

**MUNICIPALITY OF SALEM
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2010**

This section of Salem City's annual financial report presents our discussion and analysis of the City's financial performance during the fiscal year ended on December 31, 2010. Please read it in conjunction with the City's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

- During the year, the City's revenues generated from charges for services, taxes and other revenues of the governmental programs were \$221,656 more than the \$700,506 governmental expenditures. This is a 25.96% decrease over the prior year when revenues exceeded expenditures by 299,383.
- In the City's business-type activities, revenues increased 8% to \$482,719 (this does not include the capital grant dollars received for the Water Treatment Plant) and expenses increased .32%.
- The total cost of the City's Governmental programs was \$116,037; 19.85% higher than 2009. There were many variables for this increase and are explained in detail on page 7 of this report.
- The revenues for the governmental activities show an increase of 4.3% or \$38,310. The increase in revenue is mainly from an increase in Taxes, Operating & Capital Gants, and Contributions. The result of the increase of revenues & expenditures is an increase to Net Assets of \$221,656 in 2010.

OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of three parts – management's discussion and analysis (this section), the basic financial statements, including related notes, and required supplementary information. The basic financial statements include two kinds of statements that present different views of the City:

- The first two statements are government-wide financial statements that provide both long-term and short-term information about the City's overall financial status.
- The remaining statements are fund financial statements that focus on individual parts of the City government, reporting the City's operations in more detail than the government-wide statements.
 1. The governmental funds statements tell how general government services like public safety were financed in the short-term as well as what remains for future spending.
 2. Proprietary fund statements offer short- and long-term financial information about the activities that the City operates like businesses. The City has two proprietary funds – the Water Fund and the Sewer Fund.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of required supplementary information that further explains and supports the information in the financial statements.

Figure A-1 summarizes the major features of the City's financial statements, including the portion of the City government they cover and the types of information they contain. The remainder of the overview section of the management's discussion and analysis explains the structure and contents of each of the statements.

**Figure A-1
Mayor Features of City of Salem's Government-wide and Fund Financial Statements**

	Government-Wide Statements	Fund Statements	
		Governmental Funds	Proprietary Funds
Scope	Entire City government	The activities of the City that are not proprietary or fiduciary, such as finance office, police, streets, park	Activities the City operates similar to private businesses, the water and sewer systems.
Required Financial Statements	*Statement of Net Assets * Statement of Activities	*Balance Sheet *Statement of Revenues, Expenditures and Changes in Fund Balances	* Balance Sheet *Statement of Revenues, Expenditures and Changes in Net Assets * Statement of Cash Flows
Type of Asset/Liability Information	Accrual accounting and economic resources focus	Modified accrual accounting and current financial resources focus	Accrual accounting and economic resources focus
Type of Asset/Liability Information	All assets and liabilities, both financial and capital, and short-term and long-term	Only assets expected to be used up and liabilities that come due during the year or soon thereafter no capital assets included.	All assets and liabilities, both financial and capital, and short-term and long-term
Type of Inflow/Outflow Information	All revenues and expenses during year, regardless of when cash is received or paid.	Revenues for which cash is received during or soon after the end of the year; expenditures when goods or services have been received and payment is due during or soon thereafter	All revenues and expenses during year, regardless of when cash is received or paid.

Government-wide Statements

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

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

- Increases or decreases in the City’s net assets are an indicator of whether its financial health is improving or deteriorating, respectively.
- To assess the overall health of the City you need to consider additional non-financial factors such as changes in the City’s property tax base and changes in the sales tax revenue base.

The government-wide financial statements of the City are reported in three categories:

- Governmental Activities -- This category includes most of the City’s basic services, such as police, fire, public works, parks department and general administration. Property taxes, sales taxes, charges for services, state and federal grants and interest earnings finance most of these activities.

- Business-type Activities -- The City charges a fee to customers to help cover the costs of certain services it provides. The City's water and sewer systems are included here.
- Component Units -- The City includes one other entity in its report – the Housing and Redevelopment Commission. Although legally separate, this “component unit” is important because the City is financially accountable for them.

Fund Financial Statements

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

- State Law requires some of the funds.
- The City Council establishes other funds to control and manage money for particular purposes or to show that it is properly using certain taxes and grants.

The City has two kinds of funds:

- Governmental Funds – Most of the City's basic services are included in the governmental funds, which focus on (1) cash and other financial assets that can readily be converted to cash flow in and out and (2) the balances left at the year-end that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that helps you determine 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 encompass the additional long-term focus of the government-wide statements, we provide additional information on the subsequent page that explains the relationship (or differences) between them.
- 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 short- and long-term financial information. The City's enterprise funds (one type of proprietary fund) are the same as its business-type activities, but provide more detail and additional information, such as cash flows.

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

Net Assets

The City's combined net assets increased by 6.7% between fiscal year 2009 and 2010; a \$618,014 increase (See Table A-1).

TABLE A-1 CITY OF SALEM NET ASSETS - FISCAL YEAR 2010

	Governmental			Business-Type			Total		
	Activities			Activities					
	2008	2009	2010	2008	2009	2010	2008	2009	2010
Current and Other Assets	840,832	1,177,805	1,016,400	926,460	569,001	602,858	1,767,292	1,746,806	1,619,257
Capital Assets	1,379,632	1,360,283	1,755,052	3,211,823	4,201,724	4,171,672	4,591,454	5,562,007	5,926,724
Total Assets	2,220,464	2,538,089	2,771,452	4,138,282	4,770,724	4,774,530	6,358,746	7,308,813	7,545,981
Long-Term Debt Outstanding	7,699	8,151	11,710	1,736,805	2,452,804	2,361,458	1,744,504	2,460,955	2,373,168
Deferred Revenue (salestax)	29,550	30,900	33,700				29,550	30,900	33,700
Other Liabilities	18,649	35,089	40,437	518,439	46,743	45,536	537,088	81,832	85,973
Total Liabilities	55,898	74,140	85,847	2,255,244	2,499,547	2,406,994	2,311,142	2,573,687	2,492,841
Net Assets:									
Invested in Capital Assets									
Net of Related Debt	1,379,632	1,360,283	1,755,052	1,480,113	1,754,608	1,814,424	2,859,744	3,114,891	3,569,476
Restricted	347,118	142,505	187,933	117,907	145,323	154,597	465,024	287,828	342,529
Unrestricted	437,816	961,161	742,620	285,019	371,246	398,516	722,835	1,332,407	1,141,135
Total Net Assets	2,164,565	2,463,949	2,685,605	1,883,039	2,271,178	2,367,536	4,047,604	4,735,126	5,053,141
Beginning Net Assets	1,876,266	2,164,565	2,463,949	1,175,370	1,883,039	2,271,178	3,051,636	4,047,604	4,735,126
Increase (Decrease) in									
Net Assets	288,300	299,383	221,656	707,669	388,139	96,358	995,968	687,522	318,014
Percentage of Increase									
(Decrease) in Net Assets	15.4%	13.8%	9.0%	60.2%	20.6%	4.2%	32.6%	17.0%	6.7%

This section explains the differences between the current and prior year's assets, liabilities, and changes in net assets.

The city as a whole reports an increase in net assets of 6.7%. The Current Assets (cash & receivables) decreased by 7.3% (\$127,549) as a result of the local cash spent on Capital Improvements and the extensive street repairs. The Capital Assets increased 6.6% (\$364,717) - from the Hill, Pierce & Lightner Street Project, addition of Equipment in the Street & Water Departments, and installation of a block of water main and five blocks of storm sewer. The Total Assets increased 3.24%. Liabilities for the city decreased 3.14%. The increase to Other Liabilities is from an increase in claims payables at the end of the year.

There are three categories of Net Assets reported in Table A-1. Invested in Capital Assets Net of Related Debt, Net Assets Restricted and Net Assets Unrestricted.

- The Capital Assets Net of Related Debt increased \$454,585 or 14.6% from the addition of the Capital Assets listed above and no additional debt incurred in 2010.
- The Restricted Net Assets increased 19%. The dollars received for the Water Surcharge Fee; Storm Sewer Fee; the front footage Street Assessment; and the dollars set aside for future street projects consist of the Restricted Net Assets; and only a portion of the Storm Sewer Fee reserves was used to fund the 2010 Street Project.
- The Unrestricted Net Assets decreased 14.4% due to the increase in Net Assets from the aforementioned projects funded with local cash.

The Statement of Net Assets reports all financial and capital resources. The statement presents the assets and liabilities in order of relative liquidity. The liabilities with average maturities greater than one year are reported in two components – the amount due within one year and the amount due in more than one year. The long-term liabilities of the city, consisting of compensated absences payable and State Revolving Loans have been reported in this manner on the Statement of Net Assets. The difference between the city’s assets and liabilities is its net assets.

REVENUE COMPARISON, TABLE A-2; FIGURE A-2

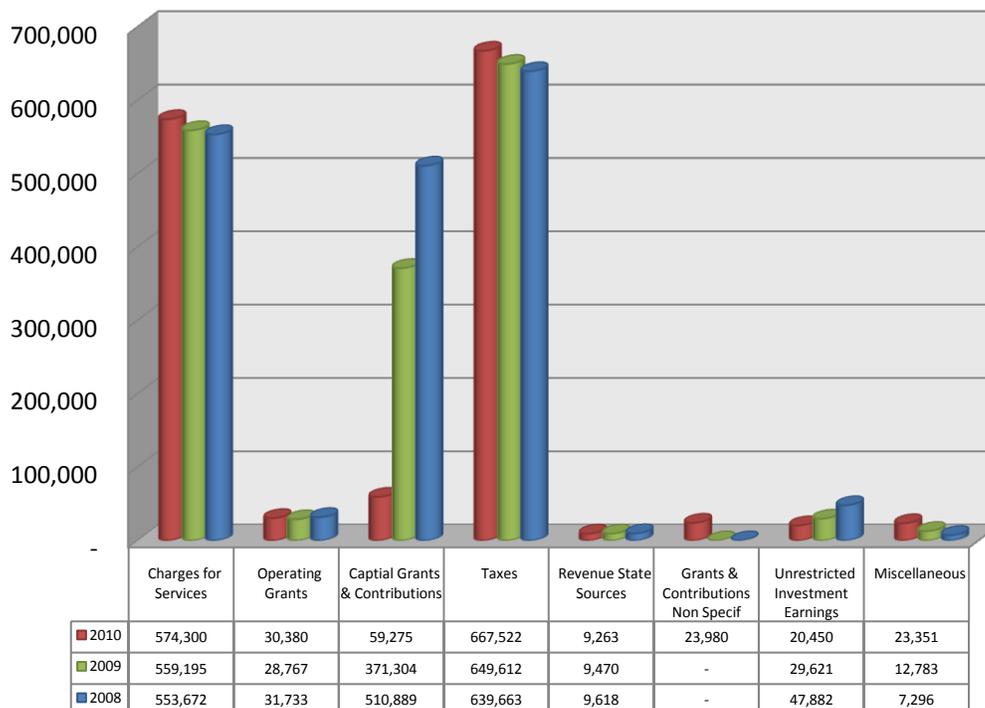
**TABLE A-2
MUNICIPALITY OF SALEM
Changes in Net Assets 12/31/2010**

	Governmental			Business-Type			Total		
	Activities			Activities					
	2008	2009	2010	2008	2009	2010	2008	2009	2010
Revenues									
Program Revenues									
Charges for Services	110,880	131,031	129,031	442,792	428,164	445,270	553,672	559,195	574,300
Operating Grants	31,733	28,767	30,380				31,733	28,767	30,380
Capital Grants & Contributions	35,663	41,169	55,635	475,226	330,134	3,639	510,889	371,304	59,275
Taxes	639,663	649,612	667,522				639,663	649,612	667,522
Revenue State Sources	9,618	9,470	9,263				9,618	9,470	9,263
Grants & Contributions Non Specif						23,980	-	-	23,980
Unrestricted Investment Earnings	20,966	16,519	12,980	26,916	13,102	7,469	47,882	29,621	20,450
Miscellaneous	7,296	7,283	17,351		5,500	6,000	7,296	12,783	23,351
Total Revenues	855,818	883,852	922,162	944,934	776,900	486,358	1,800,753	1,660,753	1,408,521
Expenses									
General Government	129,239	125,481	147,532				129,239	125,481	147,532
Public Safety	84,911	110,089	116,106				84,911	110,089	116,106
Public Works	158,120	165,661	248,820				158,120	165,661	248,820
Health & Welfare	3,443	6,256	4,377				3,443	6,256	4,377
Culture & Recreation	174,825	174,044	178,045				174,825	174,044	178,045
Conservation & Development	-	-	5,626				-	-	5,626
Miscellaneous Expenditures	-	2,939	(0)				-	2,939	(0)
Debt Service	-	-	-				-	-	-
Water Services				160,404	289,839	291,010	160,404	289,839	291,010
Sewer Services				93,862	98,922	98,990	93,862	98,922	98,990
Total Expenses	550,539	584,469	700,506	254,266	388,761	390,000	804,804	973,230	1,090,506
Excess (Deficiency) Before									
Special and Transfers	305,280	299,383	221,656	690,669	388,139	96,358	995,948	687,523	318,014
Special Items	-	-	-	-	-	-	-	-	-
Transfers	(17,000)	-	-	17,000	-	-	-	-	-
Increase (Decrease) in Net Assets	288,280	299,383	221,656	707,669	388,139	96,358	995,948	687,523	318,014
Ending Net Assets	2,164,565	2,463,949	2,685,605	1,883,039	2,271,178	2,367,536	4,047,604	4,735,127	5,053,141

The City's total 2010 revenues were \$1,408,521 which is a decrease of 15.2% (\$252,232) from 2009.

- Charges for Goods and Services increased 2.7% (Business Type activities increased 4% and the Governmental Activities decreased 1.5%). The user fees in the Water & Sewer funds increased as a result of a water rate increase and an increase of 6% in gallons billed; the General Fund's decreased from a reduction in participants in the summer recreation programs.
- Operating grants increased 5.6% from an increase in dollars received for Motor Vehicle Licenses and a \$660.00 grant received from the Dept of Agriculture for the planting of trees.
- Capital Grants & Contributions decreased by 84%. Governmental Activities saw a \$14,566 (35%) increase from the street assessments for the 2010 Street Project; and the Business Type Activities saw a \$326,495 decrease because less grant dollars were received in 2010 for the Water Filtration Project.
- Taxes increased by \$17,910 this reflects an increase in sales tax & property tax revenue. The sales tax revenue increased 2.28% and the property taxes increased 3.7%.
- Revenue from State Sources saw a 2.2% decrease (\$207) - these dollars are from Liquor Tax Reversion and Bank Franchise taxes.
- Grants & Contributions Non Specific - is a new line on the chart in 2010 and is a one-time payment made to the Water Department from Verizon Wireless of \$23,980 for the extra cost of painting the Water Tower in 2009.
- Investment earnings show a 31% decrease in revenue. The interest rates and cash balances both declined 2010.
- Miscellaneous revenues increased 82.7% (\$10,568). The City sold land on the South end of Main Street and 12 months of rent was received in the Water Department from Verizon Wireless (2009 was 11 months).

Figure A-2, City of Salem Revenue Comparison 2008-2010

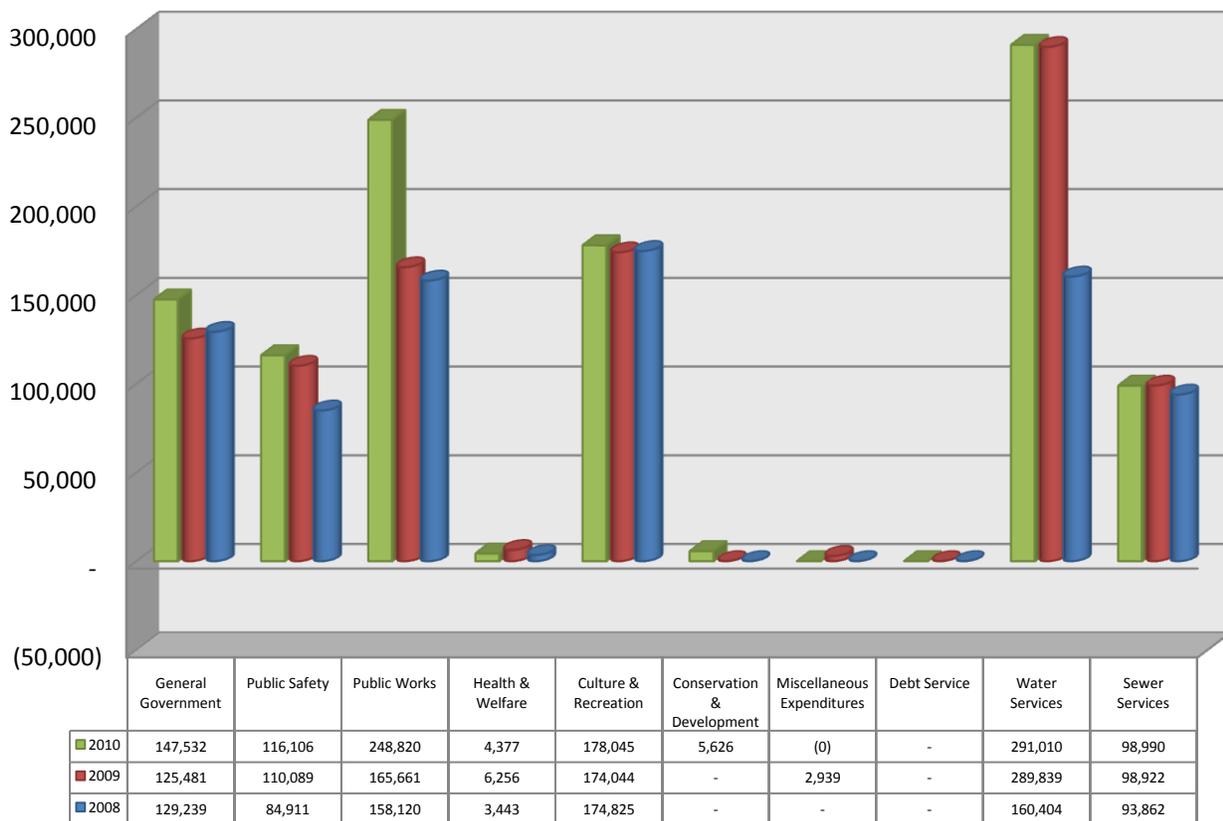


EXPENDITURE COMPARISON, TABLE A-2 & FIGURE A-3

The city's expenses show an overall 12% increase (2010 vs. 2009).

- General Government Expenditures increased 17.6% (\$22,051) from the increased number of nuisance mowing in 2010 and the moving of 20% the finance officer's salary from the Water Dept to the Finance Office Dept.
- Public Safety expenses increased 5.5% which is from a \$23,000 donation to the Rural Fire Association.
- Public Works expenses increased 50% as a result of the \$60,000 spent on street repairs, the purchase of 1800T of gravel, and an increase in snow removal expenditures.
- Health & Welfare expenses decrease 30% (\$1,879) due to a decrease in mosquito control chemicals purchased – a grant was received from the Dept of Health in the form of chemicals in 2010.
- Culture & Recreation expenses decreased 2.3% (\$4,001). Summer Recreation costs decreased 40% from a decrease in the number of coaches hired and supplies purchased; pool costs decreased 13.3% from a the decrease in wages and chemicals purchased; park expenditures decreased 15.45% mainly from a decrease in wages; and the armory expenses increased 36.6% - wages increased and all the lighting in the armory was upgraded for energy efficiency.
- Conservation & Development is a new category, the Zoning, Promoting and Advertising of Salem moved from General Governmental expenditures.
- Miscellaneous Expense is zero in 2010. In 2009, the City incurred expenses in the buy-back of inventory from the operators of the Salem Bar and the closing of another business operating under a city liquor license.
- Water Fund Expenditures increased .4% (\$1,171). Costs stabilized quite a bit from 2008 to 2009, but the finance officer's wages were removed from the Water Fund. The filtration plant still requires quite a few extra hours for CIP's to the system which results in higher chemical & utility costs.
- Sewer Fund Expenditures increased .07% (\$68).

Figure A-3, City of Salem, Functional Expenses, Fiscal Year 2008-2010



SOURCE OF REVENUE (Figure A-4, A-5 and A-6)

Eighty-eight percent (88%) of the City’s revenue comes from charges for goods and services and taxes, with 47 cents of every dollar coming from charges for services (primarily water and sewer operations) and 41 cents of every dollar raised comes from some type of tax. (See Figure A-4). Another 8% came from state and federal grants for operating & capital purposes and the remaining revenue comes from state-shared revenues and interest earnings. This varied from 2009 as there was an increase in charges for goods and service and taxes; but less grant dollars received for the Water Filtration Project.

Figure A-4, City of Salem Sources of Revenue for Fiscal Year 2010

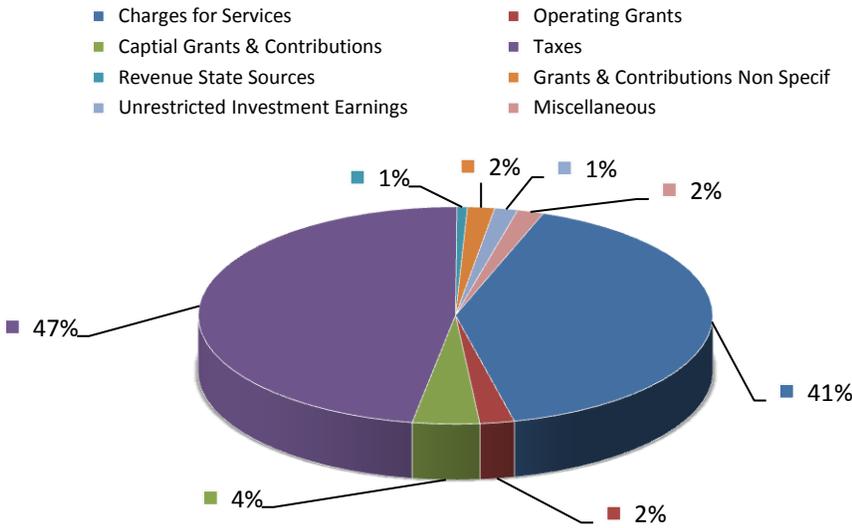


Figure A-5 City of Salem, Sources of Revenue for Fiscal Year 2009

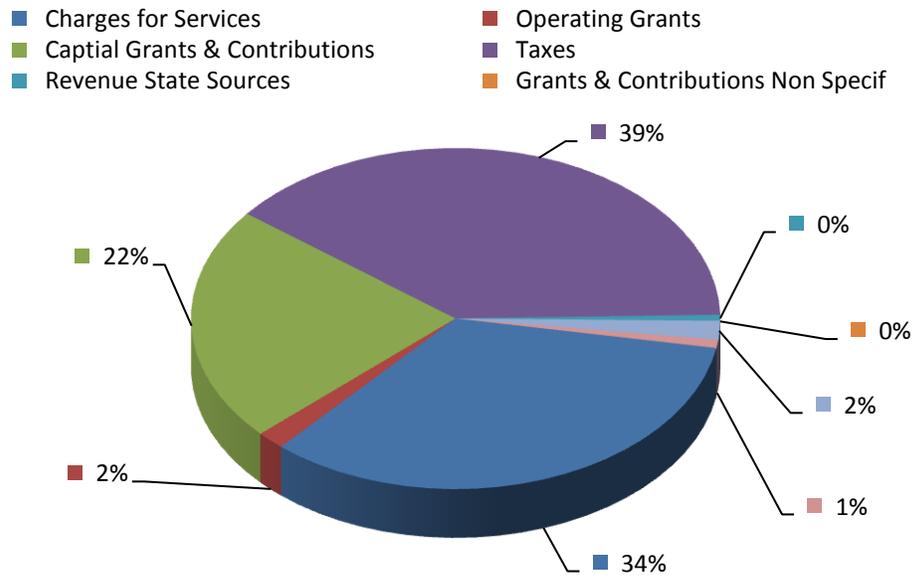
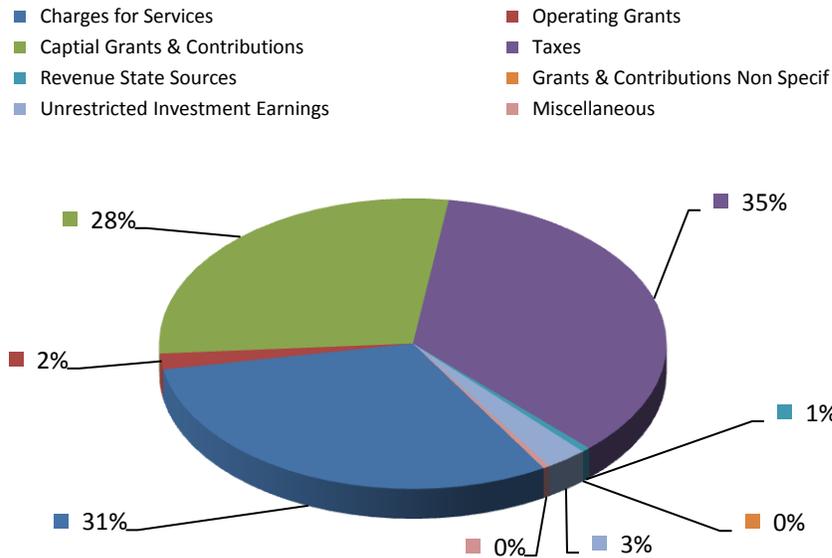


Figure A-6, City of Salem, Sources of Revenue for Fiscal Year 2008



FUNCTIONAL EXPENSES - FIGURE A-7, A-8 and A-9

The City's expenses cover a range of services with 59% related to public works services (road maintenance – chip seal – street sweeping – snow plowing; water & sewer system services). Culture and Recreation (Summer Recreation, Pool, Parks and Armory) make up 16%; General Government (Publications, Council, Attorney, Insurance, Finance Office & City Hall/Bar Buildings) accounted for 14%; Public Safety (Police, Civil Defense, and Fire Department) accounted for 11% and Debt Service, Conservation & Development, Health & Welfare, and Miscellaneous expenditures each accounted for less than 1% of expenditures. The expenditures service percentages varied slightly from 2009 – mainly from the shift in wages between departments.

Figure A-7, City of Salem, Functional Expenses for Fiscal Year 2010

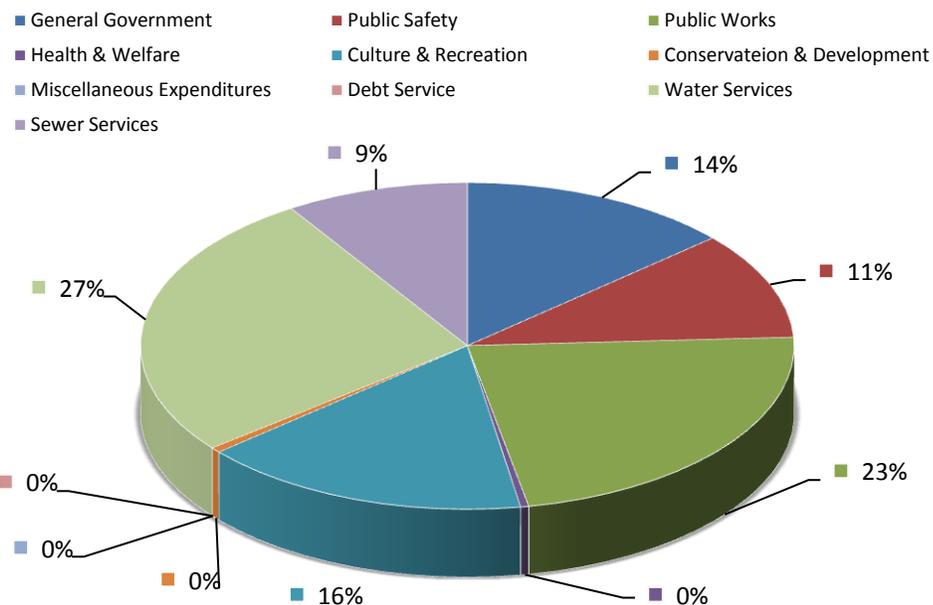


Figure A-8, City of Salem, Functional Expenses for Fiscal Year 2009

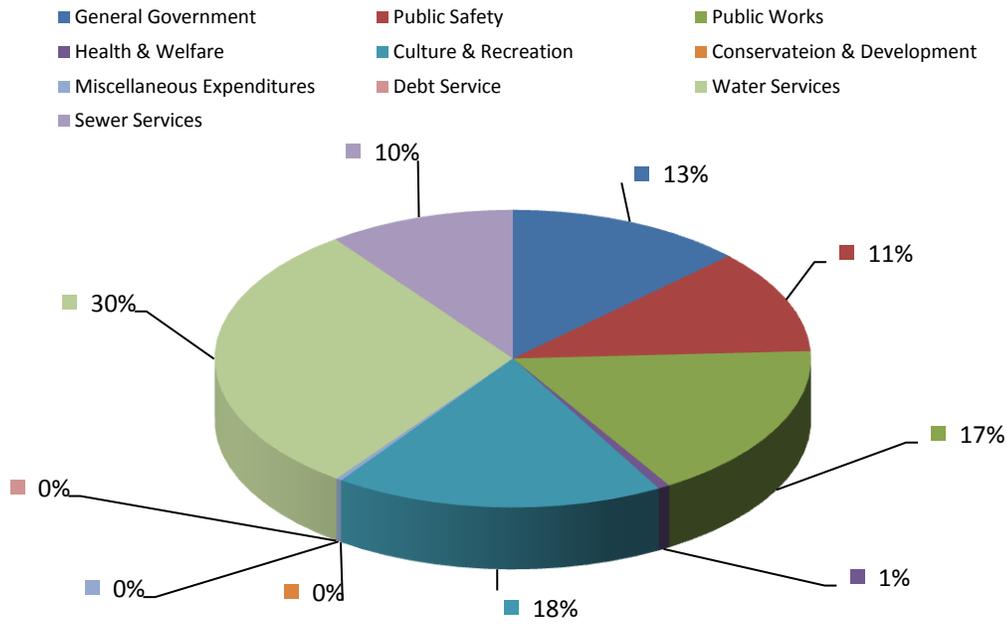
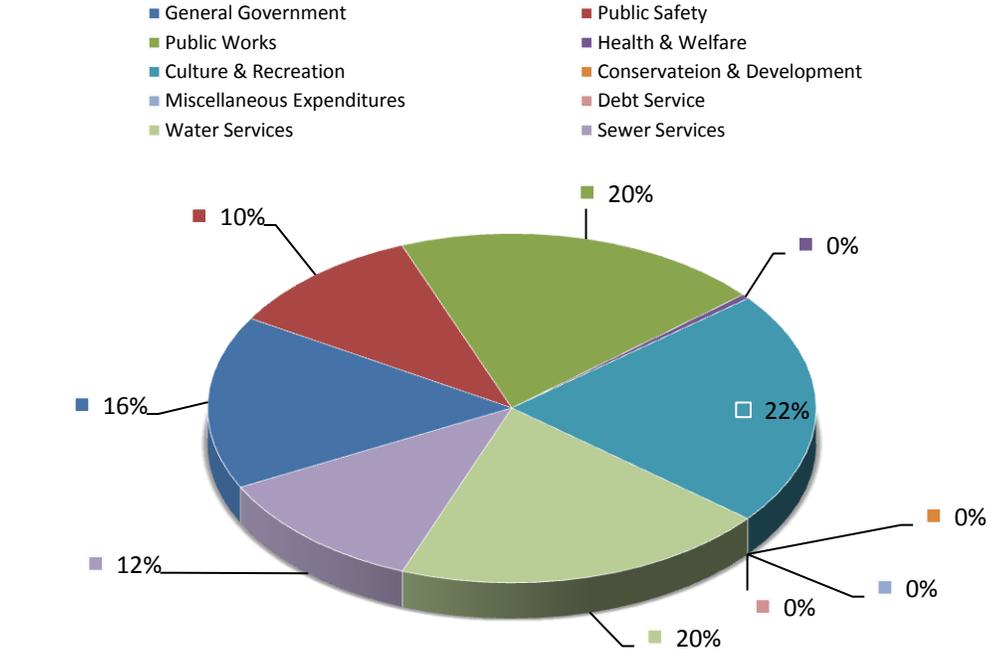


Figure A-9, City of Salem, Functional Expenses for Fiscal Year 2008



Governmental Activities

Revenues of the City's Governmental activities increased by 4.3%; both property tax & sales tax saw an increase; the Operating Grants, and Capital Grants & Contributions increased 23% - due to the street project assessments received in 2010; Investment Earnings decreased 21.4%; and the Miscellaneous Revenue showed an increase due to the sale of land on the south end of Main Street. The Governmental expenditures increased 19.9%. General Government increased 17.8% as a result of 80% of Finance Officers wages being charged to Governmental expenses (in prior years 60% was charged); the nuisance mowing costs were high in 2010. Public Safety costs increased due to a donation to the Rural Fire Association. The Public Works costs increased by 50% as a consequence of spending \$60,000 on street repairs, the purchasing of 1800 ton of gravel, and increased snow removal costs. Health & Welfare decreased because less money was spent on Mosquito Control chemicals.

Business-type Activities

Operating revenues of the City's business-type activities increased 8% as a result of the \$1.50 increase to the water flat fee; the expenditures increased by \$1,239 (.32%); and net assets increased 4.24%.

- The Water Rates were adjusted in 2010 to accommodate the higher costs of running the Water Treatment Plant. The revenues generated from Charges for Services increased 4%; Investment earnings decreased; the water department received a one-time payment (\$23,980) from Verizon Wireless for the increased cost incurred to paint the water tower. The sewer department saw a 1% increase in revenues from user fees. The increase in the Charges for Services revenue in both the water and sewer departments are attributed to Buhler Mfg's startup and use of water and the occupancy of some of the empty houses and apartments in Salem during 2008 and 2009.
- The increase in expenses was mainly from the Water Department. The Water Department's new Water Filtration Plant still required additional hours for C.I.P.'s (clean in place) of the Ultra Filtration system. The plant specs called for one cleaning a month and currently the filters are being cleaned every 10 to 13 days; which attributes to higher wage, chemical and pumping costs. The Sewer Department saw a slight increase in expenses due to the replacement of a furnace at the main lift station and repairs to the south lift station. The time put into the operation of the new water treatment plant was hoped to decrease in 2010, but unfortunately this will continue to be an issue until the number of CIP's are reduced.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

The financial analysis of the City's funds mirror those highlighted in the analysis of governmental and business-type activities presented above. The City maintained five governmental funds - General, Sales Tax, Street Assessment, Storm Sewer and a Capital Projects Funds and only two business type funds - Water and Sewer Funds. Each fund saw an increase in Net Assets; although lower than the two prior years, as a consequence of local cash used for the 2010 projects compared to grants and loans received in prior years.

General Fund Budgetary Highlights

Over the course of the year, the City Council revised the City's budget four times. These amendments fall into three categories:

- Supplemental appropriations and contingency transfers approved for unanticipated, yet necessary, expenses to provide for items necessary for the health and welfare of its citizens.
- Increases in appropriations, primarily by contingency transfer, to prevent budget overruns.

There were four budget changes during the year. The budget was increased due to the purchase of a Snow Blower & Sander in the Street Department; Budgeting for the Street Project (Hill, Pierce & Lightner); storm sewer repairs; tree planting at the park and city hall (funded partially by a grant); the budgeting of 80% instead of the original 60% of the Finance Officers wages in the Finance Dept budget; batteries for the Civil Defense siren; the Street Repair Project; the 1800T of gravel purchased, the Green/Douglas Storm Sewer Project; the Armory Lighting Project and the higher snow removal costs.

CAPITAL ASSET ADMINISTRATION

By the end of 2010, the City had invested \$5,926,724 in a broad range of capital assets, including, land, buildings, infrastructure, and various machinery and equipment. (See Table A-3.) This amount represents a net increase (including additions and deductions) of \$364,117 or 6.56% over FY2009.

TABLE A-3
CITY OF SALEM - CAPITAL ASSETS
(net of depreciation)

	Governmental			Business-type		
	Activities			Activities		
	2008	2009	2010	2008	2009	2010
Land	51,324	51,324	49,675	41,866	41,866	41,866
Buildings	191,014	182,461	173,908		1,272,633	1,246,661
Improvements Other Than Buildings	912,575	881,170	1,281,072	1,443,727	1,828,603	1,811,399
Machinery & Equipment	224,720	204,754	250,397	149,812	1,058,622	1,048,878
Construction In Progress	-	40,575	-	1,576,418	-	22,868
Total Capital Assets (Net)	<u>1,379,632</u>	<u>1,360,283</u>	<u>1,755,052</u>	<u>3,211,823</u>	<u>4,201,724</u>	<u>4,171,672</u>

This year's major capital asset additions included:

- The Governmental additions for 2010 were two street projects which include the rebuilding and matting of the following streets: Pierce Street from Drake to Lightner; Lightner from Hill to Brown; and Hill Street from Center to Hwy 38. Storm Sewer was added on Hill Street from Brown north to Center Ave and on Center Ave from Hill east to Pierce. Land saw a decrease due to the sale of Tract A-1 & A2 on the south end of Main Street. Equipment increased from the purchase of a new snow blower and sander. Buildings show a decrease due to depreciation.
- Business-type additions for 2010 saw a decrease to Buildings, Improvements Other Than Buildings and Equipment due to depreciation. The Construction in Progress dollars are from the on-going engineering fees from warranty issues in the Water Treatment plant (shop floor and the functioning of the water treatment plant). The Water Fund did purchase 80 new Radio Read meters; upgraded the handheld meter reader; replaced one block of 4" cast iron water main and two fire hydrants. The Sewer Dept refurbished five manholes.

The City's fiscal year 2011 capital budget projects include the following: The Water Department will be replacing a couple of fire hydrants due to age and a Hwy 81 State DOT project; the Sewer Department will be rehabilitating approximately four to five manholes; and the General Fund has budgeted for the purchase of a mower and hiring of a seasonal employee to mow the city property and the nuisance property; street projects will not be decided until after the first of the year. The Council will be looking at streets repairs but with the large project completed in 2010 the availability of funds may be an issue in 2011. The shop floor in the water treatment plant will be replaced at no cost to the City in the spring of 2011. WesTech Inc will be fixing the CIP problem in February or March of 2011.

In 2010, the General Fund used \$478,727.64 in local cash for all of the 2010 capital projects. They included a major street rebuild and paving project; Hill (Hwy 38 to Center), Pierce (Drake to Lightner) & Lightner (Hill to Brown); installation of storm sewer on two blocks of Hill Street (an extension of the southeast storm sewer system), two blocks of Center Ave and Green/Douglas Streets; and the purchase of a new snow blower and sander. The Water Department purchased 80 new radio read meters, upgraded the radio read handheld, installed one block of water main; two new hydrants; and Water Treatment Plant warranty issues with local cash amounting to \$72,906.59. The Sewer Dept refurbished five manholes at a cost of \$9,990.00.

The City had \$106,222.28 in the General Fund Capital Replacement Reserve Account at the end of 2010 – specifically for Main Street Lighting, baseball field fencing, a new Concession Stand/Restroom at the Softball field complex and Street projects. The 2011 Budget placed an additional \$227,000.00 into the Capital Reserve Account – specifically for Street Projects and new restrooms/concessions stand at the Softball field park. The City will continue to put block(s) of water main in as money is available.

LONG-TERM DEBT

At year-end, the City had \$2,357,248 in SRF Loans (Revenue Bonds), and \$15,920 in other long-term obligations. This is a decrease of 3.6% as shown on Table A-4 below. The City’s obligation for compensated absences increased (due to an increase in vacation leave available for years of service), and the SRF loan balances decreased \$89,867 (from payments made on said debt).

**TABLE A-4
CITY OF SALEM - Outstanding Debt and Obligations**

	Governmental			Business-type		
	Activities			Activities		
	2008	2009	2010	2008	2009	2010
Compensated Absences	7,699	8,151	11,710	5,095	5,688	4,210
Drinking Water SRF Loan 2003	-	-	-	73,152	61,459	49,352
Drinking Water SRF Loan 2005	-	-	-	310,991	298,514	285,626
Drinking Water SRF Loan 2008	-	-	-	555,831	1,331,625	1,304,217
Clean Water SRF Loan 2003	-	-	-	435,966	414,824	392,933
Clean Water SRF Loan 2005	-	-	-	355,770	340,694	325,121
Total Outstanding Debt Obligations	7,699	8,151	11,710	1,736,805	2,452,804	2,361,458

The City is liable for the accrued vacation leave payable to all full-time employees who have been employed for more than one year. The increase in 2010 on the governmental side is the result of an increase in accumulated vacation leave payable and the decrease on the Business Type side is from the decrease in hours carried over from FY2010.

The City has outstanding \$1,639,195 in Drinking Water SRF Loans and \$718,054 in Clean Water SRF Loans (Revenue Bonds). The bonds are secured and paid for from the Water and Sewer Funds. The City does not anticipate the use of any tax dollars to pay for these bonds.

- The 2003 bonds were used for the 2003 Street and Utility Project (This project extended water and sewer service on S. Main Street and on Brown Ave; and started the Storm Sewer System in Southeast Salem.) The 2003 DWSRF Loan will be fully paid off on July 15, 2014 and the 2003 CWSRF will be fully paid off on July 15, 2024.
- The 2005 bonds were used for the 2005 Street and Utility Project (This project replaced Water main on Nebraska and Essex Streets; extended storm sewer on George Ave and replaced storm sewer on Essex Ave.) The 2005 CW SRF Loan closed in 2006 and the DWSRF Loan closed in 2007. Both are 20 year loans – the CWSRF will be paid off in July 2026, and the DWSRF will be paid off in April 2027.
- The 2008 DWSRF Loan closed in 2009, this is a 30 year loan and will be paid off in 4/15/2039. The loan is specifically for the Water Filtration (Treatment) project, and a Water Surcharge was established to pay off the debt on this bond. Each household pays \$9.90 per month or 118.80 annually to retire the debt.

ECONOMIC FACTORS AND NEXT YEAR’S BUDGETS AND RATES

The City’s current economic position has leveled off from a slight decline in 2008. The City experienced growth of 1% in 2010 compared to 1.1% in 2009. The growth factor allows the City the ability to increase the amount of revenue generated from

property taxes, the increase for 2011 is \$2,660.00; in 2010 it was \$2,811. Under the state mandated property tax freeze, property taxes from one year to the next may increase 3% or an amount based on the Consumer Price Index (CPI) whichever is lower plus the growth factor. 2010 property tax levy requests payable in 2011 only increased 1% (Growth 1%; CPI 0%) or \$2,660.00; down from the 2009 property tax levy requests payable in 2010 which was 4.1% (CPI of 3% & Growth of 1.1%) or \$10,475.87.

One of the primary sources of revenue to the City is taxable retail sales in the community (sales tax). In studying the actual sales tax revenue (once revenue was received for the entire FY), the 2010 vs. 2008 taxable sales base increased 1.25%; the 2010 vs. 2009 taxable sales base increased 5.82%. The City's 2011 tax revenue budget did not increase. The City passed an Ordinance in 2007 implementing an additional 1% tax on gross receipts from the sale of leases or rentals of hotel, motel, campsites or other lodging accommodations; the sale of alcoholic beverages as defined in SDCL 35-1-1; establishments where the public is invited to eat, dine or purchase and carry out prepared food for immediate consumption; and ticket sales or admissions to places of amusement, athletic and cultural events within the municipality. The tax was not payable until January 2008 and was estimated to generate \$11,000.00 in revenue; this revenue can only be used for the purpose of land acquisition, architectural fees, construction costs, payment for civic center, auditoriums or athletic facility buildings, including the maintenance, staffing and operations of such facilities, and the promotion and advertising of the municipality, its facilities, attractions and activities. The actual dollars raised by this tax in 2010 was \$24,491.42 a 72.58% increase; in 2009 was 14,191.51 which was a 7.8% decrease from 2008's revenue of \$15,392.64; but still was 29.01% more than the estimated \$11,000.00. The 2010 increase is thought to be from audits performed by the Dept of Revenue; it appears that some businesses were not paying the tax. The City's 2011 budget did not include any use of these revenues, but will be discussed as a means of finance for projects. The revenues are in a "Special Revenue Fund" as designated by SDCL 10-45.

The City's adopted 2011 General Fund budget decreased 4.6% to \$831,850.00. The City's General Government Budget increased 12.98% as a result of 100% of the Finance Officer's salary put into the General Fund (in the past it was 60% General, 20% Water & 20% Sewer); there was decreases in the Public Safety due to a 2010 donation to the rural fire association; Capital Outlay decreased \$13,000 and Capital Replacement decreased \$25,670. The remaining departments varied slightly by reason of a shift in wages between departments. The budget was increased to accommodate an increase in wages for the city's employees (4% full-time & 2% part-time), but wages are not set until January.

The City's business-type activities (water and sewer operations) expect that the revenues for the 2011 financials will increase as a consequence of a \$3.00 Water flat fee rate increase. The flat fee was increased to meet debt obligations and to set money aside for filter replacement in the Water Treatment Plant and Water main replacement. It is the Councils understanding that the Water Treatment Plant C.I.P's will be reduced in 2011, as WesTech, the producer of the filtration system, will diligently work to rectify the issue by the end of March 2011; which in turn will decrease the employee wages in the Water Department along with pumping & chemical costs. The 2011 Water Budget decreased 1.7% (\$4610) from 2010 and the 2011 Sewer Budget decreased 7.9% as a result of the removal of 20% of the Finance Officer's wages.

The Council increased the Water Flat Fee \$3.00 but provided a reduced rate of \$9.50 to those living alone on social security with no other retirement income. Those residents qualifying were required to file an affidavit claiming they met the qualifications for the reduce rate with City Hall. The 2011 rates are a water flat fee of \$12.50, .004 cents per gallon used, plus a \$9.90 Water Surcharge fee. The Sewer Rates remained at a Residential flat fee of \$20.00, and 40% of the Water Usage Fee but not less than \$20.00 for commercial users. A CIP increase to the water rate was projected; but unfortunately, the cost to run the Water Treatment Plant, the need to replace 30 blocks of 4" CIP water main and filters in the Water Treatment Plant required a drastic increase. The City's local cost for building the Water Treatment Plant was \$104,500 more than originally projected; which resulted in a depletion of the Equipment Repair & Replacement reserves. At the end of 2010, the Equipment Repair & Replacement Fund had a balance of \$56,884, and to be able to replace water main, replace the Nano & Ultra Filters at their scheduled life expectancies, and to meet the 110% Debt obligation on the DWSRF loans; the \$3.00 increase was necessary. The Sewer Department rates were not increased. All rates are reviewed annually

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 demonstrate the City's accountability for the money it receives. If you have questions about this report or need additional information, contact the City of Salem's Finance Office, 400 N. Main, P.O. Box 249, Salem, SD 57058.