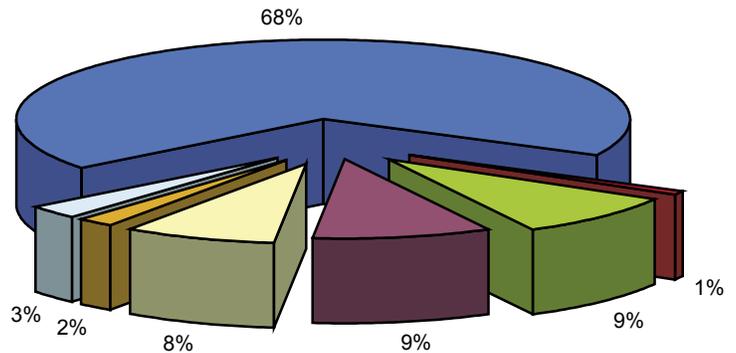
(In thousands)



City Wide Program Expenses

(In thousands)

- General Government \$60,153
- Safety \$64,368
- Public Works \$55,077
- Parks, Rec, Ed, Arts & Culture \$13,785
- Social Services \$19,199
- Business-Type \$463,893
- Govt Activities Interest \$6,493



In order to provide a complete picture of the changes in net assets of the City, information is provided separately for the net assets of governmental and business-type activities. See the table on the next page.

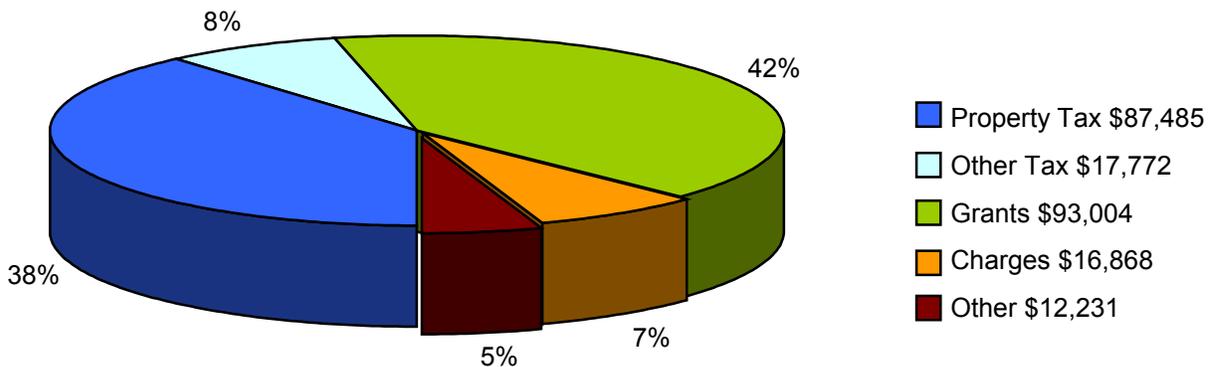
City of Chattanooga's Changes in Net Assets
(in thousands)

	Governmental		Business-type		Total	
	Activities		Activities			
	2006	2005	2006	2005	2006	2005
Revenues						
Program revenues:						
Charges for services	\$ 16,868	\$ 17,545	\$ 471,063	\$ 422,207	\$ 487,931	\$ 439,752
Grants and contributions	43,838	45,129	3,455	1,977	47,293	47,106
General revenues:						
Property taxes	87,485	89,491	-	-	87,485	89,491
Other taxes	17,772	14,388	-	-	17,772	14,388
Investment income	3,441	1,546	3,016	1,942	6,457	3,488
Miscellaneous	-	-	817	185	817	185
Unrestricted grants	49,166	48,501	-	-	49,166	48,501
Change in equity interest	8,790	-	-	-	8,790	-
Gain on sale of assets	-	81	-	-	-	81
Total revenues	227,360	216,681	478,351	426,311	705,711	642,992
Expenses						
Governmental activities:						
General government	60,153	59,851	-	-	60,153	59,851
Public safety	64,368	63,805	-	-	64,368	63,805
Public works	55,077	54,324	-	-	55,077	54,324
Parks and recreation	13,785	13,563	-	-	13,785	13,563
Social services	19,199	21,530	-	-	19,199	21,530
Interest on long-term debt	6,493	6,004	-	-	6,493	6,004
Business-type activities:						
Electric utility	-	-	417,792	371,630	417,792	371,630
Sewer	-	-	35,395	33,607	35,395	33,607
Solid waste	-	-	4,678	4,260	4,678	4,260
Storm water	-	-	4,476	4,709	4,476	4,709
Housing management	-	-	1,552	1,698	1,552	1,698
Total expenses	219,075	219,077	463,893	415,904	682,968	634,981
Excess (deficiency) before special item and transfers	8,285	(2,396)	14,458	10,407	22,743	8,011
Transfers	2,458	(563)	(2,458)	563	-	-
Increase (decrease) in net assets	\$ 10,743	\$ (2,959)	\$ 12,000	\$ 10,970	\$ 22,743	\$ 8,011

GOVERNMENTAL ACTIVITIES. Current fiscal year revenues for the City’s governmental activities were \$227.4 million compared to \$216.7 million last year, up 4.9 percent. Current year expenses were \$219.1 million, approximately the same amount last year with a \$1,500 decrease.

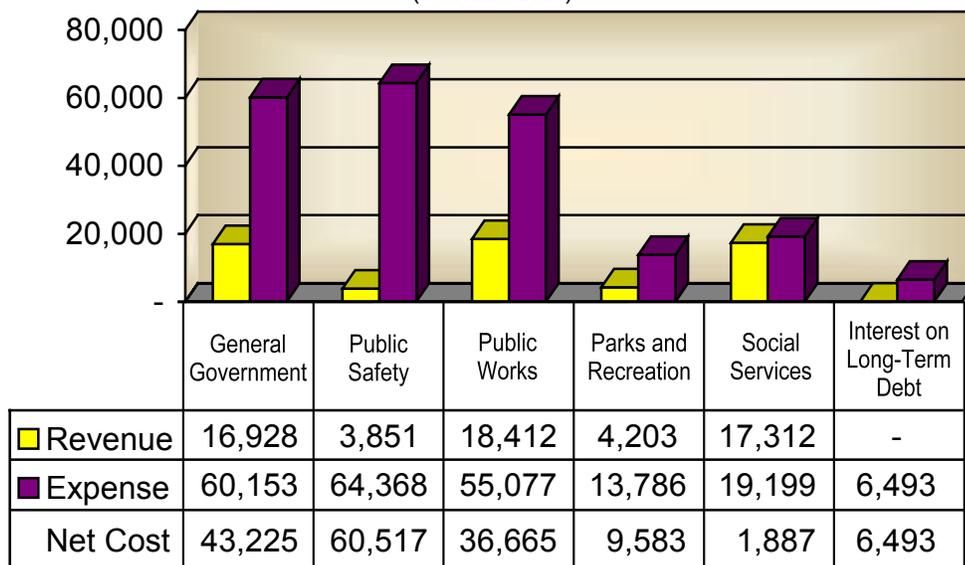
- The single largest source of governmental activity revenue, property taxes and payments in-lieu of tax, increased by \$1.1 million, or 1.2 percent due to a change in the method of accounting for \$3 million in PILOT by the EPB.
- The final payment on bonds to finance the Chattanooga Hamilton County Convention and Trade Center was made during the current fiscal year. Under terms of this joint venture Chattanooga and Hamilton County were to receive an equity interest in the portion of the center financed with these bonds after the debt is paid-in-full. The dollar value is based on the share of debt service paid; the City’s 2/3 equity (\$8.8 million) is added to the governmental activities. See Note 12 of the financial statements.
- Expenses for governmental activities were virtually unchanged from the prior year.

Revenues by Source - Governmental Activities
(In thousands)



Expenses and Program Revenues Governmental Activities

(In thousands)



BUSINESS-TYPE ACTIVITIES. Revenues for the City's business-type activities were \$478.4 million for the year just completed; this is a \$52.0 million increase or 12.2 percent. The increase in revenue was partially offset by a \$48.0 million, 11.5 percent, increase in expenses, to \$463.9 million. All business-type activities are briefly covered below.

Electric Power Board

- The largest source of business-type activity revenue is generated from the Electric Power Board. Operating revenue from customers increased by \$48.7 million, 13.0 percent, due to increased power usage as a result of an increase in cooling days and two rate increases passed on from TVA. This increase in revenue was largely offset by a \$47.9 million increase in operating costs including a \$42.9 million increase in purchased power costs.
- Total net assets of the Electric Power Board increased \$6.1 million to \$245.8 million for fiscal year 2006, an increase of 2.5 percent.
- Net assets invested in capital and restricted for use total \$270.3 million leaving a negative \$24.5 million available to finance day-to-day operations (unrestricted net assets). The negative unrestricted net assets are the result of high infrastructure start-up costs for the telecommunications segment.

Interceptor Sewer System

- Net assets of the Interceptor Sewer System increased \$2.9 million, 1.3 percent, to \$234.1 million.

- Operating revenues rose only \$533,329, 1.5 percent, while operating expenses rose \$2.0 million, 7.2 percent with \$1.4 million of the increase attributable to increased cost of electricity, natural gas and chemicals.
- Unrestricted net assets, those that can be used to finance on-going operations, decreased \$381,433 to \$32.2 million. An additional \$4.6 million is restricted for future capital spending.

Solid-Waste Fund

- The City of Chattanooga operates a municipal solid waste landfill. In 1991 the Environmental Protection Agency (EPA) issued an unfunded Federal mandate establishing closure and postclosure care requirements for such landfills. As a result of an aggressive program to meet these requirements, the Solid Waste Fund remains in a negative net asset position. However during fiscal year 2006 net assets increased by \$1.3 million or 8.2 percent. This follows a \$2.0 million increase in fiscal year 2005.
- To date the City has accrued liabilities of \$4.8 million for a closed landfill and \$5.2 million for a landfill currently in operation, a \$458,000 or 4.8 percent increase over last year. Many of these costs are being financed through general obligation bonds.
- The major customer of the landfill is the City itself. During the current fiscal year tipping fees from the City of Chattanooga were \$4.8 million, 88.5 percent of total tipping fees.

Stormwater Management

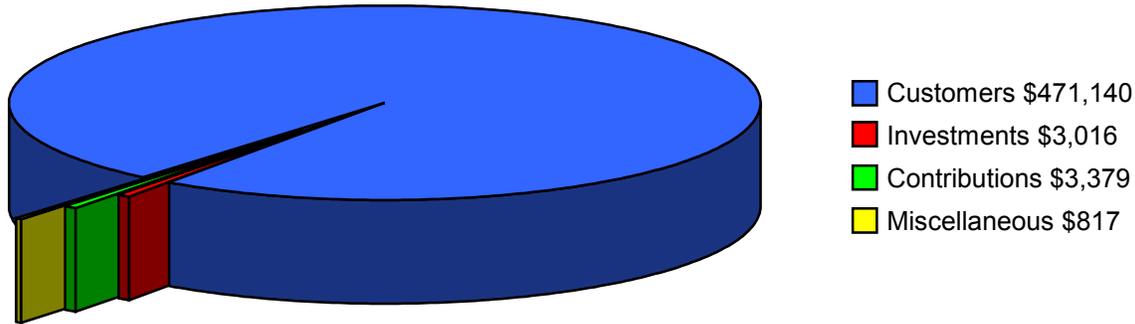
- The Stormwater Fund, established to comply with EPA guidelines, now has \$28.3 million in net assets, an increase of \$2.0 million, 7.4 percent, from last year.
- \$22.6 million of the net assets are invested in capital assets as a result of the aggressive capital campaign designed to continually improve storm water drainage and discharge within the City. This is a \$1.9 million, 9.0 percent increase.
- The amount set aside for capital improvements and the amount available to fund day-to-day operations increased from a combined \$5.6 million to \$6.2 million. Capital improvements are being paid from net assets instead of being funded through debt.

Housing Management

- The Housing Management Fund reported \$1.2 million in rental income, a decrease of 12.0 percent from last year. During the same period operating expenses decreased 17.3 percent to \$1.2 million.
- The fund ended the year with net assets of \$4.0 million, a decrease of \$287,000, or 6.6 percent. All of the net assets are invested in capital leaving a deficit of \$301,800 in assets available to meet on-going operations.

The following graph presents the major sources of revenue for business-type activities. Also presented is a chart showing the operating expense of each business-type activity as compared to operating revenue generated.

**Revenues by Source
Business-Type Activities**
(In thousands)



**Operating Expenses and Revenues
Business-Type Activities**
(in thousands)

	Electric	Sewer	Solid Waste	Storm Water	Housing
Revenue	\$ 422,143	\$ 36,510	\$ 5,552	\$ 5,730	\$ 1,204
Expense	413,741	30,386	3,498	3,712	1,220
Operating income (loss)	\$ 8,402	\$ 6,124	\$ 2,054	\$ 2,018	\$ (16)

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

The City of Chattanooga uses fund accounting to help it control and manage money for particular purposes or to demonstrate compliance with legal requirements. The following provides a more detailed analysis of the City's funds.

GOVERNMENTAL FUNDS. Governmental funds focus on providing information on the near-term flow of resources. The City's governmental funds reported a combined fund balance of \$88.1 million at the end of the fiscal year. 61.9 percent of this amount (\$54.6 million) is available for day-to-day operations (unreserved fund balance). All of the governmental funds reported a positive ending fund balance. Information about the major governmental funds is presented below.

General Fund. This is the chief operating fund of the City of Chattanooga. Total fund balance of the City's General Fund increased by 18.1 percent or \$8.6 million to \$56.0 million during the fiscal year. Unreserved fund balance was \$51.7 million, of which \$6.6 million is designated for future spending. During the fiscal year unreserved, undesignated fund balance increased \$6.2 million or 15.8 percent. Key factors are as follows:

- Total revenues increased \$5.3 million from the prior year with most categories of revenue seeing an increase.
 - o During the current fiscal year \$3.1 million of payments in-lieu of tax from EPB, an enterprise fund of the City, were reclassified from tax to transfers. Without the EPB revenue in either year, property tax increased \$1.1 million 1.2 percent over last year.
 - o Licenses and permits were \$179,000 higher, 4.4 percent, primarily due to an increase in construction related permits.
 - o Intergovernmental revenues increased \$4.0 million or 7.7 percent over the prior year with county-wide sales tax being the largest component. County-wide sales tax increased \$1.5 million, 6.3 percent, while state sales tax increased \$981,000 or 10.4 percent. State income tax increased almost 43 percent or \$922,000. These increases are directly related to consumer spending and increased investment returns for Chattanooga investors.
 - o Charges for services increased 4.3 percent or \$162,000. During the year the preservation fees for future renovations of the Memorial Auditorium and Tivoli Theatre were increased resulting in a \$64,000 increase. Certificates of occupancy, phased construction review fees and technology fees for City court also increased.
 - o Fines, Forfeitures and Penalties were up almost \$62,000 or 4.4 percent. The largest change was in parking tickets.
 - o Interest income increased \$1.7 million, 143 percent, due to the improved interest rate environment.
 - o The old childrens hospital building was sold for \$1.1 million to a neighboring health care facility. The sale was the major factor in the increase of miscellaneous revenue.
- Total expenditures decreased almost \$168,000 from the previous year.
 - o Personnel costs rose by approximately \$1.8 million or 2.2 percent over last year. Due to vacancy controls in place, wages rose only \$486,000 or .7 percent. The largest increase was in pension contributions which increased 16.2 percent, \$1.2 million.
 - o General Fund's share of lease payments due under a lease agreement with the Chattanooga Downtown Redevelopment Corporation decreased by almost \$621,000. Although funding from the sales tax generated in the tourist development zone decreased by \$296,800 because of relocation of a car dealership, there was an increase in funding from operations of The Chattanooga.
 - o Other changes include a decrease in injured on duty costs of \$707,000 reflecting a reduction in the number of major cases and a decrease in fire hydrant maintenance costs of \$550,000. These were partially offset by \$600,000 in additional funding for the liability insurance fund. They were also offset by increases in utilities and vehicle fuel costs of \$2.9 million.

Capital Projects Fund. This fund focuses on project-to-date costs for many projects within the City. At the end of the year, the fund reported \$11.5 million in fund balance all of which was reserved for completion of projects already begun. Fund balance for this fund fluctuates from year to year based on

debt issued and expenditures for projects; new debt increases fund balance while construction decreases it. For fiscal year 2006 there was a \$5.1 million decrease. Analysis of project income and expenditures follows.

- Cash inflows for the year include \$10.1 million in notes payable, \$3.4 million received from federal, state and county governments, \$6.2 million in transfers from General Fund and \$2.4 combined from the Community Development and Hotel-Motel Tax funds.
- Current year expenditures of \$27.2 million include \$6.2 million for construction of the waterfront development, \$9.2 million for street, traffic light and streetscape improvements, \$2.1 million for park improvements, \$3.5 million for fire and police equipment and \$2.0 million on renovation of City Hall.

PROPRIETARY FUNDS. The City's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail. As the City completed the fiscal year its proprietary funds, which include both enterprise funds and an internal service fund, had combined net assets of \$499.1 million.

- There is a shortage of \$10.5 million to meet on-going obligations as a result of the use of EPB net assets for infrastructure construction prior to issuance of bonds as previously discussed. The majority of net assets, \$491.7 million, is invested in capital assets with an additional \$17.9 million restricted for future use.
- Net assets of the enterprise funds rose \$12.0 million, 2.5 percent. Factors concerning the finances of the enterprise funds have already been addressed in the discussion of the City's business-type activities.
- The internal service fund serves City government by providing fuel, vehicle maintenance, fleet leasing and by accounting for the City's liability for self-insurance. Fund balance for this fund increased \$1.9 million to address a prior year deficit resulting from accruals for potential liabilities and an adjusted rate structure for fleet management.

GENERAL FUND BUDGETARY HIGHLIGHTS. The City's budget ordinance provides for the basic functions of City government, encompassing all major departments and agencies of the City. There were no differences between original and final budgets since reallocations within the General Fund are authorized in the budget ordinance.

When comparing final budgeted revenues to actual, there was a \$7.6 million surplus for the year with all major revenue categories higher than budget. Property tax collections for fiscal year 2006 exceeded budget expectations; the same is true of county-wide sales tax. As a result, taxes and intergovernmental revenues exceeded budget by \$1.6 million and \$2.0 million, respectively. Investment income was \$2.1 million more than anticipated.

Expenditures were less than budgetary estimates by \$3.7 million. All departments were below budget as a result of the continuation of vacancy control and performance management programs; salaries and benefits were under budget by \$2.7 million. The budget for General Fund anticipated using \$4.1 million of fund balance during the year; instead \$8.6 million was added to fund balance.

CAPITAL ASSET AND DEBT ADMINISTRATION

CAPITAL ASSETS. At the end of this year, the City had \$2.2 billion (net of accumulated depreciation) invested in capital assets, an increase of .66 percent. This investment includes land, buildings, utility system improvements, machinery and equipment, park facilities and infrastructure. The following table shows the investment in capital assets by both governmental activities and business-type activities.

City of Chattanooga's Capital Assets

(net of depreciation, in thousands of dollars)

	Governmental Activities		Business-type Activities		Total	
	2006	2005	2006	2005	2006	2005
Non-depreciable:						
Land & Easements	\$ 989,000	\$ 963,319	\$ 14,072	\$ 14,005	\$1,003,072	\$ 977,324
Work in progress	20,830	69,401	49,534	34,283	70,364	103,684
Depreciable:						
Buildings	111,709	116,161	62,173	52,899	173,882	169,060
Equipment	26,257	27,123	231,387	237,361	257,644	264,484
Improvements	7,987	7,914	-	-	7,987	7,914
Infrastructure	371,988	346,360	307,663	309,297	679,651	655,657
Total	<u>\$1,527,771</u>	<u>\$1,530,278</u>	<u>\$ 664,829</u>	<u>\$ 647,845</u>	<u>\$2,192,600</u>	<u>\$2,178,123</u>

Highlights for this year's major capital asset additions:

- Land purchases include \$475,000 for greenways and purchase of a Civil War landmark.
- The major additions to work-in-progress are \$6.2 million on the 21st Century Waterfront development, \$2.6 million for continued work on the Hope VI project, \$2.0 renovation costs for City Hall and \$640,000 for development of the Enterprise South Industrial Park.
- Equipment purchases include \$1.3 million for fire equipment (breathing apparatus, a rescue truck and a fire truck), \$1.0 for police cars and laptops in the vehicles and \$800,000 for public works equipment.
- Street improvements and street lighting of \$8.4 million were the major additions to infrastructure. An additional \$9.8 million of donated road beds and streets were accepted from contractors.
- The Electric Power Board invested \$44.7 million in plant assets for the year. This includes \$19.3 million in power distribution systems, \$16.2 in building under construction and \$5.5 million for telecommunications improvements.
- \$3.3 million was capitalized as new infrastructure for the Interceptor Sewer System.

The capital budget for fiscal year 2007 anticipates spending over \$30 million for various capital projects including \$4.1 million for expansion and upgrade of the City's parks and park facilities, \$8.6 million for various public works projects such as street improvements, curbs, gutters and sidewalks, \$1.7 million for fire equipment and building improvements, computer software replacement and upgrades of \$2.6 million, \$3.5 million for city vehicles, \$6.9 million for solid waste disposal and recycling and \$1.5 million for various storm water projects. \$12 million in bonds has been approved to help finance a portion of these projects.

More detailed information about the City's capital assets is presented in the notes to the financial statements.

DEBT ADMINISTRATION. At year-end the City had \$452.0 million in long-term debt outstanding. This is a \$12.2 million decrease (2.6 percent) from last year. Detail is shown in the table and narrative that follow.

City of Chattanooga's Long-term Debt
(in thousands)

	Governmental Activities		Business-type Activities		Total	
	2006	2005	2006	2005	2006	2005
General obligation bonds (backed by the City)	\$ 120,680	\$125,317	\$113,410	\$125,388	\$234,090	\$250,705
Revenue bonds (backed by specific revenues)	-	-	32,000	33,600	32,000	33,600
Notes payable	21,357	13,594	46,070	47,212	67,427	60,806
Capital leases	118,276	118,843	214	234	118,490	119,077
Total	<u>\$ 260,313</u>	<u>\$257,754</u>	<u>\$191,694</u>	<u>\$206,434</u>	<u>\$452,007</u>	<u>\$464,188</u>

- The City of Chattanooga maintains a "AA" rating from both Standard & Poor's and Fitch Investor's Service for general obligation debt and a rating of "1" for the CDRC swaption.
- City Charter limits the amount of general obligation debt a City can issue to 10 percent of the assessed value of all taxable property within the City's corporate limits. For the current fiscal year that limit is \$386.0 million. The City's tax-supported debt of \$84.3 million is well within that limit.

During the year the City issued the following new debt:

- Additional draws of \$1.4 million were made on a \$5.0 million Fannie Mae loan approved in FY04 to fund the Hope VI project, a governmental activity. The loan will be repaid by Community Development Block Grant program revenue. Currently \$2.5 million is outstanding.
- Additional draws of \$8.7 million were made on two state revolving loan funds for governmental activities capital. The total combined loan amount is \$31.0 million. At year-end there was \$14.7 million outstanding.
- \$1.3 million of notes payable for telecommunications equipment. The loan will be paid from revenue from EPB telecommunications operations; EPB is a business-type activity.

- Operations of River Pier Parking Garage were moved from the Chattanooga Downtown Redevelopment Corporation, a component unit of the City, to City governmental activities. This included \$186,703 outstanding on an equipment loan.

More detailed information about the City's long-term liabilities is presented in the notes to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The following factors were taken into account when adopting the General Fund budget for 2007:

- Conservative forecasts are for local and state tax collections to continue improving.
- Interest rates are on the rise with an increased availability of funds to invest.
- The local unemployment rate remains significantly below the state average of 4.6 percent at 3.8 percent and below the national average of 4.6 percent.

Anticipated revenues in the General Fund budget are \$179.0 million, up 5.1 percent from the 2006 budget. Property tax, county-wide and state sales tax collections are projected to grow by 2.4 percent, 6.6 percent and 11.7 percent, respectively, based on an improving economy. Interest earnings are estimated to increase over 100 percent due to increased available funds and rising interest rates. Fines, forfeitures and penalties are expected to increase by 22.2 percent based on current year collections.

Budgeted expenditures are expected to increase 5.1 percent to \$179.0 million from \$170.3 million. Salaries and fringe benefits are expected to increase by 3.6 percent while operations are estimated to increase 7.2 percent. The City will continue the vacancy control policy to manage the costs associated with salaries and benefits. There is an anticipated use of \$8.33 million in fund balance, \$8.0 million for capital with the remainder for the current year Office of Multicultural Affairs study not encumbered during the current fiscal year.

A modest increase in net assets for the City's business-type activities is expected during FY 2007.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

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

City of Chattanooga Finance Department
100 East 11th Street
Chattanooga, Tennessee 37402
(423) 757-5232
www.chattanooga.gov

CITY OF CHATTANOOGA, TENNESSEE

STATEMENT OF NET ASSETS
June 30, 2006

	Primary Government			Component Units
	Governmental Activities	Business-Type Activities	Total	
ASSETS				
Cash and cash equivalents	\$ 30,465,124	\$ 50,561,736	\$ 81,026,860	\$ 5,221,303
Investments	51,509,387	32,055,189	83,564,576	679,663
Receivables, net of allowance for uncollectibles	117,475,632	48,689,647	166,165,279	3,847,050
Net investment in capital lease	-	-	-	115,925,472
Internal balances	(15,352)	15,352	-	-
Due from component units	375,000	-	375,000	-
Due from primary government	-	-	-	329,749
Deferred charges	-	2,502,470	2,502,470	1,980,226
Inventories	1,640,943	6,530,332	8,171,275	332,046
Prepaid items	8,000	3,071,642	3,079,642	662,697
Other assets	-	3,979,090	3,979,090	-
Restricted assets:				
Cash and cash equivalents	-	-	-	2,285,570
Investments	1,727,094	13,185,689	14,912,783	13,863,617
Endowment investments	3,232,394	-	3,232,394	-
Receivables	-	75,962	75,962	94,446
Net pension assets	8,421,667	-	8,421,667	46,540
Equity interest in joint venture	8,789,979	-	8,789,979	-
Land and other nondepreciable assets	1,009,829,708	63,605,988	1,073,435,696	20,498,895
Other capital assets, net of accumulated depreciation	517,941,319	601,223,458	1,119,164,777	62,938,566
Total assets	1,751,400,895	825,496,555	2,576,897,450	228,705,840
LIABILITIES				
Accounts payable and accrued liabilities	15,614,913	89,821,167	105,436,080	4,699,975
Customer deposits	-	14,534,000	14,534,000	-
Due to component units	329,749	-	329,749	-
Due to primary government	-	-	-	375,000
Contracts payable	981,206	360,216	1,341,422	1,141,899
Unearned revenue	87,943,740	-	87,943,740	408,090
Accrued closure and post-closure care	-	10,013,509	10,013,509	-
Accrued postretirement benefits	-	9,709,000	9,709,000	-
Other liabilities	-	10,279,566	10,279,566	-
Long-term liabilities:				
Due within one year	11,608,216	16,605,380	28,213,596	3,200,000
Due in more than one year	265,246,117	177,018,769	442,264,886	139,938,920
Total liabilities	381,723,941	328,341,607	710,065,548	149,763,884
NET ASSETS				
Invested in capital assets, net of related debt	1,269,926,195	491,351,965	1,761,278,160	69,587,124
Restricted for:				
Capital projects	1,727,094	-	1,727,094	-
Debt service	1,296,631	-	1,296,631	14,647,529
Renewal and replacement	-	17,944,835	17,944,835	1,105,521
Permanent endowments:				
Expendable	45,786	-	45,786	-
Nonexpendable	3,243,029	-	3,243,029	-
Unrestricted	93,438,219	(12,141,852)	81,296,367	(6,398,218)
Total net assets	\$1,369,676,954	\$497,154,948	\$1,866,831,902	\$ 78,941,956

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

CITY OF CHATTANOOGA, TENNESSEE

STATEMENT OF ACTIVITIES
Year Ended June 30, 2006

Functions/Programs	Expenses	Program Revenues		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions
PRIMARY GOVERNMENT				
Governmental activities:				
General government	\$ 60,152,675	\$ 9,279,550	\$ 6,745,695	\$ 902,562
Public safety	64,367,574	1,121,281	920,135	1,809,520
Public works	55,077,404	2,392,789	4,861,437	11,157,855
Parks, recreation, education, arts & culture	13,785,184	2,910,484	721,364	570,856
Social services	19,199,188	1,163,593	16,148,374	-
Interest on long-term debt	6,493,154	-	-	-
Total governmental activities	<u>219,075,179</u>	<u>16,867,697</u>	<u>29,397,005</u>	<u>14,440,793</u>
Business-type activities:				
Electric utility	417,792,000	422,143,000	-	3,377,000
Sewer	35,395,214	36,509,866	-	2,000
Solid waste/sanitation	4,678,270	5,475,554	76,532	-
Storm water	4,475,706	5,730,458	-	-
Housing management	1,552,119	1,204,120	-	-
Total business-type activities	<u>463,893,309</u>	<u>471,062,998</u>	<u>76,532</u>	<u>3,379,000</u>
TOTAL PRIMARY GOVERNMENT	<u>\$ 682,968,488</u>	<u>\$ 487,930,695</u>	<u>\$ 29,473,537</u>	<u>\$ 17,819,793</u>
Component units:				
Airport authority	\$ 8,973,892	\$ 5,779,745	\$ 846,920	\$ 7,915,490
Transportation authority	16,817,049	4,347,431	6,084,288	6,191,217
Downtown redevelopment	17,878,134	17,856,241	-	-
TOTAL COMPONENT UNITS	<u>\$ 43,669,075</u>	<u>\$ 27,983,417</u>	<u>\$ 6,931,208</u>	<u>\$ 14,106,707</u>
General revenues:				
Property taxes				
Liquor and beer taxes				
Other taxes				
Grants and contributions not allocated to specific programs:				
County-wide sales taxes				
City allocation of state sales taxes				
City allocation of state income taxes				
Tourist Development Zone taxes				
Unrestricted investment earnings				
Miscellaneous				
Gain on equity interest in joint venture				
Endowment contributions				
Transfers				
Total general revenues and transfers				
Change in net assets				
Net assets, beginning				
Net assets, ending				

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

Net (Expense) Revenue and Changes in Net Assets			
Primary Government			Component Units
Governmental Activities	Business-type Activities	Total	
\$ (43,224,868)	\$ -	\$ (43,224,868)	\$ -
(60,516,638)	-	(60,516,638)	-
(36,665,323)	-	(36,665,323)	-
(9,582,480)	-	(9,582,480)	-
(1,887,221)	-	(1,887,221)	-
(6,493,154)	-	(6,493,154)	-
<u>(158,369,684)</u>	<u>-</u>	<u>(158,369,684)</u>	<u>-</u>
-	7,728,000	7,728,000	-
-	1,116,652	1,116,652	-
-	873,816	873,816	-
-	1,254,752	1,254,752	-
-	(347,999)	(347,999)	-
<u>-</u>	<u>10,625,221</u>	<u>10,625,221</u>	<u>-</u>
<u>(158,369,684)</u>	<u>10,625,221</u>	<u>(147,744,463)</u>	<u>-</u>
-	-	-	5,568,263
-	-	-	(194,113)
<u>-</u>	<u>-</u>	<u>-</u>	<u>(21,893)</u>
<u>-</u>	<u>-</u>	<u>-</u>	<u>5,352,257</u>
87,484,889	-	87,484,889	-
6,393,852	-	6,393,852	-
11,378,543	-	11,378,543	-
35,217,473	-	35,217,473	-
10,379,781	-	10,379,781	-
3,071,346	-	3,071,346	-
497,075	-	497,075	-
3,441,171	3,015,706	6,456,877	692,990
-	817,415	817,415	1,062,439
8,789,979	-	8,789,979	-
500	-	500	-
2,458,048	(2,458,048)	-	-
<u>169,112,657</u>	<u>1,375,073</u>	<u>170,487,730</u>	<u>1,755,429</u>
10,742,973	12,000,294	22,743,267	7,107,686
<u>1,358,933,981</u>	<u>485,154,654</u>	<u>1,844,088,635</u>	<u>71,834,270</u>
<u>\$ 1,369,676,954</u>	<u>\$ 497,154,948</u>	<u>\$ 1,866,831,902</u>	<u>\$ 78,941,956</u>

CITY OF CHATTANOOGA, TENNESSEE

BALANCE SHEET
GOVERNMENTAL FUNDS
June 30, 2006

	General	Capital Projects	Other Governmental Funds	Total Governmental Funds
ASSETS				
Cash and cash equivalents	\$ 6,574,610	\$ 7,901,940	\$11,229,186	\$ 25,705,736
Investments	42,613,849	4,320,864	9,534,162	56,468,875
Receivables, net of allowance for uncollectibles:				
Taxes	87,519,452	-	-	87,519,452
Accounts	-	77,344	57,990	135,334
Notes	1,340,112	859,777	-	2,199,889
Other	4,684,618	-	-	4,684,618
Due from other funds	-	385,616	3,947	389,563
Due from component units	375,000	-	-	375,000
Due from other governments	17,697,478	1,906,532	2,919,456	22,523,466
Inventories	851,163	-	-	851,163
Prepaid items	8,000	-	-	8,000
	<u>\$161,664,282</u>	<u>\$15,452,073</u>	<u>\$23,744,741</u>	<u>\$200,861,096</u>
LIABILITIES AND FUND BALANCES				
Liabilities:				
Accounts payable and accrued liabilities	\$ 5,043,639	\$ 2,148,342	\$ 1,294,954	\$ 8,486,935
Due to other funds	21,228	-	385,616	406,844
Due to other governments	1,071,013	510,101	-	1,581,114
Due to component unit	-	329,749	-	329,749
Deferred revenue	99,485,692	-	1,467,779	100,953,471
Contracts payable	-	981,206	-	981,206
	<u>105,621,572</u>	<u>3,969,398</u>	<u>3,148,349</u>	<u>112,739,319</u>
Fund balances:				
Reserved for:				
Encumbrances	2,147,839	-	64,469	2,212,308
Library endowment	-	-	3,242,029	3,242,029
Public safety awards	-	-	1,000	1,000
Inventories	851,163	-	-	851,163
Prepaid items	8,000	-	-	8,000
Capital improvements	-	11,482,675	-	11,482,675
Notes receivable	1,340,112	-	-	1,340,112
Debt service escrow	-	-	1,296,631	1,296,631
Unreserved, designated for:				
Debt service	-	-	5,842,577	5,842,577
Other long-term liabilities	-	-	718,404	718,404
Subsequent years' expenditures	6,557,035	-	-	6,557,035
Unreserved, undesignated, reported in:				
General fund	45,138,561	-	-	45,138,561
Special revenue	-	-	9,385,496	9,385,496
Permanent funds	-	-	45,786	45,786
	<u>56,042,710</u>	<u>11,482,675</u>	<u>20,596,392</u>	<u>88,121,777</u>
Total liabilities and fund balances	<u>\$161,664,282</u>	<u>\$15,452,073</u>	<u>\$23,744,741</u>	<u>\$200,861,096</u>

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

CITY OF CHATTANOOGA, TENNESSEE

RECONCILIATION OF THE BALANCE SHEET OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF NET ASSETS

June 30, 2006

Differences in amounts reported for governmental activities in the statement of net assets on page 1:

Fund balances - total governmental funds	\$ 88,121,777
Amounts reported for governmental activities in the statement of net assets are different because:	
Capital assets used in government activities are not financial resources and, therefore, are not reported in the funds.	1,527,385,851
Certain revenues will be collected after year-end but are not available soon enough to pay for the current period's expenditures and therefore are deferred in the funds.	13,009,731
The General Pension Plan has been funded in excess of annual required contributions, creating a net pension asset. This asset is not a currently available financial resource and is not reported in the funds.	8,421,667
The equity interest in the joint venture represents an interest in the capital assets of the joint venture. This interest is not a financial asset and, therefore, is not reported in the funds.	8,789,979
Internal service fund is used by management to charge the costs of fleet management and risk management activities to individual funds. The assets and liabilities of the internal service fund are included in governmental activities in the statement of net assets.	1,977,405
Long-term liabilities are not due and payable in the current period and therefore are not reported in the funds. Interest on long-term debt is not accrued in governmental funds, but rather is recognized as an expenditure when due. All liabilities, both current and long-term, are reported in the statement of net assets. This item consists of the following:	
General obligation serial bonds	\$ (120,680,396)
Less net deferred refunding and original premiums and discounts	667,177
Notes payable	(21,356,582)
Capital leases	(118,275,709)
Compensated absences	(16,712,236)
Accrued interest payable	(1,671,710)
	<u>(278,029,456)</u>
Net assets of governmental activities	<u>\$ 1,369,676,954</u>

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

CITY OF CHATTANOOGA, TENNESSEE

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS

Year Ended June 30, 2006

	General	Capital Projects	Other Governmental Funds	Total Governmental Funds
REVENUES				
Taxes	\$ 99,517,097	\$ -	\$ 3,640,518	\$ 103,157,615
Licenses and permits	4,272,090	-	-	4,272,090
Intergovernmental	56,359,718	3,431,378	23,326,335	83,117,431
Charges for services	3,936,968	-	355,739	4,292,707
Fines, forfeitures, and penalties	1,472,402	-	-	1,472,402
Investment income	2,892,000	494,694	562,789	3,949,483
Contributions and donations	74,665	184,325	155,723	414,713
Miscellaneous	5,648,712	957,983	2,284,851	8,891,546
Total revenues	<u>174,173,652</u>	<u>5,068,380</u>	<u>30,325,955</u>	<u>209,567,987</u>
EXPENDITURES				
Current:				
General government	44,267,249	-	19,111,776	63,379,025
Public safety	62,846,034	-	217,256	63,063,290
Public works	28,025,831	-	4,772,020	32,797,851
Parks, recreation, education, arts & culture	13,113,632	-	-	13,113,632
Community development	-	-	3,029,762	3,029,762
Capital outlay/fixed assets	-	27,155,459	1,139,177	28,294,636
Debt service:				
Principal retirement	-	-	7,735,136	7,735,136
Interest and fiscal charges	-	-	6,402,538	6,402,538
Total expenditures	<u>148,252,746</u>	<u>27,155,459</u>	<u>42,407,665</u>	<u>217,815,870</u>
Excess (deficiency) of revenues over (under) expenditures	<u>25,920,906</u>	<u>(22,087,079)</u>	<u>(12,081,710)</u>	<u>(8,247,883)</u>
OTHER FINANCING SOURCES (USES)				
Transfers in	3,142,000	8,536,311	16,976,882	28,655,193
Transfers out	(20,470,396)	(1,632,495)	(4,094,254)	(26,197,145)
Issuance of notes payable	-	10,106,804	-	10,106,804
Total other financing sources (uses)	<u>(17,328,396)</u>	<u>17,010,620</u>	<u>12,882,628</u>	<u>12,564,852</u>
Net change in fund balance	8,592,510	(5,076,459)	800,918	4,316,969
FUND BALANCE, beginning	<u>47,450,200</u>	<u>16,559,134</u>	<u>19,795,474</u>	<u>83,804,808</u>
FUND BALANCE, ending	<u>\$ 56,042,710</u>	<u>\$ 11,482,675</u>	<u>\$ 20,596,392</u>	<u>\$ 88,121,777</u>

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

CITY OF CHATTANOOGA, TENNESSEE
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES
Year Ended June 30, 2006

Differences in amounts reported for governmental activities in the statement of activities on pages 2 and 3:

Net change in fund balances - total governmental funds	\$ 4,316,969
Amounts reported for governmental activities in the statement of activities are different because:	
Capital outlay expenditures in governmental funds, that meet the capitalization threshold, are shown as capital assets in the statement of net assets.	26,803,524
Depreciation expense on governmental capital assets are included in the governmental activities in the statement of activities.	(36,280,624)
Contributions of capital assets are not reflected in the governmental funds, but are reported in the statement of activities. This item consists of streets contributed by developers.	9,848,077
The net effect of various transactions involving capital assets is to decrease net assets.	(3,045,453)
The gain on equity interest in joint venture is reported in the statement of activities. This gain does not provide current financial resources and is not reflected in the governmental funds.	8,789,979
Proceeds of long-term debt (e.g., bonds, notes) provide financial resources to governmental funds, while the repayment of principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets. Also, governmental funds report the effect of premiums, discounts, and deferred amounts on refundings when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities. This amount is the net effect of these differences in the treatment of long-term debt and related items.	(2,429,288)
The net revenues of internal service funds are reported with governmental activities.	1,942,329
Certain items reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditure in the governmental funds.	(679,130)
Governmental revenues that provide current financial resources are reported in the governmental funds, while revenues that will not be collected for several months after the fiscal year are deferred. The statement of activities includes certain revenues that do not provide current financial resources.	<u>1,476,590</u>
Change in net assets of governmental activities	<u>\$ 10,742,973</u>

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

CITY OF CHATTANOOGA, TENNESSEE
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN
FUND BALANCE - BUDGET AND ACTUAL
GENERAL FUND
Year Ended June 30, 2006

	Budgeted Amounts		Actual Amounts	Variance with Final Budget - Over (Under)
	Original	Final		
REVENUES				
Taxes	\$ 97,898,265	\$ 97,898,265	\$ 99,517,097	\$ 1,618,832
Licenses and permits	3,922,957	3,922,957	4,272,090	349,133
Intergovernmental	54,372,065	54,372,065	56,359,718	1,987,653
Charges for services	3,867,451	3,867,451	3,936,968	69,517
Fines, forfeitures, and penalties	1,172,500	1,172,500	1,472,402	299,902
Investment income	831,041	831,041	2,892,000	2,060,959
Contributions and donations	120,627	120,627	74,665	(45,962)
Miscellaneous	4,427,626	4,427,626	5,648,712	1,221,086
Total revenues	<u>166,612,532</u>	<u>166,612,532</u>	<u>174,173,652</u>	<u>7,561,120</u>
EXPENDITURES				
General government	37,483,336	37,483,336	36,224,858	(1,258,478)
Finance and Administration	9,451,292	9,451,292	8,409,280	(1,042,012)
Police	39,171,374	39,171,374	38,709,462	(461,912)
Fire	25,670,196	25,670,196	24,967,306	(702,890)
Public Works	28,223,437	28,223,437	28,090,859	(132,578)
Parks, recreation, education, arts & culture	13,307,898	13,307,898	13,206,377	(101,521)
Total expenditures	<u>153,307,533</u>	<u>153,307,533</u>	<u>149,608,142</u>	<u>(3,699,391)</u>
Excess of revenues over expenditures	<u>13,304,999</u>	<u>13,304,999</u>	<u>24,565,510</u>	<u>11,260,511</u>
OTHER FINANCING SOURCES (USES)				
Transfers In	3,141,612	3,141,612	3,142,000	388
Transfers out	(20,500,691)	(20,500,691)	(20,470,396)	30,295
Total other financing sources (uses)	<u>(17,359,079)</u>	<u>(17,359,079)</u>	<u>(17,328,396)</u>	<u>30,683</u>
Net change in fund balance	<u>\$ (4,054,080)</u>	<u>\$ (4,054,080)</u>	7,237,114	<u>\$ 11,291,194</u>
Adjustment for encumbrances			<u>1,355,396</u>	
Net change in fund balance (GAAP basis)			8,592,510	
FUND BALANCE at beginning of year (GAAP basis)			<u>47,450,200</u>	
FUND BALANCE at end of year (GAAP basis)			<u>\$ 56,042,710</u>	
EXPLANATION OF DIFFERENCES:				
REVENUES				
Actual amounts (budgetary basis) from the budgetary comparison schedule			\$ 174,173,652	
Differences - none			-	
Total revenues as reported on the statement of revenues, expenditures, and changes in fund balances - governmental funds			<u>\$ 174,173,652</u>	
EXPENDITURES				
Actual amounts (budgetary basis) from the budgetary comparison schedule			\$ 149,608,142	
Adjustment for encumbrances			<u>(1,355,396)</u>	
Total expenditures as reported on the statement of revenues, expenditures, and changes in fund balances - governmental funds			<u>\$ 148,252,746</u>	

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

CITY OF CHATTANOOGA, TENNESSEE

PROPRIETARY FUNDS

STATEMENT OF NET ASSETS

June 30, 2006

	Business-type Activities - Enterprise Funds						Governmental Activities - Internal Service Fund
	Major Funds				Other Fund		
	EPB	Interceptor Sewer System	Solid Waste/ Sanitation	Storm Water	Housing Management	Total	
ASSETS							
CURRENT ASSETS							
Cash and cash equivalents	\$ 38,238,000	\$ 1,806,109	\$ 4,538,992	\$ 5,748,079	\$ 230,556	\$ 50,561,736	\$ 4,759,388
Investments	1,899,000	29,637,073	-	519,116	-	32,055,189	-
Receivables:							
Customer service	43,983,000	4,273,198	90,495	708,801	-	49,055,494	226,785
Other	276,000	88,985	-	154	-	365,139	-
Less allowance for doubtful accounts	(564,000)	(500)	(200)	(386,309)	-	(951,009)	-
Inventories	5,982,000	548,332	-	-	-	6,530,332	789,780
Prepaid items	3,062,000	-	-	-	9,642	3,071,642	-
Due from other funds	-	13,330	338	1,684	-	15,352	1,929
Due from other governments	-	-	45,023	-	-	45,023	186,088
Other current assets	554,000	-	-	-	50,090	604,090	-
Total current assets	93,430,000	36,366,527	4,674,648	6,591,525	290,288	141,352,988	5,963,970
NONCURRENT ASSETS							
Restricted assets:							
Investments	-	1,416,523	11,769,166	-	-	13,185,689	-
Accounts receivable	-	-	75,962	-	-	75,962	-
Total restricted assets	-	1,416,523	11,845,128	-	-	13,261,651	-
Capital assets:							
Land	3,491,000	7,992,355	1,517,514	987,330	83,789	14,071,988	-
Buildings	16,871,000	41,303,711	1,717,098	-	8,719,028	68,610,837	589,948
Vehicles and machinery	399,941,000	30,522,189	5,075,045	1,385,875	957	436,925,066	1,212,825
Construction in progress	49,534,000	-	-	-	-	49,534,000	-
Sewer system	-	403,099,719	-	-	-	403,099,719	-
Storm water system	-	-	-	43,773,334	-	43,773,334	-
Telecommunications system	26,739,000	-	-	-	-	26,739,000	-
	496,576,000	482,917,974	8,309,657	46,146,539	8,803,774	1,042,753,944	1,802,773
Less accumulated depreciation	(195,776,000)	(168,118,426)	(5,170,852)	(7,476,456)	(1,382,764)	(377,924,498)	(1,417,597)
Net capital assets	300,800,000	314,799,548	3,138,805	38,670,083	7,421,010	664,829,446	385,176
Other assets:							
Deferred charges	1,018,000	1,119,854	220,028	144,588	-	2,502,470	-
Conservation loans receivable	175,000	-	-	-	-	175,000	-
TVA discounted energy units	3,375,000	-	-	-	-	3,375,000	-
Total other assets	4,568,000	1,119,854	220,028	144,588	-	6,052,470	-
Total noncurrent assets	305,368,000	317,335,925	15,203,961	38,814,671	7,421,010	684,143,567	385,176
Total assets	\$ 398,798,000	\$ 353,702,452	\$ 19,878,609	\$ 45,406,196	\$ 7,711,298	\$ 825,496,555	\$ 6,349,146

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

	Business-type Activities - Enterprise Funds						Governmental Activities - Internal Service Fund
	Major Funds				Other Fund		
	EPB	Interceptor Sewer System	Solid Waste/ Sanitation	Storm Water	Housing Management	Total	
LIABILITIES							
CURRENT LIABILITIES							
Current maturities of long-term liabilities	\$ 2,245,000	\$ 10,816,712	\$ 2,022,874	\$ 1,520,794	\$ -	\$ 16,605,380	\$ 28,681
Accounts payable and accrued liabilities	83,154,000	2,038,152	481,291	520,016	3,627,708	89,821,167	285,154
Accrued claims	-	-	-	-	-	-	3,590,000
Customer deposits	2,267,000	-	-	-	-	2,267,000	-
Contracts payable	-	360,216	-	-	-	360,216	-
Conservation advances	277,000	-	-	-	-	277,000	-
Due to other governments	-	-	21,477	-	-	21,477	-
Other current liabilities	5,425,000	-	-	-	-	5,425,000	-
Total current liabilities	93,368,000	13,215,080	2,525,642	2,040,810	3,627,708	114,777,240	3,903,835
LONG-TERM LIABILITIES							
Notes and capital leases payable	1,971,000	40,598,461	-	996,464	-	43,565,925	-
Compensated absences	864,000	825,992	72,330	170,686	-	1,933,008	467,906
Customer Deposits	12,267,000	-	-	-	-	12,267,000	-
Accrued closure and post closure care	-	-	10,013,509	-	-	10,013,509	-
Revenue bonds payable	30,400,000	-	-	-	-	30,400,000	-
Original issue discount	(55,000)	-	-	-	-	(55,000)	-
General obligation bonds payable	-	65,515,698	22,034,407	13,642,775	-	101,192,880	-
Deferred refunding	-	(3,305,321)	(812,132)	(518,867)	-	(4,636,320)	-
Original issue premium	-	2,757,553	1,109,671	751,052	-	4,618,276	-
Other noncurrent liabilities	4,506,000	-	-	-	50,089	4,556,089	-
Accrued postretirement benefits	9,709,000	-	-	-	-	9,709,000	-
Total long-term liabilities	59,662,000	106,392,383	32,417,785	15,042,110	50,089	213,564,367	467,906
Total liabilities	153,030,000	119,607,463	34,943,427	17,082,920	3,677,797	328,341,607	4,371,741
NET ASSETS (DEFICIT)							
Invested in capital assets, net of related debt	266,574,000	197,349,122	946,299	22,147,272	4,335,272	491,351,965	385,176
Restricted for renewal and replacement	3,747,000	4,562,505	9,120,806	514,524	-	17,944,835	-
Unrestricted	(24,553,000)	32,183,362	(25,131,923)	5,661,480	(301,771)	(12,141,852)	1,592,229
Total net assets (deficit)	\$ 245,768,000	\$ 234,094,989	\$ (15,064,818)	\$ 28,323,276	\$ 4,033,501	\$ 497,154,948	\$ 1,977,405

CITY OF CHATTANOOGA, TENNESSEE

PROPRIETARY FUNDS

STATEMENT OF REVENUES, EXPENSES, AND CHANGES
IN NET ASSETS
Year Ended June 30, 2006

	Business-type Activities - Enterprise Funds						Governmental Activities - Internal Service Fund
	Major Funds				Other Fund	Total	
	EPB	Interceptor Sewer System	Solid Waste/ Sanitation	Storm Water	Housing Management		
OPERATING REVENUES							
Charges for sales and services:							
Electric sales	\$ 402,312,000	\$ -	\$ -	\$ -	\$ -	\$ 402,312,000	\$ -
Sewer charges	-	36,509,866	-	-	-	36,509,866	-
Waste charges	-	-	5,475,554	-	-	5,475,554	-
Stormwater fees	-	-	-	5,616,353	-	5,616,353	-
Rent	-	-	-	-	1,182,305	1,182,305	-
Other services	19,831,000	-	-	114,105	21,815	19,966,920	11,516,828
Other	-	-	76,532	-	-	76,532	-
Total operating revenues	<u>422,143,000</u>	<u>36,509,866</u>	<u>5,552,086</u>	<u>5,730,458</u>	<u>1,204,120</u>	<u>471,139,530</u>	<u>11,516,828</u>
OPERATING EXPENSES							
Power purchases	334,867,000	-	-	-	-	334,867,000	-
Sewer plant operations	-	19,044,514	-	-	-	19,044,514	-
Solid waste operations	-	-	2,352,548	-	-	2,352,548	-
Storm water operations	-	-	-	2,764,346	-	2,764,346	-
Pump station operations	-	1,437,279	-	-	-	1,437,279	-
Housing management operations	-	-	-	-	918,286	918,286	-
Municipal garage operations	-	-	-	-	-	-	3,080,463
Maintenance and repairs	13,457,000	-	-	-	-	13,457,000	6,362,103
Depreciation and amortization	16,835,000	9,904,556	581,535	947,875	301,979	28,570,945	71,002
Closure/postclosure costs	-	-	563,734	-	-	563,734	-
Liability insurance	-	-	-	-	-	-	60,931
Other	48,582,000	-	-	-	-	48,582,000	-
Total operating expenses	<u>413,741,000</u>	<u>30,386,349</u>	<u>3,497,817</u>	<u>3,712,221</u>	<u>1,220,265</u>	<u>452,557,652</u>	<u>9,574,499</u>
OPERATING INCOME (LOSS)	<u>8,402,000</u>	<u>6,123,517</u>	<u>2,054,269</u>	<u>2,018,237</u>	<u>(16,145)</u>	<u>18,581,878</u>	<u>1,942,329</u>
NONOPERATING REVENUES (EXPENSES)							
Investment income	1,473,000	1,117,703	405,071	18,386	1,546	3,015,706	-
Interest expense	(491,000)	(5,008,865)	(1,180,453)	(763,485)	(331,854)	(7,775,657)	-
Other income (expense)	(3,560,000)	687,614	70,548	-	59,253	(2,742,585)	-
Total nonoperating revenues (expenses)	<u>(2,578,000)</u>	<u>(3,203,548)</u>	<u>(704,834)</u>	<u>(745,099)</u>	<u>(271,055)</u>	<u>(7,502,536)</u>	<u>-</u>
INCOME (LOSS) BEFORE CONTRIBUTIONS AND TRANSFERS	<u>5,824,000</u>	<u>2,919,969</u>	<u>1,349,435</u>	<u>1,273,138</u>	<u>(287,200)</u>	<u>11,079,342</u>	<u>1,942,329</u>
Capital contributions	3,377,000	2,000	-	-	-	3,379,000	-
Transfers in	-	-	-	683,952	-	683,952	-
Transfers out	(3,142,000)	-	-	-	-	(3,142,000)	-
CHANGE IN NET ASSETS	<u>6,059,000</u>	<u>2,921,969</u>	<u>1,349,435</u>	<u>1,957,090</u>	<u>(287,200)</u>	<u>12,000,294</u>	<u>1,942,329</u>
NET ASSETS (DEFICIT), beginning	<u>239,709,000</u>	<u>231,173,020</u>	<u>(16,414,253)</u>	<u>26,366,186</u>	<u>4,320,701</u>	<u>485,154,654</u>	<u>35,076</u>
NET ASSETS (DEFICIT), ending	<u>\$ 245,768,000</u>	<u>\$ 234,094,989</u>	<u>\$ (15,064,818)</u>	<u>\$ 28,323,276</u>	<u>\$ 4,033,501</u>	<u>\$ 497,154,948</u>	<u>\$ 1,977,405</u>

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

CITY OF CHATTANOOGA, TENNESSEE

PROPRIETARY FUNDS

STATEMENT OF CASH FLOWS
Year Ended June 30, 2006

	Business-type Activities - Enterprise Funds						Governmental Activities - Internal Service Fund
	Major Funds				Other Fund	Total	
	EPB	Interceptor Sewer System	Solid Waste/ Sanitation	Storm Water	Housing Management		
CASH FLOWS FROM OPERATING ACTIVITIES							
Receipts from customers and users	\$ 413,455,000	\$ 35,999,716	\$ 5,463,401	\$ 5,737,137	\$ 1,204,118	\$ 461,859,372	\$ 647,791
Receipts from interfund services provided	-	-	-	-	-	-	13,665,118
Receipts from operating grants	-	-	32,603	-	-	32,603	-
Payments to suppliers	(353,005,000)	(15,531,165)	(2,010,214)	(1,295,646)	(857,374)	(372,699,399)	(7,919,484)
Payments to employees	(24,019,000)	(5,658,734)	(544,804)	(1,705,690)	-	(31,928,228)	(2,543,486)
Payments in lieu of taxes	(5,731,000)	-	-	-	-	(5,731,000)	-
Net cash provided by operating activities	<u>30,700,000</u>	<u>14,809,817</u>	<u>2,940,986</u>	<u>2,735,801</u>	<u>346,744</u>	<u>51,533,348</u>	<u>3,849,939</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES							
Transfers in	-	-	-	683,952	-	683,952	-
Transfers out	(3,142,000)	-	-	-	-	(3,142,000)	-
Net cash provided by (used in) noncapital financing activities	<u>(3,142,000)</u>	<u>-</u>	<u>-</u>	<u>683,952</u>	<u>-</u>	<u>(2,458,048)</u>	<u>-</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES							
Proceeds from capital debt	539,000	-	-	-	-	539,000	-
Principal paid on capital debt	(1,600,000)	(10,518,484)	(1,988,455)	(1,476,301)	(79,183)	(15,662,423)	-
Interest paid on capital debt	(1,939,000)	(4,789,179)	(1,169,629)	(784,586)	(331,854)	(9,014,248)	-
Refunds of capital expenditures	-	539,864	-	-	-	539,864	-
Insurance settlements	-	-	-	-	59,253	59,253	-
Capital grants and contributions	3,377,000	2,000	-	-	-	3,379,000	-
Additions to capital assets	(43,216,000)	(3,978,817)	-	-	-	(47,194,817)	(58,193)
Proceeds from the sale of capital assets	323,000	330,601	-	(1,331,219)	-	(677,618)	-
Net cash flows used in capital and related financing activities	<u>(42,516,000)</u>	<u>(18,414,015)</u>	<u>(3,158,084)</u>	<u>(3,592,106)</u>	<u>(351,784)</u>	<u>(68,031,989)</u>	<u>(58,193)</u>
CASH FLOWS FROM INVESTING ACTIVITIES							
Purchases of investments	(1,100,000)	(214,223,201)	(29,588,838)	(1,036,116)	-	(245,948,155)	-
Proceeds from sales and maturities of investments	13,128,000	209,524,501	29,361,420	1,016,432	-	253,030,353	-
Interest	1,242,000	1,082,791	339,533	19,684	1,547	2,685,555	-
Net cash flows provided by (used in) investing activities	<u>13,270,000</u>	<u>(3,615,909)</u>	<u>112,115</u>	<u>-</u>	<u>1,547</u>	<u>9,767,753</u>	<u>-</u>
Net increase (decrease) in cash and cash equivalents	(1,688,000)	(7,220,107)	(104,983)	(172,353)	(3,493)	(9,188,936)	3,791,746
Cash and cash equivalents, beginning of year	39,926,000	9,026,216	4,643,975	5,920,432	234,049	59,750,672	967,642
Cash and cash equivalents, end of year	<u>\$ 38,238,000</u>	<u>\$ 1,806,109</u>	<u>\$ 4,538,992</u>	<u>\$ 5,748,079</u>	<u>\$ 230,556</u>	<u>\$ 50,561,736</u>	<u>\$ 4,759,388</u>

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

(continued on next page)

(continued from previous page)

	Business-type Activities - Enterprise Funds						Governmental Activities - Internal Service Fund
	Major Funds				Other Fund	Total	
	EPB	Interceptor Sewer System	Solid Waste/ Sanitation	Storm Water	Housing Management		
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES							
OPERATING INCOME (LOSS)	\$ 8,402,000	\$ 6,123,517	\$ 2,054,269	\$ 2,018,237	\$ (16,145)	\$ 18,581,878	\$ 1,942,329
ADJUSTMENTS NOT AFFECTING CASH							
Depreciation and amortization	17,554,000	9,904,556	581,535	947,875	301,979	29,289,945	71,002
Provision for uncollectible accounts	-	319,226	-	-	-	319,226	-
Provision for obsolete inventory	-	-	-	-	-	-	20,723
Changes in assets and liabilities:							
(Increase) decrease in accounts receivable	(8,560,000)	(917,021)	(77,691)	3,281	-	(9,551,431)	(87,156)
(Increase) decrease in due from other funds	-	(13,330)	(338)	(1,684)	-	(15,352)	2,946,741
(Increase) decrease in due from other governments	-	-	39,977	-	-	39,977	(62,473)
(Increase) decrease in inventory	(642,000)	18,361	-	-	-	(623,639)	59,165
(Increase) decrease in prepaid items	(1,577,000)	30,398	2,089	8,597	(4,864)	(1,540,780)	-
(Increase) decrease in deferred charges	(115,000)	132,682	25,297	17,332	-	60,311	-
Increase (decrease) in accounts payable	13,871,000	(801,109)	(145,578)	1,767	-	12,926,080	72,357
Increase (decrease) in accrued liabilities	-	2,349	459,306	(174,188)	-	287,467	(1,198,048)
Increase (decrease) in other assets/liabilities	1,804,000	65,447	93,922	(25,935)	65,774	2,003,208	-
Increase (decrease) in compensated absences	(37,000)	32,611	(47,359)	(19,116)	-	(70,864)	86,330
Decrease in due to other funds	-	(87,870)	(65,920)	(40,365)	-	(194,155)	(1,031)
Increase in due to other governments	-	-	21,477	-	-	21,477	-
TOTAL ADJUSTMENTS	22,298,000	8,686,300	886,717	717,564	362,889	32,951,470	1,907,610
Net cash provided by operating activities	\$ 30,700,000	\$ 14,809,817	\$ 2,940,986	\$ 2,735,801	\$ 346,744	\$ 51,533,348	\$ 3,849,939

CITY OF CHATTANOOGA, TENNESSEE

FIDUCIARY FUNDS

STATEMENT OF FIDUCIARY NET ASSETS

June 30, 2006

	<u>Pension Trust Funds</u>
ASSETS	
Investments:	
U.S. Government securities	\$ 18,975,661
Municipal bonds	67,214
Corporate bonds	27,865,995
Foreign bonds	1,361,700
Corporate stocks	204,829,069
Mutual funds - equity	116,168,527
Mutual funds - fixed income	44,288,587
Temporary investments	11,999,405
Limited partnerships	26,156,992
Other investments	875,000
Receivables:	
Accrued income	922,477
Contributions	370,768
Due from plan custodian	962,709
	<u>454,844,104</u>
LIABILITIES	
Due to plan custodian	203,223
Accounts payable and accrued expenses	635,879
	<u>839,102</u>
NET ASSETS	
Held in trust for pension benefits	<u>\$ 454,005,002</u>

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

CITY OF CHATTANOOGA, TENNESSEE
 FIDUCIARY FUNDS
 STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
 Year Ended June 30, 2006

	Pension Trust Funds
ADDITIONS	
Contributions:	
Employer	\$ 9,844,924
Employee	<u>3,852,736</u>
Total contributions	<u>13,697,660</u>
Investment income:	
Net appreciation in fair market value of investments	39,718,222
Litigation settlement	4,203,305
Interest	3,558,900
Dividends	<u>6,676,310</u>
	54,156,737
Less investment expense	<u>(1,774,791)</u>
Net investment income	<u>52,381,946</u>
Total additions	<u>66,079,606</u>
DEDUCTIONS	
Benefits paid to participants	26,975,208
Administrative expenses	<u>720,877</u>
Total deductions	<u>27,696,085</u>
CHANGE IN NET ASSETS	38,383,521
Net assets, beginning	<u>415,621,481</u>
Net assets, ending	<u><u>\$ 454,005,002</u></u>

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

CITY OF CHATTANOOGA, TENNESSEE
 COMPONENT UNITS
 STATEMENT OF NET ASSETS
 June 30, 2006

	Chattanooga Metropolitan Airport Authority	CARTA	Chattanooga Downtown Redevelopment Corporation	Total
ASSETS				
Cash and cash equivalents	\$ 1,842,842	\$ 832,128	\$ 2,546,333	\$ 5,221,303
Investments	24,535	-	655,128	679,663
Accounts receivable	2,662,500	816,717	367,833	3,847,050
Net investment in capital lease	-	-	115,925,472	115,925,472
Due from primary government	-	-	329,749	329,749
Deferred charges	186,450	-	1,793,776	1,980,226
Inventories	-	162,588	169,458	332,046
Prepaid items	268,805	241,682	152,210	662,697
Net pension asset	-	46,540	-	46,540
Restricted assets:				
Cash and cash equivalents	840,570	1,445,000	-	2,285,570
Investments	3,929,413	-	9,934,204	13,863,617
Receivables	94,446	-	-	94,446
Land and other nondepreciable assets	17,401,599	3,097,296	-	20,498,895
Other capital assets, net of accumulated depreciation	<u>36,951,348</u>	<u>25,235,979</u>	<u>751,239</u>	<u>62,938,566</u>
Total assets	<u>64,202,508</u>	<u>31,877,930</u>	<u>132,625,402</u>	<u>228,705,840</u>
LIABILITIES				
Accounts payable and accrued liabilities	569,177	1,223,775	2,907,023	4,699,975
Contracts payable	1,141,899	-	-	1,141,899
Due to primary government	-	375,000	-	375,000
Revenue bonds payable	13,935,000	-	129,200,000	143,135,000
Original issue premium (discount)	(84,663)	-	88,583	3,920
Deferred revenue	<u>8,090</u>	<u>400,000</u>	<u>-</u>	<u>408,090</u>
Total liabilities	<u>15,569,503</u>	<u>1,998,775</u>	<u>132,195,606</u>	<u>149,763,884</u>
NET ASSETS				
Invested in capital assets (net of related debt)	40,502,610	28,333,275	751,239	69,587,124
Restricted for:				
Debt service	4,864,429	-	9,783,100	14,647,529
Renewal and replacement	-	-	1,105,521	1,105,521
Unrestricted	<u>3,265,966</u>	<u>1,545,880</u>	<u>(11,210,064)</u>	<u>(6,398,218)</u>
Total net assets	<u>\$ 48,633,005</u>	<u>\$ 29,879,155</u>	<u>\$ 429,796</u>	<u>\$ 78,941,956</u>

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

CITY OF CHATTANOOGA, TENNESSEE

COMPONENT UNITS

STATEMENT OF ACTIVITIES

Year Ended June 30, 2006

	Program Revenues				Net Revenue (Expense) and Changes in Net Assets			Total
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Chattanooga Metropolitan Airport Authority	CARTA	Chattanooga Downtown Redevelopment Corporation	
CHATTANOOGA METROPOLITAN AIRPORT AUTHORITY								
Airport operations	\$ 8,973,892	\$ 5,779,745	\$ 846,920	\$ 7,915,490	\$ 5,568,263	\$ -	\$ -	\$ 5,568,263
CARTA								
CARTA operations	16,817,049	4,347,431	6,084,288	6,191,217	-	(194,113)	-	(194,113)
CHATTANOOGA DOWNTOWN REDEVELOPMENT CORPORATION								
CDRC operations	17,878,134	17,856,241	-	-	-	-	(21,893)	(21,893)
Total component units	<u>\$ 43,669,075</u>	<u>\$ 27,983,417</u>	<u>\$ 6,931,208</u>	<u>\$ 14,106,707</u>	<u>5,568,263</u>	<u>(194,113)</u>	<u>(21,893)</u>	<u>5,352,257</u>
General revenues:								
Investment income					142,059	8,838	542,093	692,990
Miscellaneous					984,868	77,571	-	1,062,439
Total general revenues					<u>1,126,927</u>	<u>86,409</u>	<u>542,093</u>	<u>1,755,429</u>
CHANGE IN NET ASSETS					6,695,190	(107,704)	520,200	7,107,686
Net assets (deficit), beginning					41,937,815	29,986,859	(90,404)	71,834,270
Net assets, ending					<u>\$ 48,633,005</u>	<u>\$ 29,879,155</u>	<u>\$ 429,796</u>	<u>\$ 78,941,956</u>

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

CITY OF CHATTANOOGA, TENNESSEE
NOTES TO BASIC FINANCIAL STATEMENTS
June 30, 2006

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CITY OF CHATTANOOGA, TENNESSEE

NOTES TO BASIC FINANCIAL STATEMENTS

June 30, 2006

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The City of Chattanooga, Tennessee (the City) was incorporated under the Private Acts of 1869. Through June 11, 1990, the City operated under the Commission form of government, consisting of an elected Mayor and four elected Commissioners, each of whom served as the head of a city department. Pursuant to an Agreed Order dated January 18, 1990, issued by the United States District Court for the Eastern District of Tennessee, Southern Division, the Board of Commissioners of the City and the offices of Mayor and Commissioner were abolished as of June 11, 1990.

The Agreed Order provided that the City Charter be amended to create the office of Mayor, with all executive and administrative authority formerly vested in the Board of Commissioners. Further, the City Council was created with all legislative and quasi-judicial authority formerly vested in the Board of Commissioners. Under the provisions of the Agreed Order, the Mayor is elected at-large and is not a member of the City Council, while the City Council is composed of nine members, with each member elected from one of nine districts within the geographic boundaries of the City.

The financial statements of the City have been prepared in accordance with generally accepted accounting principles in the United States of America ("GAAP") as applied to governmental units. The Governmental Accounting Standards Board ("GASB") is the standard-setting body for governmental accounting and financial reporting. Pronouncements of the Financial Accounting Standards Board ("FASB") issued after November 30, 1989, are not applied in the preparation of the financial statements of enterprise funds in accordance with an election made by the City under GASB Statement No. 20. The GASB periodically updates its codification of the existing Governmental Accounting and Financial Reporting Standards, which, along with subsequent GASB pronouncements (Statements and Interpretations), constitutes GAAP for governmental units. The more significant of these accounting policies are described below.

(A) Reporting Entity

In evaluating the City as a reporting entity, management has addressed all potential component units (traditionally separate reporting entities) for which the City may be financially accountable and, as such, should be included within the City's financial statements. The City (the primary government) is financially accountable if it appoints a voting majority of the organization's governing board and (1) it is able to impose its will on the organization or (2) there is a potential for the organization to provide specific financial benefit or to impose specific financial burden on the City. Additionally, the primary government is required to consider other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete.

The financial statements are formatted to allow the user to clearly distinguish between the primary government and its component units. The primary government includes separately administered organizations that are not legally separate from the City, as discussed below. Blended component units, although legally separate entities, are in substance part of the government's operations and data from these units are combined with data of the primary government. The City has no blended component units at June 30, 2006. Discretely presented component units are reported in a separate column in the basic financial statements to emphasize that they are legally separate from the City. Each discretely presented component unit has a June 30 year-end.

The financial statements of EPB (the Electric Power Board) are included in the accompanying financial statements as part of the primary government because it is not legally separate from the City. The City affirms all board member appointments and approves all disbursements of EPB funds. EPB's operations are reported as an enterprise fund.

Discretely Presented Component Units

Chattanooga Metropolitan Airport Authority - The City appoints all board members and is secondarily responsible for retirement of the revenue bonds recorded as a liability of the Airport Authority. The Airport Authority is presented as a proprietary fund type.

Chattanooga Area Regional Transit Authority (CARTA) - The City appoints ten members of the twelve-member board. Although CARTA has the authority to issue its own debt, the board members serve at the City's discretion and the City finances the majority of CARTA's operating deficits. CARTA is presented as a proprietary fund type.

Chattanooga Downtown Redevelopment Corporation - The City's Mayor, City Council Chairperson, and Chief Finance Officer are permanent members of the Board, and the City appoints the remaining board members. The Corporation has the authority to issue its own debt, but the City has agreed to finance any operating deficits of the Corporation. The Corporation is presented as a proprietary fund type.

Complete financial statements of the component units can be obtained from:

Chattanooga Metropolitan
Airport Authority
P.O. Box 22444
Chattanooga, TN 37422

CARTA
1617 Wilcox Boulevard
Chattanooga, TN 37406

Chattanooga Downtown Redevelopment Corporation
427 City Hall Annex
Chattanooga, TN 37402

(B) Joint Ventures and Related Organizations

A joint venture is a legal entity or other organization that results from a contractual agreement and that is owned, operated or governed by two or more participants as a separate and specific activity subject to joint control in which the participants retain (a) an ongoing financial interest or (b) an on-going financial responsibility. The City participates in the following joint venture:

Carter Street Corporation – The Carter Street Corporation, a nonprofit organization, owns a trade center and parking garage that were financed by bonds issued by the Industrial Development Board of Chattanooga. The Carter Street Corporation is managing the trade center and parking garage under a management agreement. Additional information regarding the City's participation in this joint venture is disclosed in Note 12.

Related Organizations – City officials are also responsible for appointing the members of the boards of other related organizations, but the City's accountability for these organizations does not extend beyond making the appointments. The Mayor or the City Council appoints the Board members of the Chattanooga Housing Authority, The Industrial Development Board of the City of Chattanooga, and The Health, Educational, and Housing Facility Board of the City of Chattanooga. During 2006 the City appropriated no funds to these organizations.

(C) Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all of the nonfiduciary activities of the primary government and its component units. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Interfund services provided and used are not eliminated in the government-wide statement of activities. In addition, the primary government is reported separately from certain legally separate component units for which the primary government is financially accountable.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

(D) Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund and fiduciary fund financial statements. Revenues are recognized when earned and expenses are recorded when a liability is incurred, regardless of the timing of the related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the City considers revenues to be available if they are collected within thirty days of the end of the fiscal period, except for property taxes, for which the time period is sixty days. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes, sales taxes, franchise taxes, licenses, and interest associated with the current fiscal period are all considered to be susceptible to accrual and have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the government.

The City reports the following major governmental funds:

General Fund – The General Fund accounts for all financial resources applicable to the general operations of City government that are not properly accounted for in another fund. Revenues are derived primarily from taxes and intergovernmental revenues.

Capital Projects Fund – The Capital Projects Fund accounts for the acquisition or construction of capital projects, other than those financed by Enterprise Funds, the Internal Service Fund, or Trust Funds. Revenues are derived primarily from the sale of general obligation bonds and notes, loans, intergovernmental revenues, and earnings on investments.

The City reports the following major enterprise funds:

EPB Fund – The EPB Fund accounts for the cost of providing electric utility and telecommunication service for the residential and commercial concerns of Chattanooga and Hamilton County, Tennessee. The EPB is a separately administered organization whose Board of Trustees is affirmed by the City. All disbursements of the EPB funds are approved by the City.

Interceptor Sewer System Fund – The Interceptor Sewer System Fund accounts for sanitary sewer services provided to the residents of the City. The fund's revenues are derived primarily from user fees and investment earnings.

Solid Waste/Sanitation Fund – The Solid Waste/Sanitation Fund accounts for the costs associated with the disposal of solid waste and recyclable materials.

Storm Water Fund – The Storm Water Fund accounts for costs associated with the City’s storm water management program as mandated by the Environmental Protection Agency and the State of Tennessee.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues include charges for services. Operating expenses include costs of services as well as materials, contracts, personnel and depreciation on capital assets. All revenues and expenses not meeting these definitions are reported as nonoperating revenues and expenses.

Additionally, the City reports the following fund types:

Special Revenue Funds - Special Revenue Funds are used to account for the proceeds of specific revenue sources (other than major capital projects) requiring separate accounting because of legal or regulatory provisions or administrative action.

Debt Service Fund – The Debt Service Fund is used to account for the accumulation of resources for the payment of interest, principal, and related costs of long-term liabilities of the governmental activities.

Permanent Funds – Permanent funds are used to report resources that are legally restricted to the extent that only earnings, not principal, may be used for purposes that support the government’s programs.

Internal Service Fund - The Internal Service Fund is used to account for fleet services and risk management activities provided to other departments or agencies of the City, or to other governmental units, on a cost-reimbursement basis. The costs associated with providing these goods or services are usually recovered from those governmental units that receive benefits.

Pension Trust Funds - The Pension Trust Funds account for resources held in trust for defined benefit pension plans to provide disability and retirement benefits for City employees/retirees. These funds are accounted for in the same manner as business enterprises providing similar services.

Amounts reported as program revenues include 1) charges to customers or applicants for goods, services, or privileges provided, and 2) operating grants and contributions, and 3) capital grants and contributions. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes.

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

(E) Budget Policy and Budgetary Data

The City follows these procedures in establishing the budgetary data reflected in the financial statements:

The City Finance Officer annually obtains information from all officers, departments, boards, commissions, and other agencies of City Government for which appropriations are made and/or revenues are collected and compiles the annual operating budget for the ensuing fiscal year beginning July 1. The compiled information, including various expenditure options and the means of financing them, is submitted to the Mayor.

During May and June, the City Council hears budget requests from agencies and departments at its regularly scheduled meetings. In addition, advertised public hearings are held to allow taxpayers' comments prior to final passage.

Prior to July, the City adopts an interim budget appropriating funds for the usual and ordinary expenses of the City Government in an amount not to exceed one-twelfth of the preceding year's operating budget for each month that the interim budget is in effect. Subsequently, the budget is legally enacted through passage of an ordinance with an operative date of July 1.

Formal budgets are adopted for the General Fund, Special Revenue Funds, and the Debt Service Fund. These formal budgets are adopted on a departmental basis and the line item estimates are from the appropriations ledger and not from a formal budget ordinance. The legal level of budgetary control is the fund level. Transfers of appropriations between funds require the approval of the City Council. The City Finance Officer may make interdepartmental and intradepartmental transfers within the General Fund.

Major capital facilities and improvements, which are accounted for by the City within the Capital Projects Fund, are subject to budgetary control on a project basis. Appropriations for a specific project do not lapse until completion of the project. Because of the project nature of these funds, budgetary comparison statements on an annual basis do not provide meaningful information and, accordingly, are not presented in the accompanying financial statements.

The budgets are prepared on a basis consistent with generally accepted accounting principles except that encumbrances are treated as budget expenditures in the year of the commitment to purchase. Budgetary comparisons presented in the report are on this budgetary basis. All unencumbered and unexpended appropriations lapse at the end of the fiscal year.

Encumbrance accounting, under which purchase orders, contracts, and other commitments for the expenditure of funds are recorded in order to reserve that portion of the applicable appropriation, is utilized for budgetary accounting controls in the governmental funds. Open encumbrances are reported as reservations of fund balances because the commitments will be honored in subsequent years. Encumbrances do not constitute expenditures or liabilities.

Expenditures may not legally exceed appropriations at or above the fund level. All budgeted amounts shown in the financial statements and the accompanying supplementary information reflect the original budget and the amended budget (which may have been adjusted for legally authorized revisions to the annual budgets during the year). During the year ended June 30, 2006, no supplemental appropriations were necessary.

(F) Assets, Liabilities and Fund Equity

1) Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks, interest-bearing deposits at various financial institutions, and short-term investments with an original maturity of three months or less.

2) Investments

Investments are stated at fair value, except for interest-earning investment contracts that have a remaining maturity of one year or less at the time of purchase. Any change in the value of investments recorded at fair value is included in investment income. Fair value is based on quoted market prices.

3) Inventories and Prepaid Items

Inventories, principally materials, supplies, and replacement parts, are valued at cost in Governmental Funds and at the lower of cost or market in Proprietary Funds, with cost determined using the first-in, first-out (FIFO) method. The costs are recorded as expenditures at the time individual inventory items are consumed (consumption method).

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items.

4) Restricted Assets

Proceeds of bonds, as well as resources set aside for their repayment, are classified as restricted assets on the statement of net assets because their use is limited by applicable bond covenants. Also, amounts due from other governments may be included as restricted assets because their use is limited by grant agreements.

5) Capital Assets

Capital assets (including infrastructure) are recorded at historical cost or at estimated historical cost if actual historical cost is not available. Contributed capital assets are recorded at their estimated fair market value on the date contributed. Capital assets include public domain infrastructure assets consisting of roads, bridges, streets and sidewalks, sewers, lighting systems, and drainage systems. The City defines capital assets as assets with an initial, individual cost of more than \$5,000 (\$25,000 for infrastructure) and an estimated useful life of three years or greater.

Additions, improvements and other capital outlays that significantly extend the useful life of an asset are capitalized. Other costs incurred for repairs and maintenance are expensed as incurred. Land and certain land improvements are inexhaustible capital assets, and are not depreciated. Depreciation on depreciable capital assets is calculated on the straight-line basis over the following estimated useful lives:

	<u>Useful Life</u>
Buildings	5 – 30 years
Vehicles and machinery	5 – 25 years
Improvements other than buildings	15 years
Sewer system	50 years
Storm water system	50 years
Telecommunications	5 – 40 years
Public domain infrastructure	10 – 50 years

Interest is capitalized on assets acquired with tax-exempt debt. The amount of interest capitalized is the net interest expense incurred (interest expense less interest income) from the date of the borrowing until completion of the project.

5) Bond Discounts and Issuance Costs

In the governmental funds, bond discounts and issuance costs are treated as period costs in the year of issue.

In proprietary funds, bond discounts and issuance costs are deferred and amortized over the term of the bonds using the effective interest method. Bond discounts are presented as a reduction of the face amount of bonds payable whereas issuance costs are recorded as deferred charges.

At the government-wide level any bond discounts and issuance costs in the governmental funds are adjusted and reported in the same manner as in proprietary funds.

6) Deferred Gain/Loss from Advance Refunding of Debt

In the proprietary funds (and for governmental activities in the government-wide financial statements) the difference between the new debt and the net carrying value of the old debt on refunded debt transactions is deferred. The deferred gain/loss is amortized using the effective interest method over the life of the new debt. The deferred gain/loss is offset against the new liability.

7) Fund Balance

Governmental funds report reservations of fund balance in the fund financial statements for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent management plans that are subject to change.

(G) Revenues, Expenditures and Expenses

Substantially all governmental fund revenues are accrued. Expenditures are recognized when the related fund liability is incurred, except for the following instances permitted by generally accepted accounting principles:

- General obligation long-term debt principal and interest are reported only when due.

- Inventory costs are reported in the period when inventory items are consumed, rather than in the period purchased.

1) Property Taxes

Property taxes are levied by the City annually based upon assessed valuations established by the Hamilton County Assessor of Property. The various types of property are assessed at a percentage of market value as follows:

Farm and residential real property	25%
Commercial and industrial property:	
Real	40%
Personal	30%
Public utilities real and personal property	55%

The property tax levy is without legal limit. The rate, as permitted by Tennessee State Law and City Charter, is set annually by the City Council and collected by the City Treasurer. Property taxes are secured by a statutory lien effective as of the original levy date of January 1. Taxes are due October 1 and become delinquent March 1. Property taxes levied for 2005 are recorded as receivables, net of estimated uncollectible amounts.

The receivables collected during the current fiscal year and those collected by the City Treasurer related to tax levies for 2005, are recorded as revenue in accordance with the principles established by the Governmental Accounting Standards Board. The net receivables estimated to be collectible subsequent to August 29, are recorded as deferred revenues at June 30, 2006.

2) Grant Revenue

The City, a recipient of grant revenues, recognizes revenues (net of estimated uncollectible amounts, if any), when all applicable eligibility requirements, including time requirements, are met. Resources transmitted to the City before the eligibility requirements are met are reported as deferred revenues.

Some grants and contributions consist of capital assets or resources that are restricted for capital purposes—to purchase, construct, or renovate capital assets associated with a specific program. These are reported separately from grants and contributions that may be used either for operating expenses or for capital expenditures of the program at the discretion of the City.

3) Investment Income

Investment income from pooled cash and investments is allocated monthly based on the percentage of a fund's average daily equity in pooled cash and investments to the total average daily-pooled equity in pooled cash and investments.

4) Compensated Absences

City employees accrue personal leave, or compensated absences, by prescribed formula based on length of service. The City limits personal leave to one hundred fifty (150) days for employees hired on or before March 27, 1990, and one hundred (100) days for employees hired thereafter. The liability for compensated absences attributable to the City's governmental funds is recorded in the government-wide financial statements. The non-current portion of the liability for employees of governmental funds is a reconciling item between the fund and government-wide financial statements. Compensated absences related to business-type activities are charged to expense with a corresponding liability established in the government-wide financial statements as well as the applicable business-type funds.

5) Interfund Transactions

During the course of normal operations, the City has numerous transactions between funds to provide services, construct assets and service debt. These transactions are generally reflected as transfers except for transactions reimbursing a fund for expenditures made by it for the benefit of another fund. Such transactions are recorded as expenditures in the disbursing fund and as a reduction of expenditures in the receiving fund. Transactions that would be treated as revenues or expenditures if the involved organizations were external to the City are treated as revenues in the receiving fund and expenditures in the disbursing fund. Transfers within governmental activities and within business-type activities are eliminated upon consolidation.

Amounts owed to one fund or component unit by another are reported as due to/due from other funds or component units. The interfund balances resulted from the time lag between the dates that (1) interfund goods and services are provided or reimbursable expenditures occur, (2) transactions are recorded in the accounting system, and (3) payments between funds are made. Amounts reported in the fund financial statements as due to/due from other funds are subject to elimination upon consolidation. Any residual balances outstanding between the governmental activities and the business-type activities are reported in the government-wide financial statements as "internal balances."

6) Payments Between the City and Component Units

Resource flows (except those that affect the statement of net assets/balance sheet only, such as loans and repayments) between a primary government and its discretely presented component units are reported as external transactions—that is, as revenues and expenses. Payments to component units consist of operating subsidy payments by the City to CARTA. The City also makes lease payments to Chattanooga Downtown Redevelopment Corporation.

7) Indirect Costs

Certain indirect costs have been included as part of the program expenses reported for the various functional activities.

8) Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(H) Net Assets

The government-wide and business-type fund financial statements utilize a net asset presentation. Net assets are categorized as invested in capital assets (net of related debt), restricted and unrestricted.

Invested in Capital Assets (net of related debt)—is intended to reflect the portion of net assets which are associated with non-liquid capital assets less outstanding capital asset related debt.

Restricted Net Assets—represent net assets that have third party (statutory, bond covenant or granting agency) limitations on their use. The City's policy is generally to use restricted net assets first, as appropriate opportunities arise.

Unrestricted Net Assets—represent unrestricted net assets. While management may have categorized and segmented portions for various purposes, the City has the unrestricted authority to alter these managerial decisions.

NOTE 2. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Compliance with Finance Related Legal and Contractual Provisions

The City incurred no material violations of finance related legal and contractual provisions.

Excess of Expenditures Over Appropriations in Individual Funds

For the year ended June 30, 2006, the City had no material excess of expenditures over appropriations in individual funds.

Net Assets/Fund Balance Deficit

The Solid Waste/Sanitation Fund has a deficit in net assets of \$15,064,818 at June 30, 2006. This deficit resulted from the recognition of cumulative landfill closure and postclosure care costs from prior years. These costs may be covered by charges to future landfill users, taxpayers, or both. The deficit decreased by \$1,349,435 from the prior fiscal year.

NOTE 3. CASH AND INVESTMENTS

The City uses a central cash and investment pool for certain Governmental Funds and Proprietary Funds. The cash and investment pool balances are classified as cash and cash equivalents in the accompanying financial statements. The City's investment policy with respect to the cash and investment pool is to maximize investment earnings while maintaining an acceptable level of risk. Because investments in the pool must provide for the future needs of the City, flexibility and liquidity of investments are generally maintained at all times.

At June 30, 2006, investments of the primary government (except for Permanent and Pension Trust Funds) and component units consist of the following:

	<u>Weighted Average Maturity (Years)</u>	<u>Fair Value or Carrying Amount</u>
Primary Government – Governmental Activities:		
U.S. Government agency securities	0.91	\$36,631,082
Certificates of deposit classified as investments	<u>0.34</u>	<u>16,605,399</u>
Total	<u>0.73</u>	<u>\$53,236,481</u>
Primary Government – Business-Type Activities:		
U.S. Government agency securities	0.74	\$36,063,664
Certificates of deposit classified as investments	<u>0.75</u>	<u>9,177,214</u>
Total	<u>0.75</u>	<u>\$45,240,878</u>
Component Units:		
U.S. Treasury Notes	1.86	\$ 2,576,968
U.S. Government agency securities	2.94	1,376,980
Certificates of deposit classified as investments	0.74	655,128
Cash equivalents classified as investments	<u>0.24</u>	<u>9,934,204</u>
Total	<u>0.80</u>	<u>\$14,543,280</u>

Interest rate risk - As a means of limiting its exposure to fair value losses arising from rising interest rates, the City's policies require purchases of investments with maturities of two years or less. The City presents its exposure to interest rate changes using the weighted average maturity method. The City manages its interest rate risk by limiting the weighted average maturity of its investment portfolio to less than one year. The City's investment portfolio did not experience any significant fluctuations in fair value during the year.

Custodial credit risk - The City's policies limit deposits and investments to those instruments allowed by applicable state laws. State statutes require that all deposits with financial institutions must be collateralized by securities whose market value is equal to 105% of the value of the uninsured deposits. The deposits must be covered by federal depository insurance or the Tennessee Bank Collateral Pool, by collateral held by the City's agent in the City's name, or by the Federal Reserve Banks acting as third party agents. State statutes also authorize the City to invest in bonds, notes or treasury bills of the United States or any of its agencies, certificates of deposit at Tennessee state chartered banks and savings and loan associations and federally chartered banks and savings and loan associations, repurchase agreements utilizing obligations of the United States or its agencies as the underlying securities, the state pooled investment fund, and mutual funds. Statutes also require that securities underlying repurchase agreements must have a market value at least equal to the amount of funds invested in the repurchase transaction.

Credit risk - The City's policies are designed to maximize investment earnings, while protecting the security of principal and providing adequate liquidity, in accordance with all applicable state laws. At June 30, 2006, the primary government's investments in U.S. Government agency securities include Federal Home Loan Bank and Federal National Mortgage Association bonds, which were rated AAA by Standard & Poor's Rating Service (S & P) or Moody's Investor Service (Moody's).

Component unit investments in U.S. Government agency securities of \$1,376,980 were securities of the Federal Home Loan Bank, Federal Home Loan Mortgage Corporation, and Federal National Mortgage Association, which were rated AAA by S & P or Moody's.

Permanent and Pension Trust funds - The Permanent and Pension Trust funds are managed with long-term objectives that include maximizing total investment earnings. State statutes and City policies allow the Permanent and Pension Trust funds a broader range of investments than other City investments. The City's Pension Trust funds have no investments in any one issuer that represent 5 percent or more of plan net assets. The credit risk of investments of the Permanent and Pension Trust funds is summarized as follows:

	<u>S & P or Moody's Rating</u>	<u>Fair Value</u>
<u>Permanent funds</u>		
Common Trust fund	Not rated	\$ 232,153
Mutual funds - equity	Not rated	1,876,233
Mutual funds - fixed income	Not rated	810,328
Mutual funds - government securities	Not rated	280,025
Cash equivalents classified as investments	Not rated	<u>33,655</u>
		<u>\$3,232,394</u>

	S & P or Moody's Rating	Fair Value
<u>City of Chattanooga General Pension Plan</u>		
Domestic corporate bonds	B	\$ 1,556,723
Domestic corporate bonds	BA	731,463
Domestic corporate bonds	CAA	1,390,928
Domestic corporate bonds	Not rated	963,577
Mutual funds - equity	Not rated	45,187,293
Mutual funds - fixed income	Not rated	44,288,587
Domestic equity securities	Not rated	90,717,897
Limited partnerships	Not rated	26,156,992
Temporary investments	Not rated	4,848,162
		<u>\$215,841,622</u>
<u>Firemen's and Policemen's Insurance and Pension Fund</u>		
U.S. Government securities	AAA	\$ 18,975,661
Domestic corporate bonds	AAA	3,830,846
Domestic corporate bonds	AA	6,243,558
Foreign bonds	AA	57,007
Domestic corporate bonds	A	9,580,119
Foreign bonds	A	548,764
Domestic corporate bonds	BAA	3,335,327
Municipal bonds	BAA	67,214
Foreign bonds	BAA	755,929
Domestic corporate bonds	Not rated	233,454
Mutual funds - equity	Not rated	70,981,234
Domestic equity securities	Not rated	114,111,172
Temporary investments	Not rated	7,151,243
Investment in real estate corporation	Not rated	875,000
		<u>\$236,746,528</u>

NOTE 4. RECEIVABLES

Receivables at June 30, 2006, consist of the following:

	<u>Governmental Activities Funds</u>			Business-Type Activities	Total
	<u>General</u>	<u>Capital Projects</u>	<u>Other Governmental</u>		
Primary Government					
Receivables:					
Taxes	\$ 90,458,899	\$ -	\$ -	\$ -	\$ 90,458,899
Accounts	-	77,344	57,990	75,962	211,296
Notes	1,340,112	859,777	-	-	2,199,889
Customer service	-	-	-	49,055,494	49,055,494
Other	4,684,618	-	-	365,139	5,049,757
Intergovernmental	<u>17,697,478</u>	<u>1,906,532</u>	<u>2,919,456</u>	<u>45,023</u>	<u>22,568,489</u>
Gross receivables	114,181,107	2,843,653	2,977,446	49,541,618	169,543,824
Less:					
Allowance for uncollectibles	<u>(2,939,447)</u>	<u>-</u>	<u>-</u>	<u>(951,009)</u>	<u>(3,890,456)</u>
Net receivables	<u>\$111,241,660</u>	<u>\$2,843,653</u>	<u>\$2,977,446</u>	<u>\$48,590,609</u>	<u>\$165,653,368</u>

Taxes receivable include the uncollected property taxes from tax levies made during the current and past nine years, as well as the anticipated levy for the current calendar year. The allowance for uncollectible taxes is the weighted average percentage of prior year collections on delinquent taxes to the total delinquent taxes receivable at June 30, 2006.

NOTE 5. INTERFUND RECEIVABLES AND PAYABLES

Interfund receivables and payables are due to charges between funds that are outstanding as of June 30, 2006, as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
Capital Projects Fund	Nonmajor Governmental Funds (Hotel/Motel)	\$385,616
Nonmajor Governmental Funds	General Fund	
Public Library		143
Human Services		3,713
State Street Aid		91
Major Enterprise Funds		
Interceptor Sewer Fund	General Fund	13,330
Solid Waste/Sanitation Fund	General Fund	338
Storm Water Fund	General Fund	1,684
Internal Service Fund	General Fund	<u>1,929</u>
		<u>\$406,844</u>

NOTE 6. INTERFUND TRANSFERS

	<u>Transfers In:</u>				<u>Total</u>
	<u>General Fund</u>	<u>Capital Projects</u>	<u>Nonmajor Governmental</u>	<u>Storm Water</u>	
Transfers out:					
General Fund	\$ -	\$6,164,000	\$13,622,444	\$683,952	\$20,470,396
Capital Projects Fund	-	-	1,632,495	-	1,632,495
Nonmajor Governmental Funds	-	2,372,311	1,721,943	-	4,094,254
Electric Power Board	<u>3,142,000</u>	-	-	-	<u>3,142,000</u>
Total	<u>\$3,142,000</u>	<u>\$8,536,311</u>	<u>\$16,976,882</u>	<u>\$683,952</u>	<u>\$29,339,145</u>

Transfers are used to 1) move revenues from the General Fund, the Capital Projects Fund, the Community Development Fund, and the Hotel/Motel Tax Fund to the Debt Service Fund as debt service principal and interest payments become due, 2) move restricted amounts from borrowings to the Capital Projects Fund and the Debt Service Fund as required, 3) move unrestricted revenues from the General Fund to other funds for various programs that the City must account for in other funds in accordance with budgetary authorizations, including amounts provided as subsidies or matching funds for various grant programs, and 4) record payments in lieu of taxes from the Electric Power Board to the General Fund.

NOTE 7. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2006 is as follows:

Primary Government

Governmental Activities:

	Beginning Balance	Additions	Deductions	Ending Balance
Non-Depreciable Assets:				
Land and land improvements	\$ 963,318,784	\$ 28,037,378	\$ 2,356,031	\$ 989,000,131
Construction in Progress	<u>69,400,659</u>	<u>15,333,407</u>	<u>63,904,489</u>	<u>20,829,577</u>
Total non-depreciable assets	<u>1,032,719,443</u>	<u>43,370,785</u>	<u>66,260,520</u>	<u>1,009,829,708</u>
Depreciable Assets:				
Buildings	155,490,391	250,084	-	155,740,475
Vehicles and machinery	89,712,014	6,735,904	1,554,173	94,893,745
Improvements other than buildings	21,976,300	783,525	-	22,759,825
Infrastructure	<u>568,601,250</u>	<u>49,002,287</u>	<u>-</u>	<u>617,603,537</u>
Total depreciable assets	<u>835,779,955</u>	<u>56,771,800</u>	<u>1,554,173</u>	<u>890,997,582</u>
Less Accumulated Depreciation for:				
Buildings	39,329,198	4,702,265	-	44,031,463
Vehicles and machinery	62,587,656	7,565,673	1,516,885	68,636,444
Improvements other than buildings	14,063,446	709,099	-	14,772,545
Infrastructure	<u>222,241,222</u>	<u>23,374,589</u>	<u>-</u>	<u>245,615,811</u>
Total accumulated depreciation	<u>338,221,522</u>	<u>36,351,626</u>	<u>1,516,885</u>	<u>373,056,263</u>
Depreciable Assets, net	<u>497,558,433</u>	<u>20,420,174</u>	<u>37,288</u>	<u>517,941,319</u>
Governmental activities capital assets, net	<u>\$1,530,277,876</u>	<u>\$63,790,959</u>	<u>\$66,297,808</u>	<u>\$1,527,771,027</u>
Business-Type Activities:				
Non-Depreciable Assets:				
Land	\$ 14,005,371	\$ 148,617	\$ 82,000	\$ 14,071,988
Construction in Progress	<u>34,283,000</u>	<u>16,243,000</u>	<u>992,000</u>	<u>49,534,000</u>
Total non-depreciable assets	<u>48,288,371</u>	<u>16,391,617</u>	<u>1,074,000</u>	<u>63,605,988</u>
Depreciable Assets:				
Buildings	68,406,837	417,000	213,000	68,610,837
Vehicles and machinery	427,343,390	22,706,241	13,124,565	436,925,066
Sewer system	399,808,197	3,622,122	330,600	403,099,719
Storm water system	42,496,355	1,276,979	-	43,773,334
Telecommunications	<u>22,622,000</u>	<u>5,648,000</u>	<u>1,531,000</u>	<u>26,739,000</u>
Total depreciable assets	<u>960,676,779</u>	<u>33,670,342</u>	<u>15,199,165</u>	<u>979,147,956</u>
Less Accumulated Depreciation for:				
Buildings	15,508,313	2,042,638	11,113,000	6,437,951
Vehicles and machinery	189,981,866	15,645,303	89,564	205,537,605
Sewer system	143,233,586	7,871,780	-	151,105,366
Storm water system	5,450,353	869,223	-	6,319,576
Telecommunications	<u>6,946,000</u>	<u>2,142,000</u>	<u>564,000</u>	<u>8,524,000</u>
Total accumulated depreciation	<u>361,120,118</u>	<u>28,570,944</u>	<u>11,766,564</u>	<u>377,924,498</u>
Depreciable Assets, net	<u>599,556,661</u>	<u>5,099,398</u>	<u>3,432,601</u>	<u>601,223,458</u>
Business-type activities capital assets, net	<u>\$ 647,845,032</u>	<u>\$ 21,491,015</u>	<u>\$ 4,506,601</u>	<u>\$ 664,829,446</u>

Discretely Presented Component Units

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Deductions</u>	<u>Ending Balance</u>
Non-Depreciable Assets:				
Land	\$ 4,380,320	\$ -	\$ -	\$ 4,380,320
Construction in Progress	<u>9,121,687</u>	<u>6,996,888</u>	<u>-</u>	<u>16,118,575</u>
Total non-depreciable assets	<u>13,502,007</u>	<u>6,996,888</u>	<u>-</u>	<u>20,498,895</u>
Depreciable Assets:				
Buildings	48,846,764	64,374	-	48,911,138
Vehicles and machinery	39,985,744	4,226,792	194,315	44,018,221
Improvements other than buildings	<u>33,384,807</u>	<u>1,001,849</u>	<u>-</u>	<u>34,386,656</u>
Total depreciable assets	<u>122,217,315</u>	<u>5,293,015</u>	<u>194,315</u>	<u>127,316,015</u>
Less Accumulated Depreciation for:				
Buildings	27,945,627	2,028,446	-	29,974,073
Vehicles and machinery	25,434,057	3,346,368	13,880	28,766,545
Improvements other than buildings	<u>4,181,900</u>	<u>1,454,931</u>	<u>-</u>	<u>5,636,831</u>
Total accumulated depreciation	<u>57,561,584</u>	<u>6,829,745</u>	<u>13,880</u>	<u>64,377,449</u>
Depreciable Assets, net	<u>64,655,731</u>	<u>(1,536,730)</u>	<u>180,435</u>	<u>62,938,566</u>
Component units capital assets, net	<u>\$ 78,157,738</u>	<u>\$ 5,460,158</u>	<u>\$180,435</u>	<u>\$ 83,437,461</u>

Depreciation expense is charged to functions as follows:**Primary Government – Governmental Activities:**

General government	\$13,509,661
Public Safety	943,161
Public Works	21,156,141
Parks and Recreation	680,968
Social Services	<u>61,695</u>
Total	<u>\$36,351,626</u>

Primary Government – Business-Type Activities:

Sewer	\$ 9,904,556
Solid Waste/Sanitation	581,536
Storm Water	947,874
Housing Management	301,978
Electric Utility	<u>16,835,000</u>
Total	<u>\$28,570,944</u>

Discretely Presented Component Units:

Transportation Authority	\$ 3,960,932
Airport Authority	2,755,020
Downtown Redevelopment	<u>113,793</u>
Total	<u>\$ 6,829,745</u>

NOTE 8. LONG-TERM LIABILITIES

Changes in long-term liabilities for the fiscal year ended June 30, 2006, were as follows:

	Balance July 1, 2005	Additions	Reductions	Balance June 30, 2006	Due Within One Year
Primary Government					
GOVERNMENTAL ACTIVITIES					
General obligation serial bonds	\$125,317,464	\$ -	\$ 4,637,068	\$120,680,396	\$ 5,328,276
Notes payable	13,594,190	10,293,507	2,531,115	21,356,582	2,603,689
Capital leases payable	118,842,663	-	566,954	118,275,709	2,761,814
Compensated absences	<u>16,918,571</u>	<u>9,792,080</u>	<u>9,501,828</u>	<u>17,208,823</u>	<u>914,437</u>
Total governmental activities	<u>\$274,672,888</u>	<u>\$20,085,587</u>	<u>\$17,236,965</u>	277,521,510	<u>\$11,608,216</u>
Net deferred refunding and original issue premiums and discounts				<u>(667,177)</u>	
				<u>\$276,854,333</u>	
BUSINESS-TYPE ACTIVITIES					
EPB:					
Revenue bonds	\$ 33,600,000	\$ -	\$ 1,600,000	\$ 32,000,000	\$ 1,600,000
Notes payable	1,774,000	1,347,000	505,000	2,616,000	645,000
Compensated absences	<u>962,000</u>	<u>-</u>	<u>98,000</u>	<u>864,000</u>	<u>-</u>
	<u>36,336,000</u>	<u>1,347,000</u>	<u>2,203,000</u>	<u>35,480,000</u>	<u>2,245,000</u>
Interceptor Sewer System:					
General obligation serial bonds	83,022,015	-	8,660,914	74,361,101	8,845,403
Notes payable	44,140,355	-	1,837,679	42,302,676	1,897,758
Capital leases payable	234,453	-	19,891	214,562	21,019
Compensated absences	<u>845,911</u>	<u>566,074</u>	<u>533,461</u>	<u>878,524</u>	<u>52,532</u>
	<u>128,242,734</u>	<u>566,074</u>	<u>11,051,945</u>	<u>117,756,863</u>	<u>10,816,712</u>
Solid Waste/Sanitation Fund:					
General obligation serial bonds	26,041,104	-	1,988,455	24,052,649	2,018,242
Compensated absences	<u>124,321</u>	<u>5,619</u>	<u>52,978</u>	<u>76,962</u>	<u>4,632</u>
	<u>26,165,425</u>	<u>5,619</u>	<u>2,041,433</u>	<u>24,129,611</u>	<u>2,022,874</u>
Storm Water Fund:					
General obligation serial bonds	16,324,417	-	1,328,563	14,995,854	1,353,079
Notes payable	1,297,921	-	147,738	1,150,183	153,720
Compensated absences	<u>203,797</u>	<u>149,363</u>	<u>168,478</u>	<u>184,682</u>	<u>13,995</u>
	<u>17,826,135</u>	<u>149,363</u>	<u>1,644,779</u>	<u>16,330,719</u>	<u>1,520,794</u>
Total business-type activities	<u>\$208,570,294</u>	<u>\$ 2,068,056</u>	<u>\$16,941,157</u>	193,697,193	<u>\$16,605,380</u>
Net deferred refunding and original issue premiums and discounts				<u>(73,044)</u>	
				<u>\$193,624,149</u>	

	<u>Balance</u> <u>July 1, 2005</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance</u> <u>June 30, 2006</u>	<u>Due Within</u> <u>One Year</u>
Discretely Presented Component Units					
Metropolitan Airport Authority:					
Revenue bonds	\$ 14,520,000	\$ -	\$ 585,000	\$ 13,935,000	\$ 630,000
Chattanooga Downtown Redevelopment Corporation:					
Revenue bonds	129,200,000	-	-	129,200,000	2,570,000
Notes payable	<u>186,703</u>	<u>-</u>	<u>186,703</u>	<u>-</u>	<u>-</u>
Total component units	<u>\$143,906,703</u>	<u>\$ -</u>	<u>\$ 771,703</u>	143,135,000	<u>\$ 3,200,000</u>
Original issue premiums and discounts				<u>3,920</u>	
				<u>\$143,138,920</u>	

In prior years, the City refunded certain general obligation and sewage facility bonds by placing the proceeds of new bonds in irrevocable trusts to provide for all future debt service payments on the refunded bonds. Accordingly, the trust account assets and the liabilities for the refunded bonds are not included in the City's financial statements. At June 30, 2006, the liabilities for the bonds refunded were as follows:

<u>Year</u> <u>Refunded</u>	<u>Remaining</u> <u>Liability</u>
1986	\$ 5,600,000
1992	17,570,000
1996	10,000,000
1998	26,715,000
2002	40,480,000
2003	31,930,000
2005	51,510,000

Debt related to governmental activities at June 30, 2006, consisted of the following:

General Obligation Bonds - The City periodically issues general obligation bonds for the acquisition and construction of major capital facilities. These bonds are direct obligations and are backed by the full faith and credit of the City. Certain bonds are subject to federal arbitrage regulations. These bonds are generally issued as 15 to 30-year serial bonds. General obligation bonds are summarized by issue as follows:

<u>Issue</u>	<u>Interest Rates</u>	<u>Principal Amount</u>
Public Improvement Refunding, Series 1998	5.00% - 5.50%	\$ 7,209,200
Municipal Public Improvement, Series 2001	5.00%	17,816,200
Public Improvement Refunding, Series 2002	4.00% - 5.38%	8,748,900
Refunding Bonds, 2002 Series A	3.00% - 5.00%	3,938,308
Hotel-Motel Tax Pledge, Series 2002	3.00% - 5.00%	49,705,000
General Obligation, 2003 Series A	2.50% - 4.20%	10,570,000
General Obligation, 2005 Series A	3.00% - 5.00%	17,222,801
Hotel-Motel Tax Refunding, Series 2005A	3.00% - 5.00%	<u>5,469,987</u>
Total payable from the Debt Service Fund		<u>\$120,680,396</u>

Hamilton County Series 1991 - Parking Garage - The City entered into an agreement with Hamilton County for cost sharing with respect to the parking garage for the Hamilton County/City of Chattanooga Courts/Jail complex in the principal amount of \$917,418. Hamilton County issued 15-year serial bonds to cover the cost of construction at rates ranging from 4.5% to 6.5%. Principal and interest payments are due annually to the County beginning 1992 through 2007. The remaining balance at June 30, 2006, is \$60,781.

Tennessee Municipal Bond Fund Loan (1997) - Pursuant to a loan agreement with the Tennessee Municipal Bond Fund, the City of Chattanooga is authorized to incur indebtedness up to \$7,908,000 for the purpose of financing certain general government capital projects. The maximum amount authorized by the agreement is being reserved by the Trustee and is disbursed to the City upon request. The loan will be repaid over a 15-year period at variable interest rates through 2012. Interest rate changes are based on the short-term tax exempt rate that is remarketed and published weekly. The balance at June 30, 2006, is \$3,935,023.

Tennessee Municipal Bond Fund Loan (2003) - Pursuant to a loan agreement with the Tennessee Municipal Bond Fund, the City of Chattanooga is authorized to incur indebtedness up to \$6,000,000 for the purpose of paying for certain general government capital projects. The maximum amount authorized by the agreement is being reserved by the Trustee and is disbursed to the City upon request. The loan will be repaid over a 15-year period at variable rates through 2018. Interest rate changes are based on the short-term tax exempt rate that is remarketed and published weekly. The balance at June 30, 2006, is \$1,683,698.

Tennessee Municipal Bond Fund Loan (2004) - Pursuant to a loan agreement with the Tennessee Municipal Bond Fund, the City of Chattanooga is authorized to incur indebtedness up to \$25,000,000 for the purpose of paying for certain general government capital projects. The maximum amount authorized by the agreement is being reserved by the Trustee and is disbursed to the City upon request. The loan will be repaid over a 20-year period at variable rates through 2024. Interest rate changes are based on the short-term tax exempt rate that is remarketed and published weekly. The balance at June 30, 2006, is \$13,045,464.

Fire Hall Land Note - During 1999 the City acquired land for the construction of a fire hall. In connection with acquiring the property, the City executed a note payable to the former owners. The note bears interest at 9.5% and will be repaid over a 15-year period. The balance at June 30, 2006, is \$31,073.

Fannie Mae American Communities Fund – In July 2003, the City entered into an agreement with Fannie Mae to borrow up to \$5,000,000 for the purpose of funding HOPE VI projects. The loan will be repaid over a 10-year period at variable rates of interest. Interest rates are adjusted quarterly to the published 3-month LIBOR plus 1.5% (7.01% at June 30, 2006). The balance at June 30, 2006, is \$2,473,620.

Chattanooga Downtown Redevelopment Corporation Capital Lease - In October 2000, the City entered into a noncancelable long-term lease with the Chattanooga Downtown Redevelopment Corporation (CDRC), for financing the cost of designing, acquiring, constructing and equipping four facilities in the Tourist Development Zone comprising more than 631,210 square feet at a cost of over \$120 million. Facilities include (1) the Chattanooga-a residential conference center, (2) parking garage, (3) the Development Resource Center, and (4) an expansion of the Chattanooga-Hamilton County Convention and Trade Center. The lease provides for semiannual payments in amounts sufficient to meet the annual debt service requirements on \$129 million in revenue bonds issued by the Industrial Development Board of the City of Chattanooga on behalf of the CDRC, a non-profit corporation. The IDB bonds are secured by payments to be made by the CDRC. The lease payments will be funded by the City's share of the 1/2% increase in the county-wide sales tax passed by county-wide referendum, income from the Chattanooga, state incremental sales tax generated in the Tourist Development Zone and interest income from a debt service reserve fund in excess of \$9 million included as part of the bond issue. In the event these sources are insufficient, the City agreed to appropriate sufficient moneys to make the lease payments. The City's lease payment was \$5,532,337 for the year ended June 30, 2006. The recorded liability under this capital lease at June 30, 2006, is \$115,925,472.

The debt service reserve fund held by the fiscal agent at June 30, 2006 is \$9,934,204. The fiscal agent is required by the agreement to apply any interest on the debt service reserve fund toward the lease payments. The debt service reserve fund will be used to retire debt near the end of the lease.

Equipment Capital Lease - In September 2003, the City entered into an equipment lease-purchase agreement to finance radio communications equipment and software upgrades at the Hamilton County "911" Emergency Communications District totaling \$3,800,000. The lease term is six years and provides for annual payments which began July 1, 2004. The recorded liability under this capital lease at June 30, 2006, is \$2,350,237.

Republic Parking Equipment Loan – During 2005 CDRC entered into a loan agreement with the Republic Parking System, Inc. The loan was for the purpose of financing parking garage equipment. The loan will be repaid in monthly installments for 36 months at 7.00% interest. During 2006 the loan and the related equipment were transferred from CDRC (a discretely-presented component unit) to governmental activities in connection with establishing the River Pier Garage Fund (a Special Revenue Fund). This transfer is included in additions to notes payable and capital assets of the primary government's governmental activities and reductions in notes payable and capital assets of discretely presented component units. The balance at June 30, 2006 is \$126,923.

Debt service requirements for general obligation bonds, notes payable, and capital leases are met by the General Fund. The compensated absences liability attributable to governmental activities will be liquidated by the General Fund and the Special Revenue Funds.

Debt related to business-type activities at June 30, 2006, consisted of the following:

<u>Issue</u>	<u>Interest Rates</u>	<u>Principal Amount</u>
EPB:		
Electric System Revenue Bonds, Series 2000	4.50% - 5.38%	\$ 32,000,000
Equipment Notes	4.40% - 4.95%	2,616,000
Interceptor Sewer System Fund:		
Municipal Public Improvement, Series 1998	5.00%	1,375,000
Municipal Public Improvement Refunding, Series 1998	5.00% - 5.50%	13,286,100
Municipal Public Improvement Refunding, Series 2002	3.50% - 4.50%	19,329,151
Refunding Bonds, 2002 Series A	3.00% - 5.00%	21,036,692
Refunding Bonds, 2003 Series B	3.00% - 3.25%	6,865,000
Refunding Bonds, 2005 Series A	3.00% - 5.00%	12,469,158
1992 State Revolving Sewer Loan*	3.98%	1,150,184
Northwest Georgia Sewer Expansion Project	4.00%	5,336,989
State Revolving Loan 2003	2.98%	35,815,503
City of Collegedale Capital Lease	Variable	214,562
Solid Waste/Sanitation Fund:		
Municipal Public Improvement, Series 1998	5.00%	760,000
Municipal Public Improvement Refunding, Series 1998	5.00% - 5.50%	3,686,100
Municipal Public Improvement, Series 2001	5.00%	3,032,600
Municipal Public Improvement Refunding, Series 2002	4.00% - 5.38%	6,774,887
Refunding Bonds, 2005 Series A	3.00% - 5.00%	9,799,062
Storm Water Fund:		
Municipal Public Improvement, Series 1998	5.00%	565,000
Municipal Public Improvement Refunding, Series 1998	5.00% - 5.50%	2,528,600
Municipal Public Improvement, Series 2001	5.00%	901,200
Municipal Public Improvement Refunding, Series 2002	4.00% - 5.38%	4,997,062
Refunding Bonds, 2005 Series A	3.00% - 5.00%	6,003,992
1992 State Revolving Sewer Loan*	3.98%	1,150,183
Total payable from business-type activities		<u>\$191,693,025</u>

*1992 State Revolving Loan Fund - The City entered into an agreement with the Tennessee Department of Health and Environment to secure a loan for the purpose of constructing a Combined Sewer Overflow Facility located at Ross's Landing. The loan will be repaid in monthly installments through 2013 with interest at 3.98%. The remaining balance at June 30, 2006, is \$2,300,367.

Georgia State Revolving Loan - Pursuant to a loan agreement with the Georgia State Revolving Loan Fund, the City of Chattanooga is authorized to incur indebtedness up to \$7,255,000 for the purpose of financing sewer expansion in Northwest Georgia. The maximum amount authorized by the agreement is being reserved by the Georgia Environmental Facilities Authority and is disbursed to the City upon request. The loan will be repaid over a 20-year period at 4% interest through 2020. The balance at June 30, 2006, is \$5,336,989.

State Revolving Loan 2003 - The City entered into an agreement with the Tennessee Department of Environment and Conservation and the Tennessee Local Development Authority to secure a loan for the purpose of financing sewer projects. The loan will be repaid in monthly installments through 2025 at 2.98% interest. The balance at June 30, 2006, is \$35,815,503.

Capital Leases – The City has an agreement with the City of Collegedale to lease and purchase sewer system improvements. Lease payments are due in monthly installments through 2015 at variable rates of interest. The balance on this capital lease at June 30, 2006, is \$214,562.

EPB Equipment Notes – EPB has five installment notes outstanding at June 30, 2006, totaling \$2,616,000. The proceeds of these notes were used for electrical equipment. The notes will be repaid over a 5-year period at interest rates in the range of 4.40% to 4.95%.

Component Units debt at June 30, 2006, consisted of the following:

<u>Issue</u>	<u>Interest Rates</u>	<u>Principal Amount</u>
Metropolitan Airport Authority:		
Series A Refunding Revenue Bonds, Series 2002	2.76% - 2.80%	\$ 12,625,000
Series B Refunding Revenue Bonds, Series 2002	2.76% - 2.80%	1,310,000
Chattanooga Downtown Redevelopment Corporation:		
Chattanooga Lease Rental Revenue Bonds, Series 2000	5.00% - 5.625%	<u>129,200,000</u>
Total payable from Component Units		<u>\$143,135,000</u>

Principal and interest requirements to maturity for bonds and notes payable, excluding amounts for compensated absences, are as follows:

<u>Year</u>	<u>Primary Government</u>			
	<u>Governmental Activities</u>		<u>Business-Type Activities</u>	
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2007	\$ 7,931,965	\$ 6,215,604	\$ 16,513,202	\$ 8,040,886
2008	6,831,505	5,924,001	14,942,188	7,418,927
2009	8,193,534	5,629,801	16,965,286	6,819,370
2010	8,466,577	5,265,435	14,987,610	6,099,723
2011	8,402,276	4,921,778	13,965,122	5,452,427
2012-2016	32,289,521	20,313,844	56,076,480	19,017,577
2017-2021	23,389,400	13,880,275	38,555,042	7,608,150
2022-2026	26,672,200	8,433,632	19,743,533	2,034,468
2027-2031	19,860,000	2,576,825	-	-
	<u>\$142,036,978</u>	<u>\$73,161,195</u>	<u>\$191,478,463</u>	<u>\$62,491,528</u>
<u>Year</u>	<u>Component Units</u>			
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2007	\$ 3,200,000	\$ 7,843,290	\$ 3,200,000	\$ 7,843,290
2008	3,375,000	7,672,390	3,375,000	7,672,390
2009	2,955,000	7,527,630	2,955,000	7,527,630
2010	3,825,000	7,337,330	3,825,000	7,337,330
2011	3,950,000	7,133,293	3,950,000	7,133,293
2012-2016	23,085,000	32,241,286	23,085,000	32,241,286
2017-2021	29,815,000	25,004,515	29,815,000	25,004,515
2022-2026	31,375,000	16,561,197	31,375,000	16,561,197
2027-2031	41,555,000	6,121,194	41,555,000	6,121,194
	<u>\$143,135,000</u>	<u>\$117,442,125</u>	<u>\$143,135,000</u>	<u>\$117,442,125</u>

Principal and interest requirements to maturity for capital leases are as follows:

Year	Primary Government			
	Governmental Activities		Business-Type Activities	
	Principal	Interest	Principal	Interest
2007	\$ 2,761,814	\$ 7,551,670	\$ 21,019	\$12,633
2008	2,910,119	7,401,615	22,245	11,408
2009	3,066,000	7,242,359	23,575	10,078
2010	3,229,695	7,073,415	25,018	8,635
2011	2,789,754	6,894,284	26,585	7,068
2012-2016	16,879,059	31,508,976	96,120	10,447
2017-2021	22,891,938	25,306,096	-	-
2022-2026	31,046,241	16,889,956	-	-
2027-2031	32,701,089	5,464,949	-	-
	<u>\$118,275,709</u>	<u>\$115,333,320</u>	<u>\$214,562</u>	<u>\$60,269</u>

NOTE 9. DEFERRED COMPENSATION PLAN

The City offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all City employees, permits them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

Assets in the plan are recorded at market value but are administered by private corporations under contract with the City. It is the opinion of the City's legal counsel that the City has no liability for losses under the plan but does have the duty of due care that would be required of an ordinary prudent investor. The following is a summary of activity in the Plan for the year:

Asset balance at July 1, 2005	\$13,835,079
Deferrals of compensation	1,636,877
Earnings	1,195,597
Withdrawals	(896,630)
Administrative expenses	<u>(156)</u>
Asset balance at June 30, 2006	<u>\$15,770,767</u>

NOTE 10. EMPLOYEE RETIREMENT SYSTEMS

The primary government provides retirement benefits through three single employer defined benefit pension plans (General Pension Plan, Firemen's and Policemen's Insurance and Pension Fund, and EPB Pension Plan). All employees are eligible to participate in one of these retirement benefit plans. The City acts as Trustee for the General Pension Plan and the Firemen's and Policemen's Insurance and Pension Plan, which are included in the accompanying financial statements as pension trust funds. The City does not administer the assets of the EPB Pension Plan, therefore they are not included in the accompanying financial statements. The following is a summary of each of these plans:

City of Chattanooga Administered Pension Plans

Significant Accounting Policies:

Basis of Accounting

The financial statements of the General Pension Plan and the Firemen's and Policemen's Insurance and Pension Fund are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions to each plan are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each plan.

Cash and Cash Equivalents

The cash and cash equivalents of each plan represent balances at the financial institutions that serve as custodians of plan assets, and are not part of the City's centralized cash and investment pool. Occasionally, negative cash balances result from benefit payments and administrative expenses. Negative cash balances are replenished by transfers from investments.

Method Used to Value Investments

Investments are reported at fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Investments that do not have an established market are reported at estimated fair value.

Plan Descriptions:

(1) City of Chattanooga General Pension Plan

The City maintains a single-employer defined benefit pension plan for general City employees. Each participant is required to contribute 2 percent of earnings. The City is currently contributing 6.67 percent of the total covered payroll of the participants, which is the minimum requirement as noted by the most recent actuarial report.

The normal retirement benefit is 2 percent of average earnings multiplied by years of credited service up to twenty (20) years plus one percent of average earnings multiplied by years of credited service in excess of twenty (20) years.

The benefits payable to retirees are increased annually by a 3 percent cost-of-living increase. Future amendments to the plan provisions can be authorized by City ordinance upon recommendation from the Board of Trustees of the General Pension Plan, a statement of impact from the actuary, and a favorable opinion of the Office of Mayor.

The normal retirement date is the first day of the month following the participant's attainment of age 62. Benefits are reduced on a pro rata basis for early retirement. An employee otherwise vested shall be penalized 2.5 percent for each year of age less than 62. However, if the sum of the participant's age and years of credited service is at least eighty (80), there shall be no reduction in the immediate early retirement benefit. A deferred retirement option plan provides alternative benefits for up to 3 years of credited service to eligible members with at least 26 years of credited service.

(2) Firemen's and Policemen's Insurance and Pension Fund

The City maintains a single-employer defined benefit pension plan for the firemen and policemen employed by the City. The Plan is designed for each plan participant to contribute 8 percent of base salary. The City is currently contributing 19.6 percent of the total covered payroll of the participants, which is the minimum requirement as noted by the most recent actuarial report. Increased court costs on all forfeitures of fines or monies or on convictions of violating any City ordinances are recorded as additional contributions to the Plan. The cost of administering the plan is borne by the City.

The normal retirement benefit is 68.75 percent of average base salary, where average base salary is based on the three-year period of service yielding the highest arithmetic average of the participant's salary history. For service beyond 25 years, the benefit is increased 1.25 percent per year up to 30 years of service.

The benefits payable to retirees are increased annually by a 3 percent cost-of-living increase. These benefit provisions may be amended by City ordinance upon recommendation from the Board of Trustees of the Firemen's and Policemen's Insurance and Pension Fund and a favorable opinion of the Office of the Mayor.

The normal retirement date is the first day of the month following the participant's completion of 25 years of credited service. Reduced benefit provisions are available for those participants who have attained age 55 and have completed at least 10 years of credited service. In the event of death, job-related or non-job-related disability, participants who are not yet eligible for normal retirement benefits can receive a percentage of their salary, based on a formula using the three-year period of service yielding the highest arithmetic average of the participant's salary history. A deferred retirement option plan provides alternative benefits for up to 3 years of credit service to eligible members who have 25 years of credited service.

Current membership in each of these plans was comprised of the following as of June 30, 2006:

<u>Group</u>	<u>General Pension Plan</u>	<u>Firemen's and Policemen's Insurance and Pension Fund</u>
Retirees and beneficiaries currently receiving benefits	760	669
Vested terminated employees	73	4
Active employees	1,534	793
Actuarial update	1-1-2006	1-1-2006

Trend Information:

	<u>Year Ended</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation (Asset)</u>
General Pension Plan	12/31/05	\$3,558,187	97.54%	\$(4,255,701)
	12/31/04	2,132,773	118.74%	(4,343,073)
	12/31/03	2,204,619	102.66%	(3,943,428)
Firemen's and Policemen's Fund	12/31/05	6,566,969	97.75%	(4,165,966)
	12/31/04	6,190,284	99.64%	(4,313,641)
	12/31/03	5,719,267	99.36%	(4,336,014)

Funding Policy and Other Information:

The Board of Trustees of each plan establishes and may amend the contribution requirements of plan members and the employer. The City contributes to each plan at an actuarially determined rate. The employer's annual pension cost for the current year and related information for each plan is as follows:

	<u>General Pension Plan</u>	<u>Firemen's and Policemen's Insurance and Pension Fund</u>
Contribution rates for employer	6.67%	19.60%
Contribution rates for plan members	2.00%	8.00%
Annual pension cost	\$3,558,187	\$6,566,969
Contributions made by employer	3,543,256	6,301,668
Contributions made by plan members	1,063,437	2,789,299
Actuarial valuation date for current contributions	January 1, 2006	January 1, 2006
Actuarial cost method	Entry Age	Entry Age
Amortization method	Level Dollar	Level Percent
Remaining amortization period	30 Years Open	30 Years Open
Asset valuation method	Market Value, As Adjusted	5-Year Average
Actuarial assumptions:		
Investment rate of return	7.75%	8.00%
Projected salary increases	4.50-5.50%	3.25%
Inflation rate	3.00%	3.00%

The City's annual pension cost and net pension obligation (asset) related to each plan for the current year were as follows:

	<u>General Pension Plan</u>	<u>Firemen's and Policemen's Insurance and Pension Fund</u>
Annual required contribution	\$ 3,518,054	\$ 6,454,038
Interest on net pension obligation (asset)	(336,588)	(345,091)
Adjustment to annual required contribution	<u>376,721</u>	<u>458,022</u>
Annual pension cost	3,558,187	6,566,969
Contributions made	<u>(3,470,815)</u>	<u>(6,419,294)</u>
Increase in net pension obligation (asset)	87,372	147,675
Net pension obligation (asset) at beginning of year	<u>(4,343,073)</u>	<u>(4,313,641)</u>
Net pension obligation (asset) at end of year	<u>\$(4,255,701)</u>	<u>\$(4,165,966)</u>

During 2006 the General Pension Plan received a litigation settlement of \$4,203,305. This amount is net of attorneys' fees and other costs. The settlement resolved the Plan's claims against a brokerage firm related to the Plan's investment earnings in prior years.

Financial Reports:

The City of Chattanooga administered plans do not issue stand-alone financial reports and are not included in the report of a public employee retirement system or a report of another entity. The plan financial statements are as follows:

Combining Statement of Plan Net Assets:

	<u>General Pension Plan</u>	<u>Firemen's and Policemen's Insurance and Pension Fund</u>	<u>Total</u>
ASSETS			
Receivables:			
Accrued income	\$ 247,553	\$ 674,924	\$ 922,477
Contributions:			
Employer	285,239	-	285,239
Employee	85,529	-	85,529
Due from plan custodian	<u>-</u>	<u>962,709</u>	<u>962,709</u>
Total receivables	<u>618,321</u>	<u>1,637,633</u>	<u>2,255,954</u>
Investments, at fair value:			
U.S. Government securities	-	18,975,661	18,975,661
Municipal bonds	-	67,214	67,214
Corporate bonds	4,642,691	23,223,304	27,865,995
Foreign bonds	-	1,361,700	1,361,700
Corporate stocks	90,717,897	114,111,172	204,829,069
Mutual funds - equity	45,187,293	70,981,234	116,168,527
Mutual funds - fixed income	44,288,587	-	44,288,587
Temporary investments	4,848,162	7,151,243	11,999,405
Limited Partnerships	26,156,992	-	26,156,992
Other investments	<u>-</u>	<u>875,000</u>	<u>875,000</u>
Total investments	<u>215,841,622</u>	<u>236,746,528</u>	<u>452,588,150</u>
Total assets	<u>216,459,943</u>	<u>238,384,161</u>	<u>454,844,104</u>
LIABILITIES			
Due to plan custodian	-	203,223	203,223
Accrued expenses	<u>215,503</u>	<u>420,376</u>	<u>635,879</u>
Total liabilities	<u>215,503</u>	<u>623,599</u>	<u>839,102</u>
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS	<u><u>\$216,244,440</u></u>	<u><u>\$237,760,562</u></u>	<u><u>\$454,005,002</u></u>

Combining Statement of Changes in Plan Net Assets:

	<u>General Pension Plan</u>	<u>Firemen's and Policemen's Insurance and Pension Fund</u>	<u>Total</u>
ADDITIONS			
Contributions:			
Employer	\$ 3,543,256	\$ 6,301,668	\$ 9,844,924
Employee	<u>1,063,437</u>	<u>2,789,299</u>	<u>3,852,736</u>
Total contributions	<u>4,606,693</u>	<u>9,090,967</u>	<u>13,697,660</u>
Investment income:			
Net appreciation in fair market value of investments	21,361,547	18,356,675	39,718,222
Litigation settlement	4,203,305	-	4,203,305
Interest	402,247	3,156,653	3,558,900
Dividends	<u>2,267,657</u>	<u>4,408,653</u>	<u>6,676,310</u>
	28,243,756	25,921,981	54,156,737
Less investment expense	<u>(498,788)</u>	<u>(1,276,003)</u>	<u>(1,774,791)</u>
Net investment income	<u>27,735,968</u>	<u>24,645,978</u>	<u>52,381,946</u>
Total additions	<u>32,342,661</u>	<u>33,736,945</u>	<u>66,079,606</u>
DEDUCTIONS			
Benefits paid to participants	8,779,747	18,195,461	26,975,208
Administrative expenses	<u>224,673</u>	<u>496,204</u>	<u>720,877</u>
Total deductions	<u>9,004,420</u>	<u>18,691,665</u>	<u>27,696,085</u>
NET INCREASE	23,338,241	15,045,280	38,383,521
NET ASSETS HELD IN TRUST FOR PENSION BENEFITS			
Beginning of year	<u>192,906,199</u>	<u>222,715,282</u>	<u>415,621,481</u>
End of year	<u>\$216,244,440</u>	<u>\$237,760,562</u>	<u>\$454,005,002</u>

(3) EPB Pension Plan

Plan Description and Provision:

EPB's Retirement Plan (the "Plan") is a Single Employer Defined Benefit Pension Plan administered by an individual designated by EPB. A stand-alone financial report is not issued for this plan. The Plan provides retirement benefits to Plan members. Article VIII of EPB of Chattanooga Retirement Plan assigns the authority to establish and amend benefit provisions to EPB.

Funding Policy:

Contribution requirements of Plan members and the EPB are established and can be amended by the EPB. The Plan does not require Plan members to make a contribution. The EPB is required to contribute at an actuarially determined rate, the current rate is 9.43% of annual covered payroll.

Annual Pension Cost and Net Pension Obligation:

EPB's annual pension cost of the Plan for the current year was \$2,165,000. There is no net pension obligation as EPB has contributed the annual required contribution, adjusted with interest, as calculated by actuarial valuation. The annual required contribution was determined as part of an actuarial valuation performed as of August 1, 2005, using the aggregate cost method. The aggregate cost method does not identify or separately amortize unfunded actuarial liabilities. Significant actuarial assumptions used in the valuation included (a) a rate of return on the investment of present and future assets of 8.0% per year compounded annually, (b) projected salary increases of 4.0% per year compounded annually, (c) no postretirement benefit increases, and (d) a discount rate of 8.0%.

Trend Information:

<u>Year Ended</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
6/30/06	\$2,165,000	100%	\$ -
6/30/05	1,988,000	100%	-
6/30/04	1,932,000	100%	-

EPB 401(k) Plan

EPB also has a 401(k) plan which permits employees to invest up to 13 percent of salary in a tax-deferred savings plan. EPB contributes up to 4.0 percent of an employee's salary. EPB contributions are fully vested and amounted to \$744,000 for the year ended June 30, 2006.

Pension Plans of Component Units

CARTA is the only component unit with separate defined benefit pension plans, and complete pension disclosures are in CARTA's separately-issued financial statements. Actuarially determined employer contribution requirements were met for the year ended June 30, 2006. Condensed disclosures for CARTA's defined benefit pension plans are as follows:

<u>Year Ended</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation (Asset)</u>
6/30/06	\$414,422	91%	\$ (46,540)
6/30/05	397,422	89%	(127,952)
6/30/04	397,790	95%	(161,485)

Postemployment Benefits

The City provides postemployment health and medical benefits for retirees and their dependents in accordance with the applicable City ordinance. Substantially all of the City's employees may become eligible for the benefits if they reach normal retirement age while working for the City. At June 30, 2006, there were 920 employees who had retired and were receiving healthcare benefits. The City is insured for a portion of these benefits. All the associated costs are accounted for in the General Fund and Enterprise Funds. For the year ended June 30, 2006, the City recognized expenditures of approximately \$6,214,495, which was offset by \$1,527,903 of retiree contributions.

NOTE 11. CONSERVATION PROGRAMS

EPB is a fiscal intermediary for the Tennessee Valley Authority's (TVA) conservation programs. As of June 30, 2006, outstanding funds advanced by TVA totaled \$467,000 to be used by EPB for customer loans in connection with TVA's insulation and heat pump conservation programs. At June 30, 2006, the outstanding receivables for loans made from these funds amounted to \$451,000. A total of approximately \$78,417,000 has been loaned to EPB's customers since the programs were begun in 1977.

NOTE 12. JOINT VENTURE

The City has an equity interest in Carter Street Corporation, a nonprofit organization. Carter Street Corporation's board consists of five members. Two members are appointed by the Mayor of the City and two are appointed by the Hamilton County, Tennessee Mayor. The appointment of the fifth member, who serves as chairman, is agreed on by the City Mayor and the County Mayor.

Carter Street Corporation owns and manages a trade center and a parking garage that were financed by bonds issued by the Industrial Development Board of Chattanooga. The City and Hamilton County, Tennessee funded the repayment of the bonds through lease payments to Carter Street Corporation. Pursuant to the lease agreement, the City has a two-thirds equity interest in Carter Street Corporation upon the repayment of the bonds during the year ended June 30, 2006. The City's lease payments from the General Fund to Carter Street Corporation were \$1,415,389 during the year ended June 30, 2006.

The City's two-thirds equity interest in Carter Street Corporation is computed as follows:

Total net assets	<u>\$13,184,969</u>
Multiplied by two-thirds	<u> x 2/3</u>
City's equity interest	<u>\$ 8,789,979</u>

Complete financial statements can be obtained from: Carter Street Corporation
P.O. Box 6008
Chattanooga, TN 37401

Condensed financial information for Carter Street Corporation as of June 30, 2006, is as follows:

ASSETS

Cash	\$ 698,780
Accounts receivable, net	377,459
Inventories	80,002
Prepaid items	27,931
Capital assets, net	12,208,636
Other assets	<u>19,300</u>
Total assets	<u>\$13,412,108</u>

LIABILITIES AND NET ASSETS

LIABILITIES

Accounts payable and accrued expenses	\$ 172,973
Accrued interest	-
Advance deposits	54,166
Bonds payable	<u>-</u>
Total liabilities	<u>227,139</u>

NET ASSETS

Invested in capital assets, net of related debt	12,208,636
Unrestricted	<u>976,333</u>
Total net assets	<u>13,184,969</u>
Total liabilities and net assets	<u>\$13,412,108</u>

SCHEDULE OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

Total operating revenues	\$ 5,624,831
Total operating expenses	<u>6,352,996</u>
Loss from operations	(728,165)
Nonoperating revenues	618,178
Nonoperating expenses	<u>21,746</u>
Net loss	(131,733)
Net assets at July 1, 2005	<u>13,316,702</u>
Net assets at June 30, 2006	<u>\$13,184,969</u>

NOTE 13. COMMITMENTS AND CONTINGENCIES

The City and its component units are parties to various lawsuits and claims in the ordinary course of their operations. Management believes that the potential adverse impact of these proceedings would not be material to the basic financial statements of the City.

The City has received federal and state grants for specific purposes that are subject to review and audit by grantor agencies. Such audits could result in reimbursements to the grantor agencies for expenditures disallowed under the terms of the grants. City management is not aware of any potential losses from such disallowances and believes that reimbursements, if any, would not be material.

The City has entered into various construction commitments. Such contracts include contracts for improvements to sewer, solid waste, and storm water systems, and acquisition and construction contracts related to general government capital projects. Several of these contracts were in progress but not completed as of June 30, 2006. The total contractual commitments outstanding as of June 30, 2006, aggregated approximately \$20,869,032. The City has sufficient funds available to cover these commitments

NOTE 14. CONDUIT DEBT OBLIGATIONS

From time to time, the Industrial Development Board and the Health, Educational and Housing Facility Board of the City of Chattanooga have issued bonds to provide financial assistance to private-sector entities for the acquisition and construction of industrial and commercial facilities deemed to be in the public interest. The bonds are secured by the property financed and are payable solely from payments received on the underlying mortgage loans. Upon repayment of the bonds, ownership of the acquired facilities transfers to the private-sector entity served by the bond issuance. Neither the City, the State, nor any political subdivision thereof is obligated in any manner for repayment of the bonds. Accordingly, the bonds are not reported as liabilities in the accompanying financial statements.

As of June 30, 2006, 119 series of Industrial Revenue Bonds had been issued. The principal amount of the series issued after July 1, 1995, was \$197,400,000. The aggregate principal amounts payable for the 108 series issued prior to July 1, 1995, could not be determined; however, their original issue amounts totaled \$253,648,700.

The Health, Educational and Housing Facility Board has issued at least thirty-six (36) bond issues since 1985, the original amount of which were \$540,340,000. The Board has no means of determining the outstanding amount of these bonds.

NOTE 15. LANDFILL CLOSURE AND POSTCLOSURE CARE COSTS

The Solid Waste/Sanitation Fund accounts for the operations of the City landfill, as well as the closure and postclosure care costs of closed landfills (Summit and 36th Street). State and federal regulations require the City to place a final cover on all landfills after closure, and the City must perform certain maintenance and monitoring functions for 30 years thereafter. The City recognizes landfill closure and postclosure care costs based on the amount of the landfill used during the year. The estimated liability for landfill closure and postclosure care costs of \$10,013,509 at June 30, 2006, is based on the use of 100 percent of the capacity of the Summit landfill, and 96 percent of the capacity of the City landfill. The estimated remaining life of the City landfill is 1.5 years. Changes in the estimated liability for landfill closure and postclosure care costs for the year ended June 30, 2006, are as follows:

Estimated liability, June 30, 2005	\$ 9,555,619
Expenses recognized	563,734
Costs incurred	<u>(105,844)</u>
Estimated liability, June 30, 2006	<u>\$10,013,509</u>

The City will recognize the remaining estimated costs of closure and postclosure care of \$210,349 as the remaining capacity is used. The estimated total current cost of the landfill closure and postclosure care of \$10,223,858 is based on the amount that would be paid if all equipment, facilities, and services required to close, monitor, and maintain the landfills were acquired at June 30, 2006. However, the actual cost of closure and postclosure care may be higher due to inflation, changes in technology, or changes in landfill laws and regulations. It is anticipated that future inflation costs will be financed in part from earnings on investments. The remaining portion of anticipated future inflation costs and additional costs that might arise from changes in postclosure requirements may need to be covered by charges to future landfill users, taxpayers, or both.

NOTE 16. RISK MANAGEMENT

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; medical benefits; unemployment compensation; injuries to employees; errors and omissions; and natural disasters. The City retains the risk of loss related to torts, certain retiree medical benefits, unemployment compensation, and injuries to employees. The General Fund accounts for all exposures, except for torts, which are accounted for in the Internal Service Fund. To minimize its losses, the City has established a limited risk management program. Premiums are paid by all funds and are available to pay claims, claim reserves, and administrative costs of the program. The premiums are used to reduce the amount of claims expenditures reported in the respective funds. As of June 30, 2006, such interfund premiums did not exceed reimbursable expenditures. There were no significant reductions in insurance coverage in the prior year, nor did the amount of settlements exceed insurance coverage for each of the past three fiscal years.

City employees eligible for medical benefits are fully insured by Cigna Healthcare.

Liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported (IBNRs). The liability does not include nonincremental claims adjustment expenses. Claim liabilities are calculated considering the effect of inflation, recent claim settlement trends including frequency and amount of pay-outs and other economic and social factors. The liabilities for claims other than tort claims are reported in governmental funds rather than the general long-term debt account group because they are expected to be liquidated with expendable available financial resources.

Interfund premiums in the Internal Service Fund are based on the insured funds' claims experience. Premiums are adjusted to cover all reported claims. It is anticipated that the settlement of an individual claim will be funded by premiums subsequent to the filing of the claim and prior to its settlement. Changes in the balances of claims liabilities during the year are as follows:

	General Fund	Internal Service Fund
Unpaid claims, June 30, 2004	\$ 517,442	\$ 2,674,000
Incurred claims (including IBNRs)	23,092,250	2,634,175
Claim payments	<u>(22,848,294)</u>	<u>(644,175)</u>
Unpaid claims, June 30, 2005	761,398	4,664,000
Incurred claims, including IBNRs/reduction in estimated liabilities	22,413,786	40,764
Claim payments	<u>(22,706,586)</u>	<u>(1,114,764)</u>
Unpaid claims, June 30, 2006	<u>\$ 468,598</u>	<u>\$ 3,590,000</u>

NOTE 17. COMPONENT UNIT SWAPTION

In March 2004 the Chattanooga Downtown Redevelopment Corporation (CDRC), a component unit of the City, sold by competitive bid a floating-to-fixed interest rate swaption. Information related to the swaption is as follows:

Objective:

CDRC entered into a swaption contract that provided CDRC an up-front payment of \$3,088,000. As a synthetic refunding of its 2000 bonds, this payment represents the risk-adjusted, present-value savings of a refunding in October 2010 without issuing refunding bonds currently. The swaption gave the counterparty the option to require CDRC to enter into a pay-fixed, receive variable interest rate swap. If the option is exercised, CDRC would expect to issue refunding bonds at that date.

Terms:

The swaption was entered into in March 2004. The \$3,088,000 payment was based on a notional amount of \$59,655,000. The counterparty has the option to exercise the agreement on October 1, 2010. If exercised, the interest rate swap will also commence October 1, 2010. The fixed rate swap (5.45%) was set at a rate that, when added to an assumption for remarketing and liquidity costs, will approximate the coupons of the "refunded" bonds. The swap's variable payment would be based on The Bond Market Association Municipal Swap Index (BMA).

Fair value:

At June 30, 2006, the swap had a negative fair value of \$3,743,275, estimated using the zero-coupon method. This method calculates the future payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon rate bonds due on the date of each future net settlement on the swap.

Market-access risk:

If the option is exercised and refunding bonds are not issued, CDRC would be obligated to make net swap payments as required by the terms of the contract. If the option is exercised and variable-rate bonds are issued, the actual savings ultimately recognized by the transaction will be affected by the relationship between the interest rate terms of the to-be-issued variable-rate bonds versus the variable payment on the swap.