

City of Mary Esther, Florida

Financial Statements

Year Ended September 30, 2005

City of Mary Esther, Florida
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INDEPENDENT AUDITOR'S REPORT

The Honorable Mayor and Members of the City Council
City of Mary Esther, Florida

We have audited the accompanying financial statements of the governmental activities, the business-type activities, and each fund of the City of Mary Esther, Florida (hereinafter referred to as "City"), as of and for the year ended September 30, 2005, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *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 provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, and each fund of the City of Mary Esther, Florida as of September 30, 2005, and the respective changes in financial position and cash flows, where applicable, thereof 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 December 15, 2005, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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.

The management's discussion and analysis and budgetary comparison information on pages 3 through 9 and 41 through 42, 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 an opinion on the basic financial statements of the City of Mary Esther, Florida taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* and is not a required part of the basic financial statements of the City of Mary Esther, Florida. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

Carly Riggs & Ingram, L.L.C.

Destin, Florida
December 15, 2005

Management's Discussion and Analysis

MANAGEMENT'S DISCUSSION AND ANALYSIS

This discussion and analysis (MD&A) of the City of Mary Esther, Florida's (the "City") financial performance provides an overview of financial activity, identifies changes in financial position, and assists the reader in focusing on significant financial issues for the fiscal year ended September 30, 2005. The MD&A provides summary level financial information; therefore, it should be read in conjunction with the accompanying financial statements.

HIGHLIGHTS

Financial Highlights

- Total assets decreased \$180,000.
- Net assets decreased by \$93,000.
- Total revenues increased by 27% or \$997,000 and total expenses increased by 24% or \$928,000.

USING THE ANNUAL REPORT

This annual report consists of a series of financial statements, prepared in accordance with the Governmental Accounting Standards Board Statement 34, *Basic Financial Statements – and Management's Discussion and Analysis - for State and Local Governments*, as amended by Statement 37. The Statement of Net Assets and the Statement of Activities (on pages 10 and 11-12) provide information about the activities of the City as a whole and present a longer-term view of the City's finances. Fund financial statements start on page 13. For governmental activities, these statements tell how these services were financed in the short term as well as what remains for future spending. Fund financial statements also report the City's operations in more detail than the government-wide statements by providing information about the City's funds. The remaining statements provided financial information about activities for which the City acts solely as a trustee or agent for the benefit of those outside of the government.

Reporting the City as a Whole

The Statement of Net Assets and the Statement of Activities

Our analysis of the City as a whole begins on page 5. One of the most important questions asked about the City's finances is, "Is the City as a whole better off or worse off as a result of the year's activities?" The Statement of Net Assets and the Statement of Activities report information about the City as a whole and about its activities in a way that helps answer that question. These statements include *all* assets and liabilities using the *accrual basis of accounting*, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the City's *net assets* and changes in them. You can think of the City's net assets - the difference between assets and liabilities – as one way to measure the City's financial health, or *financial position*. Over time, *increases or decreases* in the City's net assets are one indicator of whether its *financial health* is improving or deteriorating. You will need to consider other nonfinancial factors, however, such as changes in the City's property tax base and the condition of the City's roads, to assess the *overall health* of the City.

In the Statement of Net Assets and the Statement of Activities, we divide the City into two kinds of activities:

- *Governmental activities* – Most of the City's basic services are reported here, including the police, fire, public works, library, and parks departments, and general administration. Property taxes, franchise fees, state revenue sharing, and state and federal grants finance most of these activities.
- *Business-type activities* – The City charges a fee to customers to help cover all or most of the cost of water and sewer services it provides.

Reporting the City's Funds

Fund Financial Statements

Our analysis of the City's funds begins on page 7. The fund financial statements begin on page 13 and provide detailed information about the most significant funds – not the City as a whole. Some funds are required to be established by State law and by bond covenants. However, the City Council establishes many other funds to help it control and manage money for particular purposes or to show that it is meeting legal responsibilities for using certain taxes, grants, and other money. The City's two kinds of funds – governmental and proprietary – use different accounting approaches.

- *Governmental funds* – Most of the City's basic services are reported in governmental funds, which focus on how money flows into and out of those funds and the balances left at year-end that are available for spending. These funds are reported using an accounting method called *modified accrual accounting*, which measures cash and all other *financial assets* that can readily be converted to cash. The governmental fund statements provide a detailed *short-term view* of the City's general government operations and the basic services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs. We describe the relationship (or differences) between governmental *activities* (reported in the Statement of Net Assets and the Statement of Activities) and governmental *funds* in a reconciliation at the bottom of the fund financial statements.
- *Proprietary funds* – When the City charges customers for the services it provides – whether to outside customers or to other units of the City – these services are generally reported in proprietary funds. Proprietary funds are reported in the same way that all activities are reported in the Statement of Net Assets and the Statement of Activities. In fact, the City's proprietary fund is the same as the business-type activities we report in the government-wide statements but provide more detail and additional information, such as cash flows, for proprietary funds.

The City as Trustee

Reporting the City's Fiduciary Responsibilities

The City is the trustee, or fiduciary, for its employees' pension plan. All of the City's fiduciary activities are reported in separate Statements of Fiduciary Net Assets and Changes in Fiduciary Net Assets on pages 21 and 22. We exclude these activities from the City's other financial statements because the City cannot use these assets to finance its operations. The City is responsible for ensuring that the assets reported in this fund are used for their intended purpose.

THE CITY AS A WHOLE

The following table reflects the net assets (in thousands) of the City's governmental activities and business-type activities and is compared to the prior year.

| | Governmental Activities | | Business-type Activities | | Total Primary Government | |
|--|----------------------------|-----------------|-----------------------------|------------------|-----------------------------|------------------|
| | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 |
| Assets | | | | | | |
| Current and other assets | \$ 2,850 | \$ 2,726 | \$ 4,345 | \$ 4,348 | \$ 7,195 | \$ 7,074 |
| Capital assets, net | 5,433 | 5,492 | 6,086 | 6,328 | 11,519 | 11,820 |
| Total assets | <u>\$ 8,283</u> | <u>\$ 8,218</u> | <u>\$ 10,431</u> | <u>\$ 10,676</u> | <u>\$ 18,714</u> | <u>\$ 18,894</u> |
| Liabilities | | | | | | |
| Current liabilities | \$ 87 | \$ 28 | \$ 377 | \$ 360 | \$ 464 | \$ 388 |
| Other liabilities | 130 | 124 | 2,770 | 2,939 | 2,900 | 3,063 |
| Total liabilities | <u>217</u> | <u>152</u> | <u>3,147</u> | <u>3,299</u> | <u>3,364</u> | <u>3,451</u> |
| Net assets | | | | | | |
| Invested in capital assets, net of debt | 5,433 | 5,492 | 3,136 | 3,478 | 8,569 | 8,970 |
| Unrestricted | 2,633 | 2,574 | 4,148 | 3,899 | 6,781 | 6,473 |
| Total net assets | <u>8,066</u> | <u>8,066</u> | <u>7,284</u> | <u>7,377</u> | <u>15,350</u> | <u>15,443</u> |
| Total liabilities and net assets | <u>\$ 8,283</u> | <u>\$ 8,218</u> | <u>\$ 10,431</u> | <u>\$ 10,676</u> | <u>\$ 18,714</u> | <u>\$ 18,894</u> |

For more detailed information, see the accompanying Statement of Net Assets.

Total assets decreased by \$180,000 during the fiscal year ended September 30, 2005. This decrease primarily was due to depreciation expense charged to capital assets. Total liabilities decreased by \$87,000 for the year primarily due to scheduled debt payments. The City's combined net assets decreased by \$93,000.

The following table reflects the changes in net assets (in thousands) of the City's governmental activities and business-type activities and compares the current and previous fiscal year.

| | Governmental Activities | | Business-type Activities | | Total Primary Government | |
|-----------------------------------|----------------------------|----------|-----------------------------|----------|-----------------------------|-----------|
| | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 |
| Program revenues | \$ 1,034 | \$ 344 | \$ 1,056 | \$ 971 | \$ 2,090 | \$ 1,315 |
| General revenues | 1,728 | 1,572 | 831 | 765 | 2,559 | 2,337 |
| Total revenues | 2,762 | 1,916 | 1,887 | 1,736 | 4,649 | 3,652 |
| Function/program expenses | 2,856 | 2,127 | 1,886 | 1,687 | 4,742 | 3,814 |
| Increase (decrease) in net assets | (94) | (211) | 1 | 49 | (93) | (162) |
| Transfers | 94 | 107 | (94) | (107) | - | - |
| Net assets beginning of year | 8,066 | 8,170 | 7,377 | 7,435 | 15,443 | 15,605 |
| Net assets end of year | \$ 8,066 | \$ 8,066 | \$ 7,284 | \$ 7,377 | \$ 15,350 | \$ 15,443 |

For more detailed information, see the accompanying Statements of Activities.

The City's total revenues increased by 27% or \$997,000 and total expenses increased by 24% or \$928,000. The overall results were a \$93,000 decrease in net assets for fiscal year 2005. Our analysis below separately considers the operations of governmental and business-type activities.

Governmental Activities

Revenues for the City's governmental activities increased by 44% or \$846,000, and expenses increased by 34% or \$729,000. The primary cause for the increases in revenues and expense was the federal and state grant funds and expenses for Hurricanes Ivan and Dennis. The City received \$571,760 and incurred expense of \$597,209. Additional factors that increased the revenue were increases in Ad Valorem tax of \$79,273, occupational licenses of \$45,026, intergovernmental funds of \$99,784 along with increases in court fines and interest income. The contributing causes for increased expense were engineering cost for the Library expansion and increased health care and personnel cost.

Business-type Activities

Revenues of the City's business – type activities show a slight increase from the previous fiscal year, increasing by 8.7% or \$85,000, while expenses increased 11.7% or \$199,000. The increase in expenses was due primarily to the City contracting out the management and operations of its' Wastewater Treatment Plant to a third party, the contract for 2005 increased by \$87,126 or 20%. Other factors that caused increased expense were some emergency repairs to the water and wastewater systems resulting in expenditures of \$124,000 more than budgeted. Also, the increase in energy and fuel cost were contributing factors. The increase in revenue is a result of a rate increase of 25% in the wastewater charges.

THE CITY'S FUNDS

As the City completed the year, its governmental funds (as presented in the balance sheet on page 13) reported a *combined* fund balance of \$2,763,000, which is slightly higher than last year's total of \$2,697,000. The increase in fund balance is the result of favorable investment results and interfund transfers totaling \$66,000.

General Fund Budgetary Highlights

Over the course of the year, the City revised the City budget by a little over \$641,000. The reason for these budget increases were to pay for hurricane expenses and the City received about 95% reimbursement from FEMA and the State. There were also two grants received after the budget was approved and the revenue and expense for these had to be included in the budget; one was for the Fire Department to purchase safety equipment and training material, the other was for the Library expansion.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

At September 30, 2005, the City had approximately \$11,519,000 invested in capital assets (net of depreciation). This amount represents a net decrease (including additions and deductions) of \$301,000 or 3% over the fiscal year 2005 total.

A listing of capital assets (in thousands) of governmental and business-type activities by major category, net of depreciation, for the current and prior year follows:

| | Governmental Activities | | Business-type Activities | | Total Primary Government | |
|----------------------------------|-------------------------|----------|--------------------------|----------|--------------------------|-----------|
| | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 |
| Land | \$ 4,363 | \$ 4,363 | \$ 78 | \$ 78 | \$ 4,441 | \$ 4,441 |
| Buildings | 442 | 456 | 58 | 61 | 500 | 517 |
| Improvements other than building | 178 | 206 | 5,767 | 6,192 | 5,945 | 6,398 |
| Machinery and equipment | 449 | 560 | 183 | 226 | 632 | 786 |
| Other | 1 | 1 | - | - | 1 | 1 |
| Totals | \$ 5,433 | \$ 5,586 | \$ 6,086 | \$ 6,557 | \$ 11,519 | \$ 12,143 |

The City's fiscal year 2006 capital budget calls for it to spend another \$219,000 for various projects including the Library expansion, improvements to the Maintenance complex and new sidewalks.

Debt

At September 30, 2005, the City had \$2,950,104 in bonds outstanding, net of unamortized discount and deferred refunding expenses, versus \$3,096,849 in the prior year, a decrease of \$146,745 as shown below:

| | 2005 | 2004 | Change |
|--|--------------|--------------|--------------|
| Water and sewer revenue bonds, Series 1996 | \$ 2,950,104 | \$ 3,096,849 | \$ (146,745) |

The last payment on the debt is due in fiscal year 2018. The maximum debt service in any one year on this debt is estimated to be \$356,113 in 2015. The minimum debt service is estimated to be \$331,931 in 2018. The City pledged as security for payment of the principal and interest on the Water and Sewer Revenue Bonds the net revenues (gross revenues less cost of operation and maintenance) derived from operation of the water and sewer system together with the proceeds derived from utility taxes collected on water, electricity, natural gas, and telecommunication services charged to customers within the City and from franchise fees collected from Gulf Power Company, Okaloosa County Gas District and various telephone companies.

For additional information on Debt, see Note 6 in the accompanying financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The City of Mary Esther was established as a town under Laws of the State of Florida in 1946. On June 5, 1984, after referendum vote by the citizens of Mary Esther, the Council approved ordinance number 84-3 to incorporate Mary Esther as a city. A five-person council governs the City. The City has taxing authority and receives funds from the State. Revenues are generated by charges to the City's customers for water and wastewater related services. Rates for fiscal year 2005 have been established to provide for the operations of the City and necessary capital requirements. Tax rates did not change for fiscal year 2006. Amounts available for appropriation in the General Fund budget are \$2,575,572, an increase of 26% over the 2005 budget of \$2,045,090. An increase in grant revenue is expected to lead this change. Total budgeted expenditures are expected to rise 31% to \$5,982,290 from \$4,380,650 in 2005. The Library grant for \$415,000 and Wastewater CDBG grant for \$645,000 account for a large portion of this increase as well as \$490,000 of capital improvements to the water and collection systems. The City has no major new programs or initiatives to the 2006 budget.

As for the City's business-type activities, we expect that the 2006 results will remain about the same as 2005 since there were no rate increases this year.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, and 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 the Finance Department at (850) 243-3566.

Basic Financial Statements

City of Mary Esther, Florida

Statement of Net Assets

September 30,

2005

| | Governmental Activities | Business-type Activities | Total |
|---|----------------------------|-----------------------------|----------------------|
| Assets | | | |
| Cash and cash equivalents | \$ 766,388 | \$ 150,439 | \$ 916,827 |
| Investments | 2,014,503 | 3,110,548 | 5,125,051 |
| Accounts receivable | 67,752 | 240,583 | 308,335 |
| Due from governmental activities | - | 36,617 | 36,617 |
| Other current assets | 1,409 | - | 1,409 |
| Restricted assets | - | 767,871 | 767,871 |
| Bond issue costs | - | 39,235 | 39,235 |
| Capital assets, net | 5,433,139 | 6,085,509 | 11,518,648 |
| Total assets | 8,283,191 | 10,430,802 | 18,713,993 |
| Liabilities | | | |
| Accounts payable | 12,472 | 72,877 | 85,349 |
| Due to other governments | - | 413 | 413 |
| Due to business-type activities | 36,617 | - | 36,617 |
| Accrued interest - restricted | - | 42,528 | 42,528 |
| Customer deposits - restricted | - | 80,840 | 80,840 |
| Accrued payroll | 7,952 | - | 7,952 |
| Deferred revenue | 29,745 | - | 29,745 |
| Noncurrent liabilities: | | | |
| Due within one year | - | 180,000 | 180,000 |
| Due in more than one year | 130,079 | 2,770,104 | 2,900,183 |
| Total liabilities | 216,865 | 3,146,762 | 3,363,627 |
| Net assets | | | |
| Invested in capital assets, net of related debt | 5,433,139 | 3,135,405 | 8,568,544 |
| Restricted for: | | | |
| Debt Service | - | 688,623 | 688,623 |
| Unrestricted | 2,633,187 | 3,460,012 | 6,093,199 |
| Total net assets | \$ 8,066,326 | \$ 7,284,040 | \$ 15,350,366 |

See accompanying notes to financial statements.

Statement of Activities

Year ended September 30,

2005

| Function/Program | Program Revenues | | | | Net (Expense) Revenue and Changes in Net Assets | | Total |
|--|------------------|-------------------------|---------------------------------------|-------------------------------------|--|-----------------------------|---------------|
| | Expenses | Charges for Services | Operating Grants and Contributions | Capital Grants and Contributions | Primary Government | | |
| | | | | | Governmental Activities | Business-type Activities | |
| Governmental activities: | | | | | | | |
| General government | \$ 444,723 | \$ 138,457 | \$ - | \$ - | \$ (306,266) | \$ - | \$ (306,266) |
| Public safety | 957,353 | 198,711 | - | - | (758,642) | - | (758,642) |
| Physical environment | - | 77,818 | - | - | 77,818 | - | 77,818 |
| Transportation | 338,534 | - | - | - | (338,534) | - | (338,534) |
| Human services | 13,846 | - | - | - | (13,846) | - | (13,846) |
| Culture and recreation | 438,339 | - | - | - | (438,339) | - | (438,339) |
| Hurricane expenses | 517,698 | - | 619,711 | - | 102,013 | - | 102,013 |
| Unallocated depreciation | 145,374 | - | - | - | (145,374) | - | (145,374) |
| Total governmental activities | 2,855,867 | 414,986 | 619,711 | - | (1,821,170) | - | (1,821,170) |
| Business-type activities: | | | | | | | |
| Water and sewer | 1,886,418 | 1,056,138 | - | - | - | (830,280) | (830,280) |
| Total primary government | \$ 4,742,285 | \$ 1,471,124 | \$ 619,711 | \$ - | (1,821,170) | (830,280) | (2,651,450) |
| General revenues | | | | | | | |
| Taxes: | | | | | | | |
| Property taxes, levied for operational purposes | | | | | 858,922 | - | 858,922 |
| Franchise fees | | | | | - | 203,970 | 203,970 |
| Utility service fees | | | | | - | 454,026 | 454,026 |
| Grants and contributions not restricted to specific programs | | | | | 732,456 | 5,000 | 737,456 |
| Investment earnings | | | | | - | 100,831 | 100,831 |
| Miscellaneous | | | | | 136,641 | 66,931 | 203,572 |
| Transfers | | | | | 93,759 | (93,759) | - |
| Total general revenues | | | | | 1,821,778 | 736,999 | 2,558,777 |
| Change in net assets | | | | | 608 | (93,281) | (92,673) |
| Net assets, October 1, 2004 | | | | | 8,065,718 | 7,377,321 | 15,443,039 |
| Net assets, September 30, 2005 | | | | | \$ 8,066,326 | \$ 7,284,040 | \$ 15,350,366 |

See accompanying notes to financial statements.

City of Mary Esther, Florida

Balance Sheet - Governmental Funds

September 30,

2005

| | General Fund | Federal Programs Fund | Other Governmental Funds | Total Governmental Funds |
|--|---------------------|-----------------------|--------------------------|--------------------------|
| Assets | | | | |
| Cash and cash equivalents | \$ 766,388 | \$ - | \$ - | \$ 766,388 |
| Investments | 1,916,974 | - | 97,529 | 2,014,503 |
| Interest receivable | 764 | - | - | 764 |
| Due from other funds | - | 29,745 | 274,743 | 304,488 |
| Due from other governments | 59,126 | - | - | 59,126 |
| Accounts receivable - other | 7,862 | - | - | 7,862 |
| Other current assets | 1,409 | - | - | 1,409 |
| Total assets | \$ 2,752,523 | \$ 29,745 | \$ 372,272 | \$ 3,154,540 |
| Liabilities and fund balances | | | | |
| Liabilities: | | | | |
| Accounts payable | \$ 12,472 | \$ - | \$ - | \$ 12,472 |
| Accrued payroll | 7,952 | - | - | 7,952 |
| Deferred revenue | - | 29,745 | - | 29,745 |
| Due to other funds | 341,105 | - | - | 341,105 |
| Total liabilities | 361,529 | 29,745 | - | 391,274 |
| Fund balances: | | | | |
| Unreserved, reported in: | | | | |
| General fund | 2,390,994 | - | - | 2,390,994 |
| Capital projects funds | - | - | 372,272 | 372,272 |
| Total fund balances | 2,390,994 | - | 372,272 | 2,763,266 |
| Total liabilities and fund balances | \$ 2,752,523 | \$ 29,745 | \$ 372,272 | \$ 3,154,540 |

See accompanying notes to financial statements.

City of Mary Esther, Florida

Reconciliation of the Balance Sheet to the Statement of Net Assets

| <u>September 30,</u> | <u>2005</u> |
|--|---------------------|
| Total fund balance - governmental funds | \$ 2,763,266 |
| Capital assets used in governmental activities are not financial resources and therefore are not reported in the governmental funds. | 5,433,139 |
| Compensated absences are not due and payable in the current period and therefore are not reported in the governmental funds | (130,079) |
| <u>Total net assets - governmental activities</u> | <u>\$ 8,066,326</u> |

See accompanying notes to financial statements.

City of Mary Esther, Florida

Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds

| | 2005 | | | |
|---|--------------|-----------------------|--------------------------|--------------------------|
| | General Fund | Federal Programs Fund | Other Governmental Funds | Total Governmental Funds |
| Revenues | | | | |
| Taxes | \$ 858,922 | \$ - | \$ - | \$ 858,922 |
| Licenses and permits | 198,711 | - | - | 198,711 |
| Intergovernmental | 732,456 | 619,711 | - | 1,352,167 |
| Charges for services | 138,457 | - | - | 138,457 |
| Fines and forfeitures | 77,818 | - | - | 77,818 |
| Miscellaneous | 132,675 | 3,966 | - | 136,641 |
| Total revenues | 2,139,039 | 623,677 | - | 2,762,716 |
| Expenditures | | | | |
| General government | 445,042 | - | - | 445,042 |
| Public safety | 954,267 | - | - | 954,267 |
| Transportation | 335,950 | - | - | 335,950 |
| Human services | 13,846 | - | - | 13,846 |
| Culture and recreation | 238,743 | - | 198,750 | 437,493 |
| Hurricane expenses | - | 517,698 | - | 517,698 |
| Capital outlay | 76,186 | - | 9,875 | 86,061 |
| Total expenditures | 2,064,034 | 517,698 | 208,625 | 2,790,357 |
| Excess (deficiency) of revenues over expenditures | 75,005 | 105,979 | (208,625) | (27,641) |
| Other financing sources (uses) | | | | |
| Transfers in | 199,738 | - | 274,743 | 474,481 |
| Transfers out | (274,743) | (105,979) | - | (380,722) |
| Total other financing sources and (uses) | (75,005) | (105,979) | 274,743 | 93,759 |
| Net change in fund balances | - | - | 66,118 | 66,118 |
| Fund balances, October 1, 2004 | 2,390,994 | - | 306,154 | 2,697,148 |
| Fund balances, September 30, 2005 | \$ 2,390,994 | \$ - | \$ 372,272 | \$ 2,763,266 |

See accompanying notes to financial statements.

City of Mary Esther, Florida

Reconciliation of the Statement of Revenues, Expenditures and Changes
in Fund Balances of Governmental Funds to the Statement of Activities

| <i>Year ended September 30,</i> | 2005 |
|---|-------------|
| Net change in fund balances - total governmental funds | \$ 66,118 |
| Capital outlay, reported as expenditures in governmental funds, is shown as capital assets in Statement of Net Assets. | 86,061 |
| Depreciation expense on governmental capital assets included in the governmental activities in the Statement of Activities. | (145,374) |
| Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. | (6,197) |
| Change in net assets of governmental activities | \$ 608 |

See accompanying notes to financial statements.

City of Mary Esther, Florida

Balance Sheet - Proprietary Funds

| September 30, | 2005 | Water and Sewer Fund |
|--|-----------|-------------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ | 150,439 |
| Investments | | 3,110,548 |
| Receivables | | 240,583 |
| Due from other funds | | 36,617 |
| Total current assets | | 3,538,187 |
| Restricted assets: | | |
| Cash | | 261,456 |
| Investments | | 506,415 |
| Total restricted assets | | 767,871 |
| Bond issue costs (net of accumulated amortization) | | |
| | | 39,235 |
| Fixed assets (net of accumulated depreciation) | | |
| | | 6,085,509 |
| Total assets | \$ | 10,430,802 |
| Liabilities and Net Assets | | |
| Liabilities | | |
| Current Liabilities: | | |
| Accounts payable | \$ | 72,877 |
| Due to other governments | | 413 |
| Current liabilities payable from restricted assets | | 303,368 |
| Total current liabilities | | 376,658 |
| Non-current liabilities: | | |
| Water & sewer revenue bonds, series 1996 | | 2,770,104 |
| Total liabilities | | 3,146,762 |
| NET ASSETS | | |
| Invested in capital assets, net of related debt | | 3,135,405 |
| Restricted for debt service | | 688,623 |
| Unrestricted | | 3,460,012 |
| Total net assets | | 7,284,040 |
| Total liabilities and net assets | \$ | 10,430,802 |

See accompanying notes to financial statements.

City of Mary Esther, Florida

**Statement of Revenues, Expenses and Changes in Fund Net Assets
Proprietary Funds**

| Year ended September 30, | 2005 |
|--|---------------------------------|
| | Water and Sewer Fund |
| Revenues | |
| Charges for services: | |
| Water utility revenue | \$ 448,730 |
| Sewer utility revenue | 607,408 |
| Total revenues | 1,056,138 |
| Operating expenses | |
| Personal services | 235,745 |
| Professional services | 649,653 |
| Travel and per diem | 41 |
| Communications | 5,787 |
| Utilities | 92,304 |
| Insurance | 44,000 |
| Printing and binding | 5,200 |
| Repairs and maintenance | 335,975 |
| Other current charges | 9,942 |
| Office supplies | 7,055 |
| Operating supplies | 35,422 |
| Depreciation and amortization | 271,684 |
| Grant expense | 20,260 |
| Books and publications | 1,220 |
| Total operating expenses | 1,714,288 |
| Operating income | (658,150) |
| Non-operating revenues (expenses) | |
| Interest earnings | 100,831 |
| Interest expense | (172,130) |
| Utility service fees | 454,026 |
| Franchise fees | 203,970 |
| Grant revenue | 71,931 |
| Total non-operating revenues (expenses) | 658,628 |
| Net income (loss) before operating transfers | 478 |
| Other financing sources (uses) | |
| Operating transfers to other funds | (93,759) |
| Net income (loss) | (93,281) |
| Fund balance, October 1 | 7,377,321 |
| Fund balance, September 30 | \$ 7,284,040 |

See accompanying notes to financial statements.

City of Mary Esther, Florida

Statement of Cash Flows - Water and Sewer Fund

| Year ended September 30, | 2005 |
|---|--------------|
| Cash flows from operating activities | |
| Receipts from customers | \$ 1,061,157 |
| Payments to employees | (247,952) |
| Payments to suppliers | (1,202,307) |
| Net cash used by operating activities | (389,102) |
| Cash flows from non-capital financing activities | |
| Utility service fees | 454,026 |
| Franchise fees | 191,918 |
| Advances from other funds | (37,341) |
| Transfers to other funds | (93,759) |
| Grant revenue | 71,931 |
| Net cash provided by non-capital financing activities | 586,775 |
| Cash flows from capital and related financing activities | |
| Acquisition of fixed assets | (2,900) |
| Principal paid on bonds | (170,000) |
| Interest paid on bonds | (174,149) |
| Net cash used by capital and related financing activities | (347,049) |
| Cash flows from investing activities | |
| Redemption of investments | 70,465 |
| Interest income | 100,010 |
| Net cash provided by investing activities | 170,475 |
| Net increase (decrease) in cash and cash equivalents | 21,099 |
| Cash and cash equivalents, beginning of year | 390,796 |
| Cash and cash equivalents, end of year | \$ 411,895 |
| | (continued) |

See accompanying notes to financial statements.

City of Mary Esther, Florida

Statement of Cash Flows - Water and Sewer Fund (Continued)

Year ended September 30,

2005

| | |
|--|--------------|
| Reconciliation of operating income to net cash provided (used) by operating activities: | |
| Operating income | \$ (658,150) |
| Adjustments to reconcile operating income to net cash provided (used) by operating activities: | |
| Depreciation and amortization | 271,684 |
| Change in operating assets and liabilities: | |
| Accounts receivable | 409 |
| Accounts payable | 4,552 |
| Compensated absences | (12,207) |
| Deposits | 4,610 |

Net cash provided (used) by operating activities \$ (389,102)

See accompanying notes to financial statements.

City of Mary Esther, Florida

Statement of Net Assets - Pension Trust Fund

| <i>September 30,</i> | 2005 |
|------------------------------------|--------------|
| Assets | |
| Investments | \$ 1,140,633 |
| Total assets | 1,140,633 |
| Liabilities | |
| Liabilities | - |
| Total liabilities | - |
| Net assets | |
| Held in trust for pension benefits | \$ 1,140,633 |

See accompanying notes to financial statements.

City of Mary Esther, Florida

Statement of Changes in Net Assets - Pension Trust Fund

| <i>Year ended September 30,</i> | 2005 |
|---------------------------------|--------------|
| Additions | |
| Contributions | \$ 98,157 |
| Investment gains (losses) | 116,888 |
| Total additions | 215,045 |
| Deductions | |
| Benefits and other withdrawals | 10,358 |
| Total deductions | 10,358 |
| Change in net assets | 204,687 |
| Net assets, October 1 | 935,946 |
| Net assets, September 30 | \$ 1,140,633 |

See accompanying notes to financial statements.

City of Mary Esther, Florida

Notes to Financial Statements

NOTE 1 – NATURE OF ORGANIZATION

The City of Mary Esther (hereinafter referred to as "City") was established as a town under Laws of the State of Florida in 1946. On June 5, 1984, after referendum vote by the citizens of Mary Esther, the Council approved ordinance number 84-3 to incorporate Mary Esther as a city. The City operates under a council form of government and provides the following services: public safety (law enforcement, fire control, and protective inspections), physical environment (community development), transportation (road and street facilities), human services (animal control), culture and recreation (library and parks and recreation), sanitation (water and sewer utilities), and general government.

In evaluating how to define the City for financial reporting purposes, management has considered all potential component units. The decision to include, or exclude, a potential component unit in the reporting entity was made by applying the criteria set forth in Government Accounting Standards Board Statement 14. The basic - but not the only – criterion for including a potential component unit within the reporting entity is the governing body's ability to exercise oversight responsibility. The most significant manifestation of this ability is financial interdependency. Other manifestations of the ability to exercise oversight responsibility include, but are not limited to, the selection of governing authority, the designation of management, the ability to significantly influence operations, and accountability for fiscal matters. A second criterion used in evaluating potential component units is the scope of public service. Application of this criterion involves considering whether the activity benefits the City and/or its citizens, or whether the activity is conducted within the geographic boundaries of the City and is generally available to its citizens. A third criterion used to evaluate potential component units for inclusion or exclusion from the reporting entity is the existence of special financing relationships, regardless of whether the City is able to exercise oversight responsibilities. Management determined that there were no other government units located within the geographic boundaries of the City and, thus, no potential component units were considered.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Measurement Focus, Basis of Accounting and Basis of Presentation

Government-wide Financial Statements – Government-wide financial statements, including the statement of net assets and statement of activities, present information about the City as a whole. These statements include the non-fiduciary financial activity of the primary government.

Government-wide financial statements are prepared using the economic resources measurement focus. The statement of activities presents a comparison between direct expenses and program revenues for each function or program of the City's governmental activities. Direct expenses are those that are specifically associated with a service, program, or department and are thereby clearly identifiable to a particular function.

City of Mary Esther, Florida

Notes to Financial Statements

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Program revenues include charges paid by the recipient of the goods or services offered by the program and grants and contributions that are restricted to meeting the operations or capital requirements of a particular program. Revenues that are not classified as program revenues are presented as general revenues, with certain exceptions. The comparison of direct expenses with program revenues identifies the extent to which each governmental function or business segment is self-financing or draws from the general revenues of the City.

The effects of interfund activity have been eliminated from the government-wide financial statements.

The government-wide financial statements are prepared using the accrual basis of accounting. Revenues are recognized when earned, and expenses are recognized when a liability is incurred, regardless of the timing of the related cash flows. Property taxes are recognized in the year for which they are levied. Revenues from grants, entitlements, and donations are recognized in the fiscal year in which all eligibility requirements imposed by the provider have been satisfied.

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

Fund Financial Statements - Governmental Funds are used to account for the general government activities. Governmental fund types use the flow of current financial resources measurement focus and the modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues are recognized when susceptible to accrual (i.e., when they are "measurable and available"). "Measurable" means the amount of the transaction can be determined and "available" means collectible within the current period or soon enough thereafter to pay liabilities of the current period. The City considers all revenues available if they are collected within 60 days after year end. Expenditures are recorded when the related fund liability is incurred, except for unmatured interest on general long-term debt which is recognized when due, and certain compensated absences and claims and judgments which are recognized when the obligations are expected to be liquidated with expendable available financial resources.

Property taxes, franchise taxes, licenses, interest and special assessments are susceptible to accrual. Sales taxes collected and held by the state at year end on behalf of the City are also recognized as revenue. Other receipts and taxes become measurable and available when cash is received by the City and are recognized as revenue at that time.

Entitlements and shared revenues are recorded at the time of receipt or earlier if the susceptible to accrual criteria are met. Expenditure-driven grants are recognized as revenue when the qualifying expenditures have been incurred and all other grant requirements have been met.

City of Mary Esther, Florida

Notes to Financial Statements

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Governmental funds include the following funds:

The General Fund is the City's primary operating fund. This fund accounts for all financial resources of the general government, except those required to be accounted for in another fund. All general tax revenues and other receipts that are not restricted by law or contractual agreement to some other fund are accounted for in this fund. General operating expenditures, fixed charges and capital improvement costs that are not paid through other funds are paid from the General Fund.

The Federal Programs Fund accounts for federal assistance received from the Federal Emergency Management Agency as a result of Hurricane Ivan and Hurricane Dennis and the associated expenditures.

The Other Governmental Fund accounts for the acquisition of fixed assets or construction of major capital facilities (other than those financed by Proprietary Funds) being financed from grants or transfers from other funds.

Proprietary Funds are accounted for on the flow of economic resources measurement focus and use the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. The City applies all applicable Governmental Accounting Standards Board ("GASB") pronouncements as well as Financial Accounting Standards Board ("FASB") statements and interpretations issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

Proprietary funds include the following fund types:

Enterprise Funds are used to account for those operations that are financed and operated in a manner similar to private business or where the City has decided that the determination of revenues earned, costs incurred and/or net income is necessary for management accountability. The City's Water and Sewer Fund is an enterprise fund.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the City's enterprise fund are charges to customers for sales of water and sewer services. Operating expenses for enterprise funds include the cost of sales and service, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

City of Mary Esther, Florida

Notes to Financial Statements

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fiduciary Funds account for assets held by the City in a trustee capacity or as an agent on behalf of others. Trust funds account for assets held by the City under the terms of a formal trust agreement.

Pension Trust Fund is custodial in nature and does not present results of operations or have a measurement focus. Pension Trust Funds are accounted for using the modified accrual basis of accounting. The Pension Trust Fund accounts for the assets of the City's Employee Thrift Plan.

Cash and Cash Equivalents

The City's cash and cash equivalents are considered to be cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition.

The City maintains its deposits with banks qualified as public depositories under Florida law. All deposits are insured by Federal depository insurance and/or collateralized pursuant to the Public Depository Security Act of the State of Florida.

Investments

The City is authorized under the City's investment policy to invest and reinvest surplus public funds in its control or possession, in accordance with resolutions to be adopted from time to time and in accordance with Chapter 166.261, as amended under Chapter 21 Part IV, sections 218.40 through 218.45.

According to its policy, the City's primary objectives in priority order are: 1) safety, 2) liquidity, and 3) return on investment. The policy prohibits the following investments and investment practices:

1. Purchases on margin or short sales.
2. Derivative securities that are, in effect, a leveraged bet on future movements of interest rates or some price index. Collateralized mortgage obligations, because of their complexity and prepayment rate uncertainties, are prohibited.
3. Lending securities with an agreement to buy them back after a state period of time (reverse purchased agreements from the perspective of the public body).

All investments are stated at fair market value.

City of Mary Esther, Florida

Notes to Financial Statements

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Investments (continued)

The City's investment pool participates in the Local Government Surplus Trust Fund, operated by Florida's State Board of Administration (SBA). The SBA is governed by Chapter 19-7 of the Florida Administrative Code (FAC). The FAC provides guidance and establishes the general operating procedures for the administration of the Local Government Surplus Trust Fund. Additionally, the Florida Auditor General performs an operational audit of activities and investments of the SBA. In accordance with GASB Statement Number 31, Local Government Surplus Trust Fund is a "2A-7 like" pool and thus, SBA investments are valued using the pooled share price.

Receivables and Payables

Transactions between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "interfund receivables/payables" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds."

Advances between funds, if any, are offset by a fund balance reserve account in applicable governmental funds to indicate they are not available for appropriation and are not expendable available financial resources.

All receivables are shown net of an allowance for uncollectibles. At September 30, 2005, the City considers all receivables collectible and accordingly does not have an allowance.

Services provided, deemed to be at market, or near market rates, are treated as revenues and expenditures/expenses. Reimbursements occur when one fund incurs a cost, charges the appropriate benefiting fund, and reduces its related cost as a reimbursement. All other interfund transactions are treated as transfers. Transfers between governmental or proprietary funds are netted as part of the reconciliation to the government-wide columnar presentation.

Property Taxes

The City's ad valorem taxes are assessed by the Okaloosa County Property Appraiser and collected by the Okaloosa County Tax Collector in accordance with Florida Statutes. The City retains the right and duty to set millage rates. Property taxes are not recorded as receivables at September 30th because, though legally assessed as of January 1, they are not due and payable until after the close of the fiscal year ended the following September 30th.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Receivables and Payables (continued)

Property Taxes_(continued)

The following is the current property tax calendar.

| | |
|------------------|------------------|
| Assessment date | January 1, 2004 |
| Levy date | November 1, 2004 |
| Due date | March 31, 2005 |
| Delinquency date | April 1, 2005 |

Discounts of 1% for each month taxes are paid prior to March are granted.

Revenue recognition criteria for property taxes under GASB requires that only property taxes expected to be collected within 60 days of the current period be accrued. Property taxes which are uncollected as of the end of the fiscal year are generally immaterial in amount and highly susceptible to uncollectibility; therefore, they are not recorded as a receivable at the balance sheet date.

Water and Sewer Charges Receivable

No allowance for doubtful accounts is considered necessary in the water and sewer fund since the City has the right to discontinue customers' service. Thus, the City has elected to record bad debts using the direct write-off method. Generally accepted accounting principles require that the allowance method be used to reflect bad debts. However, the effect of the use of the direct write-off method is not materially different from the results that would have been obtained had the allowance method been followed.

Restricted Assets

Certain proceeds of the City's Enterprise Fund Revenue Bonds, as well as certain resources set aside for their repayment, are classified as restricted assets on the balance sheet because their use is limited by applicable bond covenants. Additionally, customer deposits for water and sewer services are classified as restricted assets.

Fixed Assets

Capital assets acquired or constructed for general City purposes are reported at cost in the government-wide statement of net assets but are not reported in the governmental fund financial statements. Assets are recorded at cost or estimated historical cost if purchased or constructed. Donated fixed assets are recorded at their estimated fair value at the date of donation. The City's capitalization level is \$500.

City of Mary Esther, Florida

Notes to Financial Statements

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fixed Assets (continued)

Interest costs incurred during construction of general capital assets are not considered material and are not capitalized as part of the construction.

As allowed under GASB Statement Number 34, the City elected not to capitalize and report public domain (infrastructure) general fixed assets (e.g., roads, bridges, sidewalks; and other assets that are immovable and of value only to the government) retroactively.

The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are expensed as incurred.

Property, plant and equipment in the proprietary funds of the government are recorded at cost. Property, plant and equipment donated to these proprietary fund type operations are recorded at their estimated fair value at the date of donation.

Major outlays for capital assets and improvements are capitalized in proprietary funds as projects are constructed. Interest incurred during the construction phase of proprietary fund fixed assets is reflected in the capitalized value of the asset constructed, net of interest earned on the invested proceeds over the same period.

Property, plant and equipment are depreciated using the straight-line method over the following estimated useful lives:

| Assets | Years |
|-----------------------------------|--------------|
| Improvements other than buildings | 10 - 50 |
| Machinery, equipment and vehicles | 5 - 10 |

Compensated Absences

Vested or accumulated leave (annual, personal and sick) that is expected to be liquidated with expendable available financial resources is reported as an expenditure and a fund liability of the governmental fund that will pay it. All vested or accumulated leave is accrued when incurred in the government-wide and proprietary fund financial statements. In accordance with the provisions of Governmental Accounting Standards Board Statement No. 16, *Accounting for Compensated Absences*, no liability is recorded for nonvesting accumulating rights to receive sick pay or personal leave benefits.

City of Mary Esther, Florida
Notes to Financial Statements

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Compensated Absences (continued)

The policy of the City for annual leave is as follows:

| Length of Employment | Earned Leave Per Year |
|-----------------------------|----------------------------------|
| 0 - 6 months | 40 hours |
| 7 months - 2 years | 80 hours |
| 3 - 4 years | 120 hours |
| over 5 years | 160 hours |

Certain employees are grandfathered in under the previous annual leave policy and may accumulate leave at a rate of 200 hours for 9-10 years of service and 240 hours for service in excess of 11 years.

Upon proper separation (termination) of employment, employees will be paid for all accumulated annual leave up to 240 hours.

Employees of the City also accumulate personal leave at a rate of four hours per month. Upon termination of employment, employees will be paid for all personal leave up to 96 hours.

The policy of the City for sick leave is that all full-time, permanent employees accrue sick leave at a rate of eight hours per month. The maximum number of hours to be accumulated is 1,260 for fire department employees and 960 for all other employees. Upon proper separation (termination) of employment, employees will be paid for accumulated sick leave at a rate of two hours for each eight hours of accumulated sick leave. In the case of death while employed, all accumulated sick leave will be paid to the beneficiary.

In the government-wide financial statements, compensated absences (i.e., paid absences for employee vacation leave and sick leave) are recorded as liabilities to the extent that it is probable that the benefits will result in termination payments. A liability is reported in the governmental fund financial statements only for the current portion of compensated absences expected to be paid using expendable available resources.

Long-Term Obligations

Long-term debt and other obligations financed by the enterprise fund are reported as liabilities in the fund and in the government-wide statement of net assets. For proprietary fund types, bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight line method. Bonds payable are reported net of the applicable bond premium or discount. Issuance costs are reported as deferred charges.

Changes in the City's long-term debt for the current year is reported in a subsequent note.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fund Equity

Reservations of fund balance represent amounts that are legally segregated for a specific purpose. Reservations of retained earnings are limited to outside third-party restrictions. Designations of fund balance represent tentative management plans that are subject to change. The proprietary fund's contributed capital represents equity acquired through capital grants and capital contributions from developers, customers or other funds.

Use of 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.

Budgetary Information

Annual appropriated budgets are adopted for the General Fund, Other Governmental Fund, and the Water and Sewer Fund. The annual budgets for the General Fund and Other Governmental Fund are adopted using the modified accrual basis of accounting, which is in accordance with GAAP for governmental fund types. The Water and Sewer Fund budget is also adopted on the modified accrual basis, which is not consistent with GAAP for proprietary fund types. Every appropriation, except an appropriation for a capital expenditure, lapses at the end of the year to the extent it has not been expended or encumbered.

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

1. Prior to September 30, the City Manager submits to the City Council a proposed operating budget for the fiscal year commencing the following October 1. The operating budget includes proposed expenditures and revenue sources.
2. Public hearings are conducted to obtain taxpayer comments.
3. Prior to October 31, the budget is legally enacted through passage of an ordinance.
4. The City Manager is authorized to transfer budgeted amounts among programs within a department, office or agency within any fund; however, any revisions that alter the total expenditures of any fund must be approved by the City Council.
5. Budgeted amounts have been amended by the City Council or by City Manager in accordance with applicable City ordinances.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Budgetary Information (continued)

6. Encumbrance accounting is employed in governmental funds. Encumbrances (e.g., purchase orders, contracts) outstanding at year end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be reappropriated and honored during the subsequent year.

NOTE 3 – INVESTMENTS

The following is a summary of the City's investments:

| <i>September 30,</i> | 2005 |
|---|---------------------|
| Certificates of Deposit | \$ 1,788,440 |
| Common Stock | 180,234 |
| Local Government Surplus Funds Trust Fund | 3,662,792 |
| Total investments | \$ 5,631,466 |

The Local Government Surplus Funds Trust Fund is similar to a mutual fund in that funds are available on a same day basis. As of June 30, 2005, the Local Government Surplus Funds Trust Fund had total investments of approximately \$1.8 billion. The portfolio's weighted average maturity is limited to 90 days. The City allocates interest earned on investments held in the Local Government Surplus Funds Trust Fund based on individual funds' principal balances. The City's investments in the Local Government Surplus Trust Fund investment pool are unrated.

City of Mary Esther, Florida

Notes to Financial Statements

NOTE 3 – INVESTMENTS (CONTINUED)

The common stock investments held by the City are a result of demutualization transactions entered into by the City's insurance company, Principal Financial Group, Inc., and retirement plan fiduciary, Prudential Financial, Inc. during the fiscal year ending September 30, 2002. Both of these companies converted from mutual insurance companies to stock companies. In demutualization, membership interests of eligible policy and contract holders are exchanged for compensation, which may be in the form of stock, cash or policy/contract enhancements. During the fiscal year ended September 30, 2005, the City recognized \$48,612 in net unrealized gains related to its common stock investments.

The City's current investment policy allows certain types of investments and prohibits other types of investments. Investments in common stock are neither specifically allowed nor prohibited in the investment policy. Management concluded that the continued ownership by the City of these common stock investments is acceptable under the current investment policy.

NOTE 4 - CHANGES IN CAPITAL ASSETS

Changes in capital assets for the year ended September 30, 2005 are shown below:

| | Beginning Balance | Additions | Deletions | Ending Balance |
|--|----------------------|--------------------|-------------|---------------------|
| Governmental Activities: | | | | |
| <i>Capital assets not being depreciated:</i> | | | | |
| Land | \$ 4,363,248 | \$ - | \$ - | \$ 4,363,248 |
| <i>Capital assets being depreciated:</i> | | | | |
| Buildings | 672,951 | - | - | 672,951 |
| Improvements other than building | 310,158 | 1,794 | - | 311,952 |
| Machinery, equipment and vehicles | 1,282,545 | 84,266 | (10,175) | 1,356,636 |
| Books, publications, and library materials | 1,088 | - | - | 1,088 |
| Total capital assets being depreciated | 2,266,742 | 86,060 | (10,175) | 2,342,627 |
| <i>Less accumulated depreciation for:</i> | | | | |
| Buildings | 216,053 | 15,153 | - | 231,206 |
| Improvements other than building | 118,821 | 14,914 | - | 133,735 |
| Machinery, equipment and vehicles | 802,664 | 115,306 | (10,175) | 907,795 |
| Total accumulated depreciation | 1,137,538 | 145,373 | (10,175) | 1,272,736 |
| Total capital assets being depreciated, net | 1,129,204 | (59,313) | - | 1,069,891 |
| Governmental activities capital assets, net | \$ 5,492,452 | \$ (59,313) | \$ - | \$ 5,433,139 |

City of Mary Esther, Florida

Notes to Financial Statements

NOTE 4 - CHANGES IN CAPITAL ASSETS (CONTINUED)

| | Beginning Balance | Additions | Deletions | Ending Balance |
|---|----------------------|---------------------|-----------------|---------------------|
| Business-type Activities: | | | | |
| <i>Capital assets not being depreciated:</i> | | | | |
| Land | \$ 77,878 | \$ - | \$ - | \$ 77,878 |
| <i>Capital assets being depreciated:</i> | | | | |
| Buildings | 63,415 | - | - | 63,415 |
| Improvements other than building | 9,946,102 | - | - | 9,946,102 |
| Machinery, equipment and vehicles | 636,286 | 2,898 | (53,978) | 585,206 |
| Total capital assets being depreciated | 10,645,803 | 2,898 | (53,978) | 10,594,723 |
| <i>Less accumulated depreciation for:</i> | | | | |
| Buildings | 3,776 | 1,534 | - | 5,310 |
| Improvements other than building | 3,966,722 | 212,878 | - | 4,179,600 |
| Machinery, equipment and vehicles | 425,348 | 30,812 | (53,978) | 402,182 |
| Total accumulated depreciation | 4,395,846 | 245,224 | (53,978) | 4,587,092 |
| Total capital assets being depreciated, net | 6,249,957 | (242,326) | - | 6,007,631 |
| Business-type activities capital assets, net | \$ 6,327,835 | \$ (242,326) | \$ - | \$ 6,085,509 |

The City elected not to capitalize and report general infrastructure assets (e.g., roads, bridges, sidewalks; and other assets that are immovable and of value only to the government) retroactively. The City did not have any general infrastructure asset additions during the fiscal year ending September 30, 2005.

Depreciation expense for fiscal year ended September 30, 2005, totaled \$145,373 for governmental activities and \$245,224 for business-type activities. Depreciation expense was not allocated to specific functions.

City of Mary Esther, Florida

Notes to Financial Statements

NOTE 5 – LONG-TERM DEBT

Enterprise Fund

In October, 1996, the City issued \$4,390,000 of Water and Sewer Revenue Bonds (Series 1996) with an average interest rate of 5.2 percent to advance refund \$4,030,000 of outstanding 1992 Series bonds with an average interest rate of 6.8 percent. The net proceeds of \$4.2 million (after payment of \$160,000 in bond issue costs and \$61,500 in discounts) plus \$164,700 of 1992 Series sinking fund moneys were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the 1992 Series bonds. As a result, the 1992 Series bonds are considered to be defeased and the liability for those bonds has been removed from the books of the Water and Sewer Enterprise Fund.

The advance refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of \$432,647. This difference, reported in the accompanying financial statements as a deduction from bonds payable, is being charged to operations through the year 2018 using straight-line amortization.

The City pledged as security for payment of the principal and interest on the Water and Sewer Revenue Bonds the net revenues (gross revenues less cost of operation and maintenance) derived from operation of the water and sewer system together with the proceeds derived from utility taxes collected on water, electricity, natural gas, and telecommunication services charged to customers within the City and from franchise fees collected from Gulf Power Company, Okaloosa County Gas District and various telephone companies. Revenue bonds outstanding, net of unamortized discount of \$35,487 and deferred refunding expenses of \$249,409 at year end, are as follows:

| <u>Purpose</u> | <u>Interest Rates</u> | <u>Amount</u> |
|---|-----------------------|---------------|
| Water and sewer system acquisition, construction, extension and improvements | 4.0% - 5.375% | \$ 2,950,104 |

City of Mary Esther, Florida

Notes to Financial Statements

NOTE 5 – LONG-TERM DEBT (CONTINUED)

Revenue bond debt service requirements to maturity are as follows:

| <i>Fiscal year ending September 30,</i> | Principal | Interest | Amount |
|---|---------------------|---------------------|---------------------|
| 2006 | \$ 180,000 | \$ 165,746 | \$ 345,746 |
| 2007 | 185,000 | 156,803 | 341,803 |
| 2008 | 200,000 | 147,174 | 347,174 |
| 2009 | 205,000 | 136,847 | 341,847 |
| 2010 | 220,000 | 125,846 | 345,846 |
| 2011-2015 | 1,305,000 | 434,925 | 1,739,925 |
| 2016-2018 | 940,000 | 76,325 | 1,016,325 |
| Total | \$ 3,235,000 | \$ 1,243,666 | \$ 4,478,666 |

Additional disclosures required by the Water and Sewer Revenue Bonds, Series 1996:

| Schedule of Insurance | Coverage |
|--|-----------------|
| Liability - Property/Physical Damage | \$ 2,000,000 |
| Bond, Blanket Protection Administrative | 2,000,000 |
| Inspection, Water and Sewer, and Fire Department | 1,000,000 |
| Fidelity bond - City Manager | 100,000 |
| Fidelity bond - City Clerk | 100,000 |
| Workers' Compensation | 1,000,000 |
| Accidental Death and Dismemberment | N/A |

As of September 30, 2005, there were 1,924 customers connected to the City's water and sewer system.

City of Mary Esther, Florida

Notes to Financial Statements

NOTE 5 – LONG-TERM DEBT (CONTINUED)

Changes in Long-Term Liabilities

Long-term liability activity for the fiscal year ended September 30, 2005, was as follows:

| | Beginning Balance | Additions | Reductions | Ending Balance | Amounts Due within One Year |
|--|----------------------|-----------|--------------|-------------------|-----------------------------------|
| Governmental Activities | | | | | |
| Compensated absences | \$ 123,882 | \$ 6,197 | \$ - | \$ 130,079 | \$ - |
| Business-type Activities | | | | | |
| Water and sewer bonds payable | \$ 3,405,000 | \$ - | \$ (170,000) | \$ 3,235,000 | \$ 180,000 |
| Less deferred amount on refundings | (269,768) | - | 20,359 | (249,409) | - |
| Less unamortized discount | (38,383) | - | 2,896 | (35,487) | - |
| Total bonds payable | 3,096,849 | - | (146,745) | 2,950,104 | 180,000 |
| Compensated absences | 12,207 | - | (12,207) | - | - |
| Business-type activities long-term liabilities | \$ 3,109,056 | \$ - | \$ (158,952) | \$ 2,950,104 | \$ 180,000 |

Records kept for compensated absences related only to hours earned, used, and available. Accordingly, only the net change in compensated absences payable is shown.

Compensated Absences

The total amounts of the vested portions of compensated absences as of September 30, 2005, were as follows:

| September 30, | Annual Leave | Sick Leave | Total |
|--------------------------|-----------------|---------------|------------|
| Governmental activities | \$ 92,210 | \$ 37,869 | \$ 130,079 |
| Business-type activities | - | - | - |
| Total government-wide | \$ 92,210 | \$ 37,869 | \$ 130,079 |

City of Mary Esther, Florida

Notes to Financial Statements

NOTE 6 - RESERVED RETAINED EARNINGS AND RESTRICTED ASSET ACCOUNTS

The City's bond covenants require certain reservations of the Water and Sewer Fund's retained earnings. The reserved portions are as follows:

| | |
|--|------------|
| <i>September 30,</i> | |
| Reserved for bond reserve requirement | \$ 387,416 |
| Reserved for revenue bond debt service | 182,207 |
| Reserved for renewal and replacement | 119,000 |

| | |
|---|-------------------|
| <u>Total reserved retained earnings</u> | <u>\$ 688,623</u> |
|---|-------------------|

The balances of the Water and Sewer Fund's restricted asset accounts are as follows:

| | |
|--|-------------------|
| <i>September 30,</i> | |
| Customer deposits | \$ 79,249 |
| Revenue bond reserve account | 387,416 |
| Revenue bond debt service account | 182,207 |
| Revenue bond renewal and replacement account | 119,000 |
| <u>Total restricted assets</u> | <u>\$ 767,872</u> |

NOTE 7 – INTERFUND RECEIVABLES, PAYABLES AND TRANSFERS

The following is a summary of interfund receivables and payables reported in the fund financial statements:

| | Interfund Receivables | Payables |
|----------------------------|--------------------------|-------------------|
| <i>September 30,</i> | | |
| <i>Governmental funds:</i> | | |
| General fund | \$ - | \$ 341,105 |
| Federal programs fund | 29,745 | - |
| Other governmental fund | 274,743 | - |
| <i>Proprietary funds:</i> | | |
| Water and sewer fund | 36,617 | - |
| <u>Total</u> | <u>\$ 341,105</u> | <u>\$ 341,105</u> |

Other governmental fund receivables represent the transfer of excess revenues over expenses from the general fund to cover capital improvement expenditures.

City of Mary Esther, Florida

Notes to Financial Statements

NOTE 7 – INTERFUND RECEIVABLES, PAYABLES AND TRANSFERS (CONTINUED)

The following is a summary of interfund transfers as reported in the fund financial statements:

| <u>September 30,</u> | Interfund | |
|--|--------------|---------------|
| | Transfers In | Transfers Out |
| <i>Between governmental and business-type columns:</i> | | |
| General fund (2) | \$ 199,738 | \$ - |
| Federal programs fund | - | 105,738 |
| Water and sewer fund (2) | - | 93,759 |

| | | |
|--|---------|---------|
| <i>Between funds within the governmental or business-type columns: (1)</i> | | |
| General fund (3) | - | 274,743 |
| Capital improvement fund (3) | 274,743 | - |

Notes:

- (1) These transfers are eliminated in the consolidation, by column, for the Governmental and Business-type Activities.
- (2) Transfer of excess funds from the Water and Sewer Fund to the General Fund is budgeted for and made annually to balance the General Fund budget.
- (3) Transfer of excess of revenues over expenses from the General Fund to the Other Governmental Fund is made annually to fund capital improvement expenses.

NOTE 8 – RISK MANAGEMENT

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City pays an annual premium to the Preferred Governmental Insurance Trust for the following insurance coverage: general liability, auto liability, auto physical damage, workers' compensation, inland marine, boiler machinery and special events coverage. The Preferred Governmental Insurance Trust is self-sustaining through member premiums and reinsures through commercial companies for claims in excess of specified levels, depending on the type of coverage.

The City carries commercial insurance for all other risks of loss, including fidelity bond, accidental death and dismemberment and employee health insurance. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

City of Mary Esther, Florida

Notes to Financial Statements

NOTE 9– EMPLOYEE THRIFT PLAN

The City offers its employees an Employee Thrift Plan, a defined contribution plan created in accordance with Internal Revenue Code Sections 401(a) and 501(a), as amended from time to time. The plan is available to all City employees who have attained the age of eighteen. The City's contribution to the Plan is an amount equal to six percent (6%) of the Participant's compensation for the plan year. In addition, the City contributes on behalf of each Participant who makes a contribution to the Deferred Compensation Plan one dollar (\$1.00) for every one dollar (\$1.00) of said contributions to the Deferred Compensation Plan in increments of one percent (1%) of compensation, up to six percent (6%). Any forfeiture during the year may be used to fund the City's contribution requirement.

The vesting percentage of City contributions is determined in accordance with the following schedule:

| Number of Years of Service | Vested Percentage |
|----------------------------|-------------------|
| 1 | 20% |
| 2 | 40% |
| 3 | 60% |
| 4 | 80% |
| 5 | 100% |

During the fiscal year ended September 30, 2005, the City made contributions totaling \$98,157.

NOTE 10 – LITIGATION

The City is involved in several pending and threatened legal actions. In the opinion of City management, after consulting with legal counsel, the range of potential loss from all such claims and actions should not materially affect the financial condition of the City.

Required Supplementary Information
(Other Than MD&A)

City of Mary Esther, Florida

Budgetary Comparison Schedule – General Fund

| | Year ended September 30, | | 2005 | | Actual (Budgetary Basis) (See Note A) | Variance with Final Budget Positive (Negative) |
|---|--------------------------|---------------------|---------------------|-----------------|--|---|
| | Original | Final | Budgeted Amounts | Actual | | |
| Revenues | | | | | | |
| Taxes | \$ 832,240 | \$ 832,240 | \$ 858,922 | \$ 26,682 | | |
| Federal/state grants | 70,089 | 70,089 | - | (70,089) | | |
| Licenses and permits | 179,300 | 179,300 | 198,711 | 19,411 | | |
| Intergovernmental | 604,711 | 604,711 | 732,456 | 127,745 | | |
| Charges for services | 132,574 | 132,574 | 138,457 | 5,883 | | |
| Fines and forfeitures | 43,600 | 43,600 | 77,818 | 34,218 | | |
| Miscellaneous | 182,576 | 182,576 | 132,675 | (49,901) | | |
| Total revenues | 2,045,090 | 2,045,090 | 2,139,039 | 93,949 | | |
| Expenditures | | | | | | |
| General government | 449,928 | 449,928 | 445,042 | 4,886 | | |
| Public Safety | 960,507 | 960,507 | 954,267 | 6,240 | | |
| Physical environment | - | - | 335,950 | (335,950) | | |
| Transportation | 359,834 | 359,834 | 13,846 | 345,988 | | |
| Human services | - | - | 238,743 | (238,743) | | |
| Culture and recreation | 204,732 | 204,732 | - | 204,732 | | |
| Grant expense | 70,089 | 70,089 | - | 70,089 | | |
| Capital outlay | - | - | 76,186 | (76,186) | | |
| Total expenditures | 2,045,090 | 2,045,090 | 2,064,034 | (18,944) | | |
| Excess (deficit) of revenues over expenditures | - | - | 75,005 | 75,005 | | |
| Other financing sources (uses) | | | | | | |
| Transfers in | - | - | 199,738 | (199,738) | | |
| Transfers out | - | - | (274,743) | 274,743 | | |
| Net other financing sources (uses) | - | - | (75,005) | 75,005 | | |
| Excess (deficit) of revenues and other sources over expenditures and other uses | - | - | - | - | | |
| Fund balance, October 1, 2004 | 2,390,994 | 2,390,994 | 2,390,994 | - | | |
| Fund balance, September 30, 2005 | \$ 2,390,994 | \$ 2,390,994 | \$ 2,390,994 | \$ - | | |

City of Mary Esther, Florida

Schedule of Expenditures of Federal Awards

For the year ended September 30,

2005

| Federal Grantor/Pass-Through Grantor/Program Title | Catalog of | | Amount of Expenditures (Note 1) |
|--|------------------------------------|-----------------------------|---------------------------------|
| | Federal Domestic Assistance Number | Pass-Through Grantor Number | |

Department of Homeland Security (Federal Emergency Management Agency)

Indirect:

| | | | |
|--|--------|-------|------------|
| Florida Department of Community Affairs: | | | |
| Public Assistance Grants | 97.036 | WF067 | \$ 546,001 |

Direct:

| | | | |
|--|--------|---|--------|
| Assistance to Firefighters Grant Program | 97.044 | - | 77,696 |
|--|--------|---|--------|

Total Expenditures of Federal Awards **\$ 623,697**

On the accompanying Statement of Revenues, Expenditures and Changes in Fund Balance – Governmental Funds, \$517,698 of the federal awards expenditures are shown in the Federal Programs Fund and a transfer out of \$105,979. The General Fund and the Water and Sewer Fund show transfers in totaling \$105,979 from the Federal Programs Fund as the remaining expenditures of federal awards received in fiscal year end September 30, 2005 are recorded in these funds.

Notes:

1) Basis of Presentation. The Schedule of Expenditures of Federal Awards represents amounts expended from Federal Programs during the 2004-2005 fiscal year based on the modified accrual basis of accounting. The amounts reported on the Schedule have been reconciled to and are in material agreement with amounts recorded in the District's accounting records from which the basic financial statements have been reported.

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

The Honorable Mayor and Members of the City Council
City of Mary Esther, Florida

We have audited the financial statements of the governmental activities, the business-type activities, and each fund of the City of Mary Esther, Florida (hereinafter referred to as the "City"), as of and for the year ended September 30, 2005, which collectively comprise the City's basic financial statements and have issued our report thereon dated December 15, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the City's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the City Council, management and the State awarding agencies, and is not intended to be and should not be used by anyone other than these specified parties.

Carly Riggs & Ingram, L.L.C.

Destin, Florida
December 15, 2005

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

The Honorable Mayor and Members of the City Council
City of Mary Esther, Florida.

Compliance

We have audited the compliance of City of Mary Esther, Florida (hereinafter referred to as the "City") with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal awards programs for the year ended September 30, 2005. The City's major federal awards programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal awards programs is the responsibility of the City's management. Our responsibility is to express an opinion on the City's compliance based on our audit.

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

In our opinion, the City complied, in all material respects, with the requirements referred to above that are applicable to its major federal awards programs for the year ended September 30, 2005.

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Internal Control Over Compliance

The management of the City is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal awards programs. In planning and performing our audit, we considered the City's internal control over compliance with requirements that could have a direct and material effect on a major program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on the internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants caused by error or fraud that would be material in relation to a major program or state project being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the audit committee, management, others within the organization, federal awarding agencies and pass-through entities, and specific legislative or regulatory bodies and is not intended to be and should not be used by anyone other than these specified parties.

Cary Riggs & Ingram, L.L.C.

Destin, Florida
December 15, 2005

City of Mary Esther, Florida

Schedule of Findings and Questioned Costs – Federal Awards

SUMMARY OF AUDIT RESULTS

As required by United States Office of Management and Budget *Circular A-133*, Section 505, the following is a summary of the results of the audit of the City of Mary Esther, Florida for the fiscal year ended September 30, 2005:

- The auditor's report expresses an unqualified opinion on the basic financial statements of the City of Mary Esther, Florida.
- No reportable conditions relating to the audit of the basic financial statements are reported in the Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*.
- No instances of noncompliance material to the basic financial statements of the City of Mary Esther, Florida which would be required to be reported in accordance with *Government Auditing Standards* were disclosed during the audit.
- No reportable conditions relating to the audit of the major federal award programs are reported in the Report on Compliance with Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance with *OMB Circular A-133*.
- The auditor's report on compliance for the major federal award programs for the City of Mary Esther, Florida is unqualified.
- There were no audit findings relative to the major federal award programs for City of Mary Esther, Florida.
- The programs tested as major programs included: Public Assistance Grant (97.036)
- The threshold for distinguishing between Types A and B programs was \$300,000.
- The City of Mary Esther, Florida was determined to be a low-risk auditee, as defined in *OMB Circular A-133*.

FINDINGS RELATED TO THE FINANCIAL STATEMENTS THAT ARE REQUIRED TO BE REPORTED UNDER GENERALLY ACCEPTED GOVERNMENT AUDITING STANDARDS (GAGAS)

- The results of our audit of the City of Mary Esther, Florida did not disclose any findings required to be reported in accordance with GAGAS.

FINDINGS AND QUESTIONED COSTS FOR MAJOR FEDERAL PROGRAMS

- The results of our audit of the City of Mary Esther, Florida did not disclose any findings or questioned costs required to be reported under the provision of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. No corrective action plan is required because there were no findings required to be reported under the Federal Single Audit Act.

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MANAGEMENT LETTER

The Honorable Mayor and Members of the City Council
City of Mary Esther Florida

We have audited the financial statements of the governmental activities, the business-type activities, and each fund of the City of Mary Esther, Florida (hereinafter referred to as the "City"), as of and for the year ended September 30, 2005, which collectively comprise the City's basic financial statements and have issued our report thereon dated December 15, 2005.

We conducted our audit in accordance with United States generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. We have issued our Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*. Disclosures in this report, which are dated December 15, 2005, should be considered in conjunction with this management letter.

Additionally, our audit was conducted in accordance with Chapter 10.550, Rules of the Auditor General. Those rules (Section 10.554(1)(h)) require that we address in the management letter, if not already addressed in the auditor's report on internal controls and compliance, whether or not inaccuracies, shortages, defalcations, fraud, and/or violations of laws, rules, regulations, and contractual provisions reported in the preceding annual financial audit report have been corrected. There were no inaccuracies, irregularities, shortages, defalcations, and/or violations of laws, rules, regulations, and contractual provisions disclosed in the preceding annual report.

The Rules of the Auditor General (Section 10.554(1)(h)1) require that we address in the management letter, if not already addressed in the auditor's report on internal controls and compliance, whether or not recommendations made in the preceding annual financial audit report have been followed. The recommendations made in the preceding annual financial audit report have been corrected.

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As required by the Rules of the Auditor General (Section 10.554(1)(h)2.), the scope of our audit included a review of the provisions of Section 218.415, Florida Statutes, regarding the investment of public funds. In connection with our audit, we determined that the City complied with Section 218.415, Florida Statutes.

The Rules of the Auditor General (Section 10.554(1)(h)4.), require disclosure in the management letter of the following matters if not already addressed in the Auditor's report on internal controls and compliance: (1) violations of laws, rules, regulations, and contractual provisions that have occurred, or are likely to have occurred; (2) improper or illegal expenditures; (3) improper or inadequate accounting procedures (e. g., the omission of required disclosures from the financial statements); (4) failures to properly record financial transactions; and (5) other inaccuracies, shortages, defalcations, and instances of fraud discovered by, or that come to the attention of, the auditor. Our audit disclosed none of the preceding matters.

As required by the Rules of the Auditor General (Section 10.554(1)(h)6.a.), the scope of our audit included a review of the provisions of Section 218.503(1), Florida Statutes, regarding financial emergencies. In connection with our audit, we determined that the City is not in a state of financial emergency as a consequence of the conditions described by Section 218.503(1), Florida Statutes.

As required by the Rules of the Auditor General (Section 10.554(1)(h)6.b.), we determined that the annual financial report for the City for the fiscal year ended September 30, 2004, filed with the Department of Banking and Finance pursuant to Section 218.32, Florida Statutes, is in agreement with the annual financial audit report for the fiscal year ended September 30, 2004.

As required by the Rules of the Auditor General (Section 10.554(1)(h)6.c. and 10.556(7)), we applied financial condition assessment procedures. It is management's responsibility to monitor the City's financial condition, and our financial condition assessment was based in part on representations made by management and the review of financial information provided by same.

Current Year Recommendations

There are no current year recommendations.

This management letter is intended solely for the information and use of the City Council, management and the State of Florida Office of the Auditor General, and is not intended to be and should not be used by anyone other than these specified parties.

Carri Riggs & Ingram, L.L.C.

Destin, Florida
December 15, 2005