

CITY OF SCRANTON, PENNSYLVANIA
STATUS OF CORRECTIVE ACTION AND PRIOR AUDIT FINDINGS

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INDEPENDENT AUDITORS' REPORT

October 6, 2006

The Honorable Members of the City Council of
the City of Scranton, Pennsylvania

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Scranton, Pennsylvania (the "City") as of and for the year ended December 31, 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 of Scranton management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the Sewer Authority of the City of Scranton, Pennsylvania (the "Sewer Authority") which statements reflect total assets of \$41,881,955 at March 31, 2005 and total revenues of \$10,572,969 for the year then ended; the Parking Authority of the City of Scranton, Pennsylvania (the "Parking Authority") which statements reflect total assets of \$31,613,984 at December 31 2005 and total revenues of \$1,677,990 for the year then ended; and the Redevelopment Authority of the City of Scranton (the "Redevelopment Authority") which statements reflect total assets of \$16,828,577 at December 31, 2005 and total revenues of \$447,190 for the year then ended. Those financial statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Sewer Authority and Parking Authority reflected in the City's Enterprise Funds and Redevelopment Authority reflected in the City's Aggregate Remaining Fund information, is based on the reports of the other auditors.

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

The City has determined its actuarial liability for its internal service workmen's compensation fund included in the aggregate remaining fund information at August 31, 2005 instead of December 31, 2005. Accounting principles generally accepted in the United States of America require that liabilities be valued as of the report date. The amount by which this departure would affect the liabilities, fund balance, and expenditures of the aggregate remaining fund information is not reasonably determinable.

In our opinion, except for the effects, if any, of not valuing its actuarial liability as of December 31, 2005 in the aggregate remaining fund information as described in the preceding paragraph, the financial statements referred to above present fairly, in all material respects, the respective financial position of the aggregate remaining fund information of the City of Scranton as of December 31, 2005, and the respective changes in financial position thereof for the year ended in conformity with accounting principles generally accepted in the United States of America.

In addition, in our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, business-type activities, general fund, special revenue fund OECD, special revenue fund special cities, capital projects fund, sewer authority and municipal parking authority of the City of Scranton as of December 31, 2005, and the respective changes in financial position and cash flows, where applicable, thereof for the year ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis and budgetary comparison information on pages 7 through 16 and 72 through 73 are not a required part of the basic financial statements but are supplementary information required by Accounting Principals Generally Accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquires 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 opinions on the financial statements that collectively comprise the City of Scranton's basic financial statements. The introductory section, combining and individual nonmajor fund financial statements are presented for purposes of additional analysis and are not a required part of the basic financial statements. 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 also not a required part of the basic financial statements of the City of Scranton. The combining and individual nonmajor fund financial statements and the schedule of expenditures of federal awards have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory section has not been subjected to the auditing procedures applied in the audit of the basic financial statements and accordingly, we express no opinion on them.

Management's Discussion and Analysis

As management of the City of Scranton, Pennsylvania, we offer readers of the City's financial statements this narrative overview and analysis of the financial activities of the City of Scranton for the fiscal year ended December 31, 2005. We encourage readers to review the information presented here in conjunction with additional information that we have furnished in the City's financial statements, which follow this narrative.

Financial Highlights

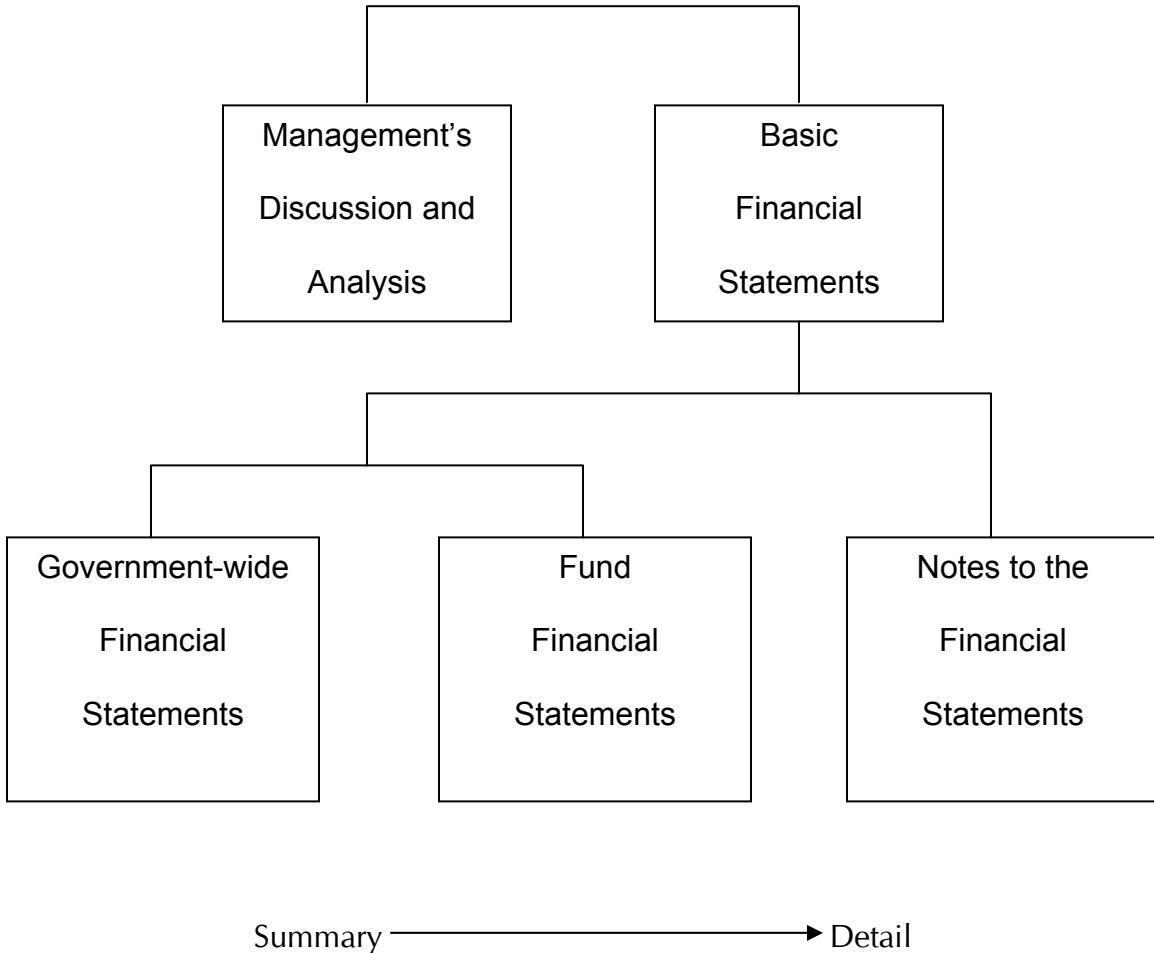
- The assets of the City exceeded its liabilities at the close of the fiscal year by \$23,115,779 (*net assets*).
- The government's total net assets increased by \$4,549,243.
- As of the close of the current fiscal year, the City's Governmental Funds reported combined ending fund balances of \$13,817,588, a decrease of \$13,656,447 in comparison with the prior year. The largest decrease was in the Reserve for Capital Projects of \$13,977,118. Approximately 33.50% of this total amount or \$4,632,566 is available for spending at the government's discretion (*unreserved fund balance*).
- At the end of the current fiscal year, unreserved fund balance for the General Fund was \$4,402,361, or 8.53% of total General Fund expenditures for the fiscal year.
- The City entered into a sublease and guarantee agreement with the Scranton Sewer Authority for the City's newly constructed Department of Public Works (DPW) complex. This transaction pumped \$5,432,500 into the City's General Fund at the end of 2005. The financing will be paid back over a three year period, concluding on December 15, 2008.
- The City of Scranton has a BBB bond rating from Standard and Poor's.

Overview of the Financial Statements

This discussion and analysis are intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements consist of three components; 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements (see Figure 1). The basic financial statements present two different views of the City through the use of government-wide statements and fund financial statements. In addition to the basic financial statements, this report contains other supplemental information that will enhance the reader's understanding of the financial condition of the City of Scranton.

Required Components of Annual Financial Report

Figure 1



Basic Financial Statements

The first two statements (pages 17 through 19) in the basic financial statements are the **Government-wide Financial Statements**. They provide both short and long-term information about the City's financial status.

The next statements (pages 20 through 32) are **Fund Financial Statements**. These statements focus on the activities of the individual parts of the City's government. These statements provide more detail than the government-wide statements. There are two parts to the Fund Financial Statements: 1) the governmental funds statements; and 2) the proprietary fund statements.

The next section of the basic financial statements is the **notes**. The notes to the financial statements explain in detail some of the data contained in those statements. After the notes, **supplemental information** is provided to show details about the City's individual funds. Budgetary information required by the General Statutes also can be found in this part of the statements.

Government-wide Financial Statements

The government-wide financial statements are designed to provide the reader with a broad overview of the City's finances, similar in format to a financial statement of a private-sector business. The government-wide statements provide short and long-term information about the City's financial status as a whole.

The statement of net assets presents the City's assets and liabilities as of the end of the recent fiscal year. The statement of activities shows the City's current year's revenue and expenses as soon as the changes occur, regardless of the timing of the related cash flows (on the accrual basis). Thus, revenue and expenses are reported in this statement for some items that will provide cash flow or use cash flow in a future period. An example of a cash inflow in the future would be when a taxpayer pays a prior year tax or fee in the future (see Taxes and Fees Receivable \$19,661,759). An example of a cash outflow in a future year would be the payment of prior year earned vacation pay (see Compensated Absences \$2,552,889). All major corporations use the accrual basis of accounting.

The government-wide financial statements include not only the City's financial information (Governmental Activities), and the Redevelopment Authority but also the financial information of the Sewer Authority, Municipal Parking Authority, and the Municipal Recreation Authority (Business-Type Activities). Financial information for these entities is reported in separate columns.

The government-wide financial statements are on pages 17 through 19.

Fund Financial Statements

A fund is a group of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City uses fund accounting so that its financial activities can be compared with other cities and governmental entities that use fund accounting. Fund accounting is required by the Governmental Accounting Standards Board (GASB). All of the funds of the City of Scranton, Pennsylvania can be divided into two categories: governmental funds and proprietary (fiduciary) funds.

Governmental Funds – Governmental funds are used to account for those functions reported as governmental activities in the government-wide financial statements. Most of the City's basic services are accounted for in governmental funds. These

funds focus on how assets can readily be converted into cash flow in and out, and what monies are left at year-end that will be available for spending in the next year. Because the focus of the governmental funds financial statements is narrower than that of the government wide financial statements, they are useful for comparing the information for governmental entities with similar information. By doing this readers may better understand the long-term impact of the City's near term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenue, expenditures and changes in fund balances provide a reconciliation to assist in this comparison between governmental funds and governmental activities.

The City of Scranton maintains individual government funds. Information in the governmental funds includes a balance sheet and a statement of revenues, expenditures, and changes in fund balances for the General Fund, OECD, the Capital Projects Fund, and the Redevelopment Authority Fund all of which are considered to be major funds. The data for non-major funds consisting of Liquid Fuels Fund, Special Cities Fund and Debt Service Fund are combined in a single accounting.

Enterprise Funds – The enterprise Funds are used for activities which are financed and operated in a manner similar to private business enterprise where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges, or where the governing body has decided that periodic determination of revenues earned, expenses incurred, or net income is appropriate for capital maintenance, public policy, management control, accountability or other purposes. These funds include the Sewer Authority, Parking Authority, and Recreation Authority. The Sewer Authority and Parking Authority are classified as major funds. The Recreation Authority is classified as a non-major fund.

Fiduciary Funds – Fiduciary funds are not accounted for in the government wide financial statements, because the resources of these funds are not available to support the City's own programs. These funds are custodial in nature.

Notes to the Financial Statements – The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements are on pages 33 through 71 of this report.

Other Information – This report includes certain other required supplementary information concerning the City, (see pages 72 through 73). A description of the schedules and reports can be found on pages 2 and 3 of the Table of Contents.

Government-Wide Financial Analysis

Net assets are useful indicators of a government's financial position. At the close of the current fiscal year, the City of Scranton's assets exceeded its liabilities by \$23,115,799.

Capital assets (land, buildings, roads, bridges and equipment) less any outstanding debt issued to acquire these assets comprise a significant portion of the City of Scranton's net assets, \$44,704,190. Although these capital assets assist the City in providing services to its citizens, they are generally not available to fund the operations of future periods.

A portion of the City's net assets, \$12,869,948, is subject to external restrictions as to how they may be used. The remaining component of net assets is the unrestricted net assets, which ended the year with a deficit of \$34,458,339. The governmental activities reported negative unrestricted net assets of \$42,349,762. The business type activities reported positive unrestricted net assets of \$7,891,423.

The City of Scranton, Pennsylvania's Net Assets

Figure 2

	City of Scranton Net Assets								
	Governmental			Business-Type			Total		
	Activities		%	Activities		%	Primary Government		%
	2005	2004	Change	2005	2004	Change	2005	2004	Change
Current Assets	109,375,899	117,782,761	-7.14%	9,076,572	9,422,735	-3.67%	118,452,471	127,205,496	-6.88%
Restricted Assets	172,000	279,551	-38.47%	7,126,938	11,788,429	-39.54%	7,298,938	12,067,980	39.52%
Capital Assets	47,292,337	36,451,594	29.74%	59,310,734	41,309,891	43.58%	106,603,071	77,761,485	37.09%
Deferred Charges	1,815,217	1,972,310	-7.96%	943,939	1,090,108	-13.41%	2,759,156	3,062,418	-9.90%
Total Assets	158,655,453	156,486,216	1.39%	76,458,183	63,611,163	20.20%	235,113,636	220,097,379	6.82%
Current Liabilities	(568,028)	5,591,499	110.16%	16,258,862	7,248,761	124.30%	15,690,834	12,840,260	22.20%
Non-Current Liabilities	169,533,623	163,852,603	3.47%	26,773,380	24,837,960	7.79%	196,307,003	188,690,563	4.04%
Total Liabilities	168,965,595	169,444,102	-0.28%	43,032,242	32,086,721	34.11%	211,997,837	201,530,823	5.19%
Net Assets:									
Invested in Capital assets net of related debt	23,060,794	30,424,920	-24.20%	21,643,396	17,972,908	20.42%	44,704,190	48,397,828	-7.63%
Restricted	8,978,826	14,365,525	-37.50%	3,891,122	2,274,325	71.09%	12,869,948	16,639,850	22.66%
Unrestricted	(42,349,762)	(57,748,331)	-26.66%	7,891,423	11,277,209	-30.02%	(34,458,339)	(46,471,122)	25.85%
Total Net Assets	(10,310,142)	(12,957,886)	-20.43%	33,425,941	31,524,442	6.03%	23,115,799	18,566,556	24.50%

City of Scranton, Pennsylvania Changes in Net Assets

Figure 3

	City of Scranton Changes in Net Assets								
	Governmental			Business-Type			Total		
	Activities		%	Activities		%	Primary Government		%
	2005	2004	Change	2005	2004	Change	2005	2004	Change
Revenues									
Program Revenues									
Fees, Fines & Charges for Services	8,602,281	9,820,128	-12.40%	12,250,959	11,290,914	8.50%	20,853,240	21,111,042	-1.22%
Operating Grants & Contributions	13,685,686	19,853,291	-31.07%	-	-	0.00%	13,685,686	19,853,291	-31.07%
Capital Grants & Contributions	3,381,861	6,941,658	-51.28%	-	-	0.00%	3,381,861	6,941,658	-51.28%
General Revenues									
Property Taxes	12,558,672	12,127,330	3.56%	-	-	0.00%	12,558,672	12,127,330	3.56%
Act 511 Taxes	26,215,395	23,401,485	12.02%	-	-	0.00%	26,215,395	23,401,485	12.02%
Grants, Subsidies & Contributions	-	165,146	-100.00%	-	-	0.00%	-	165,146	-100.00%
Cable TV Franchise Revenue	754,303	739,305	2.03%	-	-	0.00%	754,303	739,305	2.03%
Payments in Lieu of Taxes	116,000	129,666	-10.54%	-	-	0.00%	116,000	129,666	-10.54%
Investment Earnings	1,308,285	832,896	57.08%	257,855	225,965	14.11%	1,566,140	1,058,861	47.91%
Donations	63,000	-	100.00%	-	-	0.00%	63,000	-	100.00%
Sale of Property	21,494	-	100.00%	-	-	0.00%	21,494	-	100.00%
Miscellaneous	177,450	380,052	-53.31%	1,397,383	230,126	507.23%	1,574,833	610,178	158.09%
Rents & Concessions	2,710	3,417	-20.69%	-	-	0.00%	2,710	3,417	-20.69%
Grant Funds Loaned to Qualified Parties	-	515,000	-100.00%	-	-	0.00%	-	515,000	-100.00%
Casualty Gain	-	-	0.00%	23,829	-	0.00%	23,829	-	100.00%
Total Revenue & Transfers	66,887,137	74,909,374	-10.71%	13,930,026	11,747,005	18.58%	80,817,163	86,656,379	-6.74%
Expenses									
General Government & Administration	8,692,698	8,752,791	-0.69%	-	-	0.00%	8,692,698	8,752,791	-0.69%
Public Safety	30,763,622	31,312,815	-1.75%	-	-	0.00%	30,763,622	31,312,815	-1.75%
Public Works	8,612,927	11,018,525	-21.83%	-	-	0.00%	8,612,927	11,018,525	-21.83%
Health & Welfare	794,719	973,515	-18.37%	-	-	0.00%	794,719	973,515	-18.37%
Community Development	9,569,822	13,504,243	-29.13%	-	-	0.00%	9,569,822	13,504,243	-29.13%
Cultural & Recreation	1,129,283	1,023,315	10.36%	-	-	0.00%	1,129,283	1,023,315	10.36%
Other Expenditures	16,970	18,553	-8.53%	-	-	0.00%	16,970	18,553	-8.53%
Capital Expenditures	248,781	-	100.00%	-	-	0.00%	248,781	-	100.00%
Unallocated Depreciation	34,759	34,759	0.00%	-	-	0.00%	34,759	34,759	0.00%
Interest on Long Term Debt	4,375,812	4,049,448	8.06%	-	-	0.00%	4,375,812	4,049,448	8.06%
Sewer Authority	-	-	0.00%	10,270,198	10,285,602	-0.15%	10,270,198	10,285,602	-0.15%
Municipal Recreation Authority	-	-	0.00%	-	-	0.00%	-	-	0.00%
Municipal Parking Authority	-	-	0.00%	1,758,329	1,622,769	8.35%	1,758,329	1,622,769	8.35%
Total Expenses	64,239,393	70,687,964	-9.12%	12,028,527	11,908,371	1.01%	76,267,920	82,596,335	-7.66%
Change in Net Assets	2,647,744	4,221,410	-37.28%	1,901,499	(161,366)	-1278.38%	4,549,243	4,060,044	12.05%
Net Assets, Beginning of Year	(12,957,886)	(17,179,296)	-24.57%	31,524,442	31,685,808	-0.51%	18,566,556	14,506,512	27.99%
Net Assets, End of Year	(10,310,142)	(12,957,886)	-20.43%	33,425,941	31,524,442	6.03%	23,115,799	18,566,556	24.50%

Governmental activities. Governmental activities increased the City's net assets by \$2,647,744. The City's single greatest source of revenue is its Act 511 taxes. Act 511 taxes consist of the City's Wage Tax, Mercantile Tax and Occupational Privilege Tax. The City's Wage Tax is 2.4%. It is commonly incorrectly stated that the rate is 3.4%. The confusion is caused by the fact that the City's Wage Tax of 2.4% is collected along with the Scranton School District's 1% Wage Tax. The taxpayers make a single payment to the Scranton Collector of Taxes. The same collection system is used for the City and School Mercantile and Business Privilege Tax and thus the same type of confusion exists. The City's Mercantile and Business Privilege Tax rate is a flat .1% (.001) no matter what kind of business. The School District has three different rates. The wholesale business rate is .0452% (.00452), the retail rate is .0679% (.000679) and the service business rate is .513% (.00513) or more than five times the City rate.

Business-type activities: Business-type activities increased the City's assets by \$1,901,499. The largest item contributing to this increase was the \$1,807,933 realized by the Scranton Sewer Authority.

Financial Analysis of the City's Funds

Governmental Funds – The focus of the City's governmental funds is to provide information on near-term inflows, outflows, and balances of usable resources. Such information is useful in assessing the City's financing requirements. Specifically, unreserved fund balance can be a useful measure of a government's net resources available for spending at the end of the fiscal year.

The General Fund is the chief operating fund of the City. The General Fund total revenues were up \$2,325,997 from the prior year. Total General Fund Revenue was \$50,940,354 for the year 2005 versus \$48,614,356 for the year 2004. There was a \$1,428,617 increase in Wage Tax. Also, Real Estate Transfer Taxes increased by \$1,281,098. The General Fund expenditures for the year 2005 went up by \$2,519,179. Total General Fund Expenditures were \$51,587,141 for 2005 versus \$49,067,962 in 2004. The single largest increase in expenses was in Public Safety \$943,112. Also, there was a \$938,663 increase in general government expenses. Total Public Safety Expenditures were \$27,856,784 for 2005 versus \$26,913,672 for 2004.

At December 31, 2005, the Governmental Funds of the City of Scranton reported a combined fund balance of \$13,817,588, a 98.83% decrease over last year. A significant reason for the decrease in the combined fund balance is due to \$16,209,343 for capital expenditures in the Capital Projects Fund and Redevelopment Authority.

General Fund Budgetary Highlights

Revenues and other financing sources were higher than the budgeted amounts. Tax collections were greater than expected. Intergovernmental revenue was lower by

\$41,723. The primary reason was that the expected Cops Ahead Program revenue was \$200,000. The actual amount received was \$42,233. Departmental earnings were \$249,994 less than budgeted. The primary decrease was in money the City received from fines. The City budgeted \$857,500; it received \$705,603.

Other Financing Sources was \$1,031,693 greater than expected. The primary reason was that the budgeted lease proceeds were \$4,000,000. The amount actually received was \$5,500,000. This came from the City's sublease and guarantee agreement with the Scranton Sewer Authority and was used to pay for General Fund expenditures.

Expenditures and other financing uses were \$836,643 higher than budgeted. The main factor driving this large overage was employee benefits. They were \$206,204 higher than budgeted in General Government expenditures (\$2,406,182 budget vs. \$2,612,386 actual); \$672,031 higher than budgeted in Public Safety (\$12,828,767 budget vs. \$13,500,798 actual); and \$95,701 higher than budgeted in Public Works (\$1,553,434 budget vs. \$1,649,135 actual). Also, Professional Fees was \$209,000 higher than budgeted in General Government expenditures (\$649,043 budget vs. \$858,043 actual). Also, Equipment was \$238,806 higher than budgeted in Public Works expenditures (\$1,147,804 budget vs. \$1,386,610 actual).

Capital Assets

The City's capital assets consist of land and land improvements, buildings and building improvements, infrastructure (roads, sewers, etc.), furniture & equipment, vehicles and construction in progress. Also see Footnote numbers 5, 6 and 7 for additional information.

Figure 4

	City of Scranton Capital Assets (net of depreciation)						Total		
	Governmental Activities		Incr (Decr)	Business-Type Activities		Incr (Decr)	Primary Government		Incr (Decr)
	2005	2004		2005	2004		2005	2004	
Land & Land Improvements	4,317,506	5,776,298	(1,458,792)	1,033,322	1,307,338	(274,016)	5,350,828	7,083,636	(1,732,808)
Buildings & Building Improvements	16,594,144	10,882,774	5,711,370	101,801,353	87,344,389	14,456,964	118,395,497	98,227,163	20,168,334
Infrastructure	20,175,812	4,054,815	16,120,997	-	-	-	20,175,812	4,054,815	16,120,997
Furniture, Equipment & Vehicles	11,711,813	11,238,093	473,720	7,882,152	7,530,188	351,964	19,593,965	18,768,281	825,684
Construction in Progress	5,104,379	14,147,699	(9,043,320)	15,517,321	9,222,558	6,294,763	20,621,700	23,370,257	(2,748,557)
Accumulated Depreciation	(10,611,317)	(9,648,085)	(963,232)	(66,923,414)	(64,094,582)	(2,828,832)	(77,534,731)	(73,742,667)	(3,792,064)
Total	47,292,337	36,451,594	10,840,743	59,310,734	41,309,891	18,000,843	106,603,071	77,761,485	28,841,586

City of Scranton, Pennsylvania's Outstanding Debt

General Obligation and Revenue Bonds

Figure 5

	City of Scranton Long Term Debt					
	Governmental		Business-Type		Total	
	Activities		Activities		Primary Government	
	2005	2004	2005	2004	2005	2004
Balance January 1, 2005	94,920,800	80,985,968	26,141,504	12,698,107	121,062,304	93,684,075
Debt issued in 2005	6,084,449	16,295,000	2,462,981	19,394,874	8,547,430	35,689,874
Accretion & Amortization	27,664	23,467	-	-	27,664	23,467
Less Retirements	(2,490,144)	(2,383,636)	(779,078)	(5,951,477)	(3,269,222)	(8,335,113)
Balance December 31, 2005	98,542,769	94,920,799	27,825,407	26,141,504	126,368,176	121,062,303

The City of Scranton, Pennsylvania has a BBB bond rating from Standard and Poor's. Also, see footnote numbers 6 & 7 for additional information.

Pension Trust Fund

The City sponsors and administers three pension plans. The plans have been designated as severely distressed under Pennsylvania Act 205.

Internal Service Workmen's Compensation

The independent auditors qualified their opinion on the City's financial statements. This is due to the fact that the City determined its workers' compensation actuarial liability as of August 31, 2005 instead of December 31, 2005. This was also the case in 2004, and the City received a letter from the actuary addressing this concern. Therefore, the City of Scranton does not view this to be a material or significant issue.

Distressed Municipality Status

Since 1992, the City has been declared a distressed municipality by the Pennsylvania Department of Community and Economic Development. Over the past three years, the City has made significant progress in working to have this label removed. The fact that City has obtained a BBB rating from Standard & Poor's in 2003 is a sign that the City is truly on it's way to sound fiscal management. There

are many new business projects that the City is involved with in downtown Scranton. The City's Park System has also been revitalized.

Requests for Information

This report is designed to provide an overview of the City's finances for those with an interest in this area. Questions concerning any of the information found in this report or requests for additional information should be directed to Leonard Kresefski, Business Administrator, City Hall, 4th Floor, 340 N. Washington Avenue, Scranton, PA 18503.

**CITY OF SCRANTON, PENNSYLVANIA
INDEPENDENT AUDITORS' REPORT
DECEMBER 31, 2005**

CITY OF SCRANTON, PENNSYLVANIA
 GOVERNMENT WIDE STATEMENT OF NET ASSETS
 DECEMBER 31, 2005

ASSETS	PRIMARY GOVERNMENT		
	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTAL
Cash and Cash Equivalents	\$ 24,520,655	\$ 2,469,684	\$ 26,990,339
Certificate of Deposit	0	3,726,434	3,726,434
Investments	15,176,291	0	15,176,291
Receivables:			
Taxes and Fees Receivable, Net	19,661,759	0	19,661,759
Accounts Receivable, Net	2,046,520	2,250,777	4,297,297
Accrued Interest	140,340	115,718	256,058
Loans Receivable	44,072,018	0	44,072,018
Other Receivables, Net	925,398	0	925,398
Due From Other Funds	2,426,465	77,064	2,503,529
Prepaid Assets	0	44,236	44,236
Other Assets	188,426	392,659	581,085
Property Held For Resale	218,027	0	218,027
Restricted Assets:			
Restricted Cash and Cash Equivalents	172,000	2,969,468	3,141,468
Restricted Certificate of Deposit	0	2,554,307	2,554,307
Restricted Investments	0	1,173,528	1,173,528
Restricted Accounts Receivable	0	429,635	429,635
Capital Assets:			
Land	4,317,506	1,033,322	5,350,828
Buildings	11,937,008	101,492,308	113,429,316
Improvements	4,657,136	309,045	4,966,181
Infrastructure	20,175,812	0	20,175,812
Vehicles, Furniture & Equipment	11,711,813	7,882,152	19,593,965
Construction In Progress	5,104,379	15,517,321	20,621,700
Accumulated Depreciation	(10,611,317)	(66,923,414)	(77,534,731)
Deferred Charges, Net	1,815,217	943,939	2,759,156
TOTAL ASSETS	<u>\$ 158,655,453</u>	<u>\$ 76,458,183</u>	<u>\$ 235,113,636</u>

"See accompanying notes and independent auditors' report."

CITY OF SCRANTON, PENNSYLVANIA
 GOVERNMENT WIDE STATEMENT OF NET ASSETS
 DECEMBER 31, 2005

LIABILITIES	PRIMARY GOVERNMENT		
	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTAL
Short Term Debt	\$ 0	\$ 743,027	\$ 743,027
Accounts Payable	4,290,622	1,266,280	5,556,902
Accrued Liabilities	424,212	1,105,395	1,529,607
Accrued Interest	1,249,122	0	1,249,122
Due to Other Funds	(9,427,355)	11,930,884	2,503,529
Current Liabilities Payable From Restricted Assets:			
Revenue Bonds Payable	0	967,405	967,405
Lease Payable	293,876	0	293,876
General Obligation Bonds Payable	2,370,000	0	2,370,000
Governmental Notes Payable	231,495	0	231,495
Accrued Revenue Bond Interest Payable	0	245,871	245,871
Noncurrent Liabilities:			
Workers' Compensation Claims Payable	20,607,305	0	20,607,305
Deferred Revenues	53,646,145	0	53,646,145
Long-Term Debt Obligations	85,094,261	26,858,002	111,952,263
Deferred Loss On Early Retirement Of Debt	(2,480,860)	(643,589)	(3,124,449)
Governmental Notes Payable	856,069	0	856,069
Long-Term Liabilities Payable	0	119,713	119,713
Capitalized Lease Debt	9,697,068	0	9,697,068
Compensated Absences	2,113,635	439,254	2,552,889
	<u>\$ 168,965,595</u>	<u>\$ 43,032,242</u>	<u>\$ 211,997,837</u>
NET ASSETS			
Investment in Capital Assets, Net of Related Debt	\$ 23,060,794	\$ 21,643,396	\$ 44,704,190
Restricted for:			
Debt Service	2,096,925	0	2,096,925
Reserved for Capital Projects	6,476,612	0	6,476,612
Reserved for Retirement of Long-Term Obligations	405,289	3,891,122	4,296,411
Unreserved - Undesignated	(42,349,762)	7,891,423	(34,458,339)
	<u>\$ (10,310,142)</u>	<u>\$ 33,425,941</u>	<u>\$ 23,115,799</u>
	(10,310,142)	33,425,941	23,115,799

"See accompanying notes and independent auditors' report."

CITY OF SCRANTON, PENNSYLVANIA
GOVERNMENT WIDE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2005

PROGRAM ACTIVITIES	EXPENSES	PROGRAM REVENUES			NET (EXPENSES) REVENUE AND CHANGES IN NET ASSETS		
		FEES, FINES AND CHARGES FOR SERVICES	OPERATING GRANTS AND CONTRIBUTIONS	CAPITAL GRANTS AND CONTRIBUTIONS	GOVERNMENTAL ACTIVITIES	BUSINESS - TYPE ACTIVITIES	TOTAL
Governmental Activities							
General Government and Administration	\$ 8,692,698	\$ 815,545	\$ 405,915	\$ 0	\$ (7,471,238)	\$ 0	\$ (7,471,238)
Public Safety	30,763,622	819,753	2,647,061	0	(27,296,808)	0	(27,296,808)
Public Works	8,612,927	5,413,750	1,431,592	1,226,135	(541,450)	0	(541,450)
Health & Welfare	794,719	0	794,719	0	0	0	0
Community Development	9,569,822	1,508,346	8,398,933	2,066,665	2,404,122	0	2,404,122
Culture and Recreation	1,129,283	44,887	0	0	(1,084,396)	0	(1,084,396)
Other Expenditure	16,970	0	7,466	0	(9,504)	0	(9,504)
Capital Expenditures	248,781	0	0	89,061	(159,720)	0	(159,720)
Unallocated Depreciation	34,759	0	0	0	(34,759)	0	(34,759)
Interest on Long Term Debt	4,375,812	0	0	0	(4,375,812)	0	(4,375,812)
TOTAL GOVERNMENTAL ACTIVITIES	\$ 64,239,393	\$ 8,602,281	\$ 13,685,686	\$ 3,381,861	\$ (38,569,565)	\$ 0	\$ (38,569,565)
Business-Type Activities							
Sewer Authority	\$ 10,270,198	\$ 10,572,969	\$ 0	\$ 0	\$ 0	\$ 302,771	\$ 302,771
Municipal Parking Authority	1,758,329	1,677,990	0	0	0	(80,339)	(80,339)
TOTAL BUSINESS-TYPE ACTIVITIES	\$ 12,028,527	\$ 12,250,959	\$ 0	\$ 0	\$ 0	\$ 222,432	\$ 222,432
TOTAL GOVERNMENT	\$ 76,267,920	\$ 20,853,240	\$ 13,685,686	\$ 3,381,861	\$ (38,569,565)	\$ 222,432	\$ (38,347,133)
General Revenues:							
Property taxes, levied for general purposes					\$ 12,558,672	\$ 0	\$ 12,558,672
Act 511 Taxes					26,215,395	0	26,215,395
Cable Television Franchise Revenue					754,303	0	754,303
Payments in Lieu of Taxes					116,000	0	116,000
Investment Earnings					1,308,285	257,855	1,566,140
Miscellaneous					177,450	1,397,383	1,574,833
Casualty Gain					0	23,829	23,829
Rents and Concessions					2,710	0	2,710
Donations					63,000	0	63,000
Sale of Property					21,494	0	21,494
Total General Revenues and Transfers					\$ 41,217,309	\$ 1,679,067	\$ 42,896,376
Change in Net Assets					\$ 2,647,744	\$ 1,901,499	\$ 4,549,243
Net Assets, Beginning of Year					(12,957,886)	31,524,442	18,566,556
NET ASSETS, END OF YEAR					\$ (10,310,142)	\$ 33,425,941	\$ 23,115,799

"See accompanying notes and independent auditors' report."

CITY OF SCRANTON, PENNSYLVANIA
BALANCE SHEET
GOVERNMENTAL FUNDS
DECEMBER 31, 2005

	GENERAL	OECD	CAPITAL PROJECTS	REDEVELOPMENT AUTHORITY	NON-MAJOR FUNDS	TOTAL GOVERNMENTAL FUNDS
ASSETS						
Cash and Cash Equivalents	\$ 1,422,454	\$ 3,785,086	\$ 2,354,335	\$ 206,359	\$ 8,092,423	\$ 15,860,657
Investments	0	0	3,674,613	809,167	0	4,483,780
Taxes and Fees Receivable, Net	19,661,759	0	0	0	0	19,661,759
Accounts Receivable, Net	986,464	62,907	0	23,183	973,966	2,046,520
Accrued Interest	0	0	12,552	0	0	12,552
Loans Receivable	0	42,716,557	0	1,355,461	0	44,072,018
Other Receivables, Net	0	925,398	0	0	0	925,398
Due From Other Funds	459,175	0	1,368,985	0	44,234	1,872,394
Due From Other Governments	0	336,238	0	0	0	336,238
Prepaid Assets	0	0	0	0	0	0
Other Assets	0	188,427	0	0	0	188,427
Property Held for Resale	0	0	110,475	1,257,551	0	1,368,026
TOTAL ASSETS	<u>\$ 22,529,852</u>	<u>\$ 48,014,613</u>	<u>\$ 7,520,960</u>	<u>\$ 3,651,721</u>	<u>\$ 9,110,623</u>	<u>\$ 90,827,769</u>

"See accompanying notes and independent auditors' report."

CITY OF SCRANTON, PENNSYLVANIA
BALANCE SHEET
GOVERNMENTAL FUNDS
DECEMBER 31, 2005

	GENERAL	OECD	CAPITAL PROJECTS	REDEVELOPMENT AUTHORITY	NON-MAJOR FUNDS	TOTAL GOVERNMENTAL FUNDS
LIABILITIES AND FUND BALANCES						
LIABILITIES						
Accounts Payable	\$ 1,689,796	\$ 499,218	\$ 596,445	\$ 219,903	\$ 1,136,275	\$ 4,141,637
Accrued Liabilities	424,212	0	0	0	0	424,212
Other Current Liabilities	0	0	0	197,682	0	197,682
Due to Other Funds	1,269,299	151,600	447,903	0	298,489	2,167,291
Due to Other Governments				336,238	0	336,238
Deferred Revenues	<u>14,744,184</u>	<u>47,366,960</u>	<u>0</u>	<u>2,055,461</u>	<u>5,576,516</u>	<u>69,743,121</u>
TOTAL LIABILITIES	<u>\$ 18,127,491</u>	<u>\$ 48,017,778</u>	<u>\$ 1,044,348</u>	<u>\$ 2,809,284</u>	<u>\$ 7,011,280</u>	<u>\$ 77,010,181</u>
FUND BALANCES						
Reserve for Debt Service	\$ 0	\$ 0	\$ 0	\$ 84,053	\$ 2,096,925	\$ 2,180,978
Reserved for Capital Projects	0	0	6,476,612	527,432	0	7,004,044
Unreserved - Undesignated	<u>4,402,361</u>	<u>(3,165)</u>	<u>0</u>	<u>230,952</u>	<u>2,418</u>	<u>4,632,566</u>
TOTAL FUND BALANCES	<u>\$ 4,402,361</u>	<u>\$ (3,165)</u>	<u>\$ 6,476,612</u>	<u>\$ 842,437</u>	<u>\$ 2,099,343</u>	<u>\$ 13,817,588</u>
TOTAL LIABILITIES AND FUND BALANCES	<u>\$ 22,529,852</u>	<u>\$ 48,014,613</u>	<u>\$ 7,520,960</u>	<u>\$ 3,651,721</u>	<u>\$ 9,110,623</u>	<u>\$ 90,827,769</u>

"See accompanying notes and independent auditors' report."

CITY OF SCRANTON, PENNSYLVANIA
RECONCILIATION OF THE GOVERNMENTAL FUNDS
BALANCE SHEET TO STATEMENT OF NET ASSETS
DECEMBER 31, 2005

Total Fund Balance - Total Governmental Funds	\$	13,817,588
Amounts Reported for Governmental Activities in the statement of Net Assets are Different Because:		
Capital assets used in governmental activities are not financial resources and therefore are not reported as assets in governmental funds. The cost of the assets is \$ 57,903,654. and the accumulated depreciation is \$ 10,611,317..		47,292,337
Governmental funds report the effects of bond issuance cost when the debt is first issued, whereas these amounts are deferred and amortized .		1,815,217
Property taxes receivable will be collected but are not available soon enough to pay for the current period's expenditures and therefore are deferred in the fund.		10,199,217
Refuse fee receivable will be collected but are not available soon enough to pay for the current period's expenditures and therefore are deferred in the fund.		4,542,297
Internal service fund is used by management to charge the cost of the workmen's compensation insurance fund to various departments. The net revenue of the internal service fund is reported with governmental activities.		
Change in net assets is as follows:		
Cash and cash equivalents	\$	8,659,998
Investments		10,692,511
Accrued Interest		127,788
Due From Other Funds		217,833
Restricted Cash & Cash Equivalents		172,000
Accounts Payable		(148,985)
Workers' Compensation Claims Payable		<u>(20,607,305)</u>
Decrease In Net Assets		(886,160)
Deferred loans are loans made by SRA to qualified projects that will be repaid in future years but are not available soon enough to pay for the current period's expenditures and therefore are deferred in the funds.		1,355,462
Contribution of property from City to SRA held for resale by SRA eliminated and restated at original cost and net book value		(1,150,000)
Elimination of Lease Receivable/ Lease Payable Between Scranton Parking Authority and Scranton Redevelopment Authority and reporting of true outstanding debt		11,930,884
Long-Term liabilities are not due and payable in the current period and therefore are not reported as liabilities in the funds. Long-Term liabilities at year end consist of the following:		
General obligation bonds payable	\$	(87,464,261)
Governmental notes payable		(1,087,564)
Accrued interest payable		(1,051,440)
Capitalized Lease payable		(9,990,944)
Compensated absences		(2,113,635)
Deferred loss on early retirement of debt		<u>2,480,860</u>
Increase in Long Term Liabilities		<u>(99,226,984)</u>
Net Assets of Governmental Activities	\$	<u>(10,310,142)</u>

"See accompanying notes and independent auditors' report."

CITY OF SCRANTON, PENNSYLVANIA
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2005

	GENERAL	OECD	CAPITAL PROJECTS	REDEVELOPMENT AUTHORITY	NON-MAJOR FUNDS	TOTAL GOVERNMENTAL FUNDS
Revenues:						
Taxes	\$ 38,402,453	\$ 0	\$ 0	\$ 0	\$ 0	\$ 38,402,453
Intergovernmental	3,074,277	5,520,940	78,486	482,715	6,561,811	15,718,229
Departmental Earnings	1,772,506	0	0	0	76,534	1,849,040
Refuse Disposal Fee	4,756,101	0	0	0	0	4,756,101
Licenses and Permits	1,494,890	0	0	0	0	1,494,890
Cable Television Franchise Revenue	754,303	0	0	0	0	754,303
Payments in Lieu of Taxes	116,000	0	0	0	0	116,000
Investment Income	280,337	4,838	231,713	199,635	83,017	799,540
User Fee	44,887	0	0	0	0	44,887
Other Revenues	181,600	0	0	0	491,568	673,168
Rents and Concessions	0	0	0	2,710	0	2,710
Donations	63,000	0	0	0	0	63,000
Sale of Property	0	0	0	60,000	0	60,000
Program Income	0	942,304	0	0	0	942,304
Total Revenues	\$ 50,940,354	\$ 6,468,082	\$ 310,199	\$ 745,060	\$ 7,212,930	\$ 65,676,625
Expenditures:						
Current:						
General Government	\$ 12,260,593	\$ 0	\$ 0	\$ 0	\$ 267,486	\$ 12,528,079
Public Safety	27,856,784	0	0	0	0	27,856,784
Public Works	9,809,880	0	0	0	1,226,135	11,036,015
Health and Welfare	0	0	0	0	836,952	836,952
Community Development	507,407	6,493,865	0	401,099	2,192,323	9,594,694
Culture and Recreation	1,152,477	0	0	0	0	1,152,477
Other Expenditures	0	0	8,139	1,365	7,466	16,970
Debt Service						
Debt Service-Principal	0	0	0	226,859	2,182,424	2,409,283
Debt Service-Interest	0	0	0	317,023	3,515,480	3,832,503
Capital Outlay	0	0	7,692,944	8,516,399	0	16,209,343
Total Expenditures	\$ 51,587,141	\$ 6,493,865	\$ 7,701,083	\$ 9,462,745	\$ 10,228,266	\$ 85,473,100
Excess (Deficiency) of Revenues Over Expenditures	\$ (646,787)	\$ (25,783)	\$ (7,390,884)	\$ (8,717,685)	\$ (3,015,336)	\$ (19,796,475)

"See accompanying notes and independent auditors' report."

CITY OF SCRANTON, PENNSYLVANIA
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2005

	GENERAL	OECD	CAPITAL PROJECTS	REDEVELOPMENT AUTHORITY	NON-MAJOR FUNDS	TOTAL GOVERNMENTAL FUNDS
Other Financing Sources (Uses):						
Lease Proceeds	\$ 5,832,247	\$ 0	\$ 0	\$ 0	\$ 0	\$ 5,832,247
Proceeds From Tax Anticipation Note	8,999,950	0	0	0	0	8,999,950
Operating Transfers In	1,534,313	0	1,776,304	0	5,276,472	8,587,089
Operating Transfers Out	(5,887,364)	0	(36,404)	0	(2,663,321)	(8,587,089)
Bond Issuance Cost Relative to Capitalizing Lease	(67,500)	0	0	0	0	(67,500)
Proceeds From Advance Refunding	0	0	0	0	495,557	495,557
Repayment of Tax Anticipation Note	(9,120,227)	0	0	0	0	(9,120,227)
Net Other Financing Sources (Uses)	<u>\$ 1,291,419</u>	<u>\$ 0</u>	<u>\$ 1,739,900</u>	<u>\$ 0</u>	<u>\$ 3,108,708</u>	<u>\$ 6,140,027</u>
Excess (Deficiency) of Revenues and Other Financing Sources Over Expenditures and Other Financing Uses	\$ 644,632	\$ (25,783)	\$ (5,650,984)	\$ (8,717,685)	\$ 93,372	\$ (13,656,448)
Fund Balances, Beginning of Year	<u>3,757,729</u>	<u>22,618</u>	<u>12,127,596</u>	<u>9,560,122</u>	<u>2,005,971</u>	<u>27,474,036</u>
FUND BALANCES, END OF YEAR	<u>\$ 4,402,361</u>	<u>\$ (3,165)</u>	<u>\$ 6,476,612</u>	<u>\$ 842,437</u>	<u>\$ 2,099,343</u>	<u>\$ 13,817,588</u>

"See accompanying notes and independent auditors' report."

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 1 - Summary of Significant Accounting Policies

The City complies with generally accepted accounting principles (GAAP). GAAP includes all relevant Governmental Accounting Standards Board (GASB) pronouncements. In the government-wide financial statements and the fund financial statements for the proprietary funds, Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, have been applied unless those pronouncements conflict with or contradict GASB pronouncements, in which case, GASB prevails. The accounting and reporting framework and the more significant accounting policies are discussed in subsequent subsections of this Note.

Reporting Entity: The City of Scranton, Pennsylvania (the "City") was incorporated in 1866 under the provisions of the constitution and general statutes of the Commonwealth of Pennsylvania. The City is a class 2A city, as defined by the state statutes. The City operates under a mayor-council form of government and provides the following services: public safety, roads, sanitation, health, culture and recreation, and general government services.

The City has evaluated its relationship with the following organizations to determine if these organizations should be included in the annual government-wide and fund-financial statements of the City.

Sewer Authority of the City of Scranton, Pennsylvania
Parking Authority of the City of Scranton, Pennsylvania
Scranton Municipal Recreation Authority
Redevelopment Authority of the City of Scranton
Scranton Housing Authority
Scranton School District
Scranton Lackawanna Health and Welfare Authority
Municipal Industrial Development Authority of Scranton
Joint Zoo Authority of the City of Scranton and the County of Lackawanna
Scranton Public Library
Single Tax Office

As required by Governmental Accounting Standards Board Statements No. 14, these entities have been placed in one of the following categories:

- 1) Component Unit - A legally separate organization for which elected officials of the City are financially accountable. This type of entity may then be reported in one of the two following manners:

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 1 Summary of Significant Accounting Policies (Continued)

Discrete presentation - Financial data for the component unit is presented in a column separate from that of the City's financial data. There is no such presentation included in the City's government wide and fund financial statements.

Blended presentation - Financial data for the component unit is presented in the same manner as that of the City's financial data and is reported as part of the City's financial operations.

- 2) Joint Venture - A legal entity or other organization resulting from a contractual arrangement that is owned, operated or governed by two or more participants as a separate and specific activity subject to joint control, in which the participants retain an ongoing financial interest or an ongoing financial responsibility. There are no such entities included in the City's reporting entity.
- 3) Related Organization - An organization for which the City is not financially accountable even though the City appoints a voting majority of the organization's governing board.

The criteria used to determine how these organizations should be categorized in the government-wide and fund-financial statements of the City were: a) financial interdependency; b) selection of governing authority; c) designation of management; d) ability to significantly influence operations; e) accountability for fiscal matters; f) scope of public service; and g) special financing relationships.

As a result of applying these criteria, the following organizations have been categorized and determined to be and are presented as blended component units for the year ended December 31, 2005.

Sewer Authority of the City of Scranton, Pennsylvania: The Sewer Authority of the City of Scranton, Pennsylvania (the "Sewer Authority") owns the sewer system that provides waste water treatment services to the City and nearby communities. The City appoints all Sewer Authority members and guarantees its bonded debt and approves all rates. The Sewer Authority reports its financial position and its operating activities on a fiscal year of April 1 to March 31. The amounts included in the accompanying government-wide and fund-financial statements for the Sewer Authority reflects its operating results for its fiscal year of April 1, 2004 to March 31, 2005.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 1 Summary of Significant Accounting Policies (Continued)

Parking Authority of the City of Scranton, Pennsylvania: The Parking Authority of the City of Scranton, Pennsylvania (the "Parking Authority") operates parking facilities within the City. The City appoints all Parking Authority members and the City guarantees its bonded debt.

Scranton Municipal Recreation Authority: The Scranton Municipal Recreation Authority (the "Recreation Authority") operated the City's municipal golf course. The City appoints all Recreation Authority members and guaranteed its debt.

Redevelopment Authority of the City of Scranton: The Redevelopment Authority of the City of Scranton (the "Redevelopment Authority") operates for the purpose of promoting the elimination of blighted areas by declaring acquisition, sound replanning and redevelopment of such areas to be for the promotion of health, safety, convenience, and welfare for the general public good, through contract with private redevelopers and public authorities for redevelopment. The City appoints all Redevelopment Authority members and assigned repayment on seven loans receivable related to Urban Development Action Grants, Enterprise Development Zone Grants, and Commercial Industrial Loans toward repayment of the Redevelopment Authority's debt and is financially dependent upon the city.

To obtain individual financial statements for any of the above-mentioned entities, individuals should contact the administrative office of each specific entity.

BASIS OF PRESENTATION

Government-wide Financial Statements: The Statement of Net Assets and Statement of Activities display information about the reporting government as a whole. They include all funds of the reporting entity except for fiduciary funds. The statements distinguish between governmental and business-type activities. Governmental activities generally are financed through taxes, intergovernmental revenues, and other nonexchange revenues. Business-type activities are financed in whole or in part by fees charged to external parties for goods or services.

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

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 1 Summary of Significant Accounting Policies (Continued)

Fund Financial Statements: Fund financial statements of the reporting entity are organized into funds, each of which is considered to be separate accounting entities. Each fund is accounted for by providing a separate set of self-balancing accounts that constitute its assets, liabilities, fund equity, revenues, and expenditure/expenses. Funds are organized into three major categories: governmental, proprietary, and fiduciary. An emphasis is placed on major funds within the governmental and proprietary categories. A fund is considered major if it is the primary operating fund of the City or meets the following criteria:

- a. Total assets, liabilities, revenues, or expenditures/expenses of that individual governmental or enterprise fund are at least 10 percent of the corresponding total for all funds of that category or type; and
- b. Total assets, liabilities, revenues, or expenditures/expenses of the individual governmental fund or enterprise fund are at least 5 percent of the corresponding total for all governmental and enterprise funds combined.

The funds of the financial reporting entity are described below:

- 1) Governmental Fund Types
 - a) The General Fund is the general operating fund of the City and is always classified as a major fund. It accounts for all revenues and expenditures of the City not encompassed within other funds. All general tax revenues and other receipts that are not allocated by law or contractual agreement to some other fund are accounted for in the fund. General operating expenditures and the capital improvement costs that are not paid through other funds are paid from the General Fund.
 - b) Special Revenue Funds are utilized to account for proceeds of specific revenue sources (other than expendable trusts or major capital projects) used to finance specific activities as required by law or administrative regulation. The following funds included in the accompanying government-wide and fund-financial statements are accounted for as Special Revenue Funds: Special City, Liquid Fuels, Office of Economic and Community Development (OECD), and Redevelopment Authority of the City of Scranton.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 1 Summary of Significant Accounting Policies (Continued)

The Redevelopment Authority of the City of Scranton and OECD are classified as major funds. Liquid Fuels and Special Cities are classified as non-major funds.

- c) Debt Service Fund is used to account for the accumulation of financial resources for the payment of principal, interest, and related costs on general long-term debt. The fund balance of the Debt Service Fund is reserved to signify the amounts are restricted exclusively for Debt Service Expenditure, and is classified as a non-major fund.
- d) Capital Project Fund is used to account for the acquisition or construction of capital facilities being financed from general obligation bond proceeds, or transfers from other funds and is classified as a major fund.

2. Proprietary Fund Types:

- a) Internal Service Funds: The Internal Service Fund is used to account for the financing of goods or services provided by one department to other departments on a cost reimbursement basis. The City accounts for its self-insurance of worker's compensation claims in this fund. These are Proprietary Funds reported within governmental activities in the government-wide financial statements.
- b) Enterprise Funds: The enterprise Funds are used for activities which are financed and operated in a manner similar to private business enterprise where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges, or where the governing body has decided that periodic determination of revenues earned, expenses incurred, or net income is appropriate for capital maintenance, public policy, management control, accountability or other purposes. These funds include the Sewer Authority, Parking Authority, and Recreation Authority.

The Sewer Fund and Parking Authority are classified as major funds. The Recreation Authority is classified as a non-major fund.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 1 Summary of Significant Accounting Policies (Continued)

Proprietary funds distinguish operating revenues and expenses from non-operating 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. Operating expenses from the proprietary funds include the cost of personal and contractual services, supplies and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

- c) Fiduciary Fund Type: Fiduciary Funds are used to account for assets held by the City in a trustee capacity or an agent for individuals, private organizations, other governmental units and/or other funds. The Pension Trust Funds consist of the Police Pension Fund, Firemen Pension Fund, and Nonuniformed Pension Fund. These funds are accounted for within a single aggregate fund.

Management Focus and Basis of Accounting. The government-wide statements report using the economic resource measurement focus and the accrual basis of accounting generally including the reclassification or elimination of internal activity (between or within funds). Reimbursements are reported as reductions to expenses. Proprietary and fiduciary fund financial statements and financial statements of City component units also report using this same focus and basis of accounting although internal activity is not eliminated in these statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property tax revenues are recognized in the year for which they are levied while grants are recognized when grantor eligibility requirements are met.

Pension trust funds recognize employer and participant contributions in the period in which contributions are due and the City has made a formal commitment to provide the contributions. Retirement benefits and refunds are recognized when due and payable in accordance with the term of the plan.

Governmental fund financial statements report using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized when they are both measurable and available. Available means collectible within the current period or soon enough thereafter to pay current liabilities. The City considers revenues to be available if they are collected within 60 days of the end of the calendar year. Expenditures are recorded when the related fund liability is incurred except for general obligation bond principal and interest which are reported as expenditures in the year due.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 1 Summary of Significant Accounting Policies (Continued)

Major revenue sources susceptible to accrual include: Act 511 Taxes, property taxes, refuse disposal fee, intergovernmental revenues, and investment income. In general, other revenues are recognized when cash is received.

Operating income reported in proprietary fund financial statements includes revenues and expenses related to the primary, continuing operations of the fund. Principal operating revenues for proprietary funds are charges to customers for sales or services. Principal operating expenses are the costs of providing goods or services and include administrative expenses and depreciation of capital assets. Other revenues and expenses are classified as non-operating in the financial statements.

The City reports deferred revenue on its government-wide and fund financial balance sheet. Deferred revenues arise when potential revenues do not meet both the "measurable" and "available" criteria for recognition in the current period. Deferred revenues also arise when resources are received by the City before it has a legal claim to them, as when grant monies are received prior to the incurring of qualifying Expenditures. In subsequent periods, when both revenue recognition criteria are met, or when the City has a legal claim to the resources, the liability for deferred revenue is removed from the balance sheet and revenue is recognized.

Budgetary Process: The City follows these procedures in developing the budgetary data reflected in the accompanying financial statements:

The preparation of the annual operating budget begins by September 15 for the subsequent budget year. By November 15, the Mayor submits to City Council a proposed budget for the General Fund for the fiscal year commencing January 1. City Council publishes, in one or more newspapers of general circulation within the City, a summary of the budget and a notice that the budget is available for public inspection. A public hearing takes place by December 1, at which time City Council may adopt the budget with or without amendment. In amending the budget, City Council may delete, increase or decrease programs or amounts, except for expenditures required by law or for debt service. If a change in a program or a budgetary item exceeds 10% of the Mayor's proposed budget, another public hearing must take place within 72 hours to justify the change. In no case can an amendment increase authorized expenditures to an amount greater than total estimated funds available. City Council must adopt an annual budget by December 15. If City Council fails to adopt a budget by December 15, the Mayor's proposed budget becomes the official budget for the City for the ensuing year.

Cash, Cash Equivalents and Investments: For purposes of the statement of cash flows, the Proprietary Fund considers all highly liquid investments (including restricted assets) with an original maturity of three months or less when purchased.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 1 Summary of Significant Accounting Policies (Continued)

Investments: City investments are stated at fair value based on quoted market prices. Fair value is the amount at which a financial investment could be exchanged in a current transaction between willing parties.

Real Estate Taxes: Real Estate Taxes are based upon assessed valuations provided by Lackawanna County, the elected tax collector bills and collects real estate taxes. The assessed value at January 1, 2005, upon which the 2005 levy was based, was approximately \$387 million. Delinquent taxes are collected by an outside collection agency. The schedule for real estate taxes levied is as follows:

February 1	Original levy date
February 1 - March 1	2 1/2% discount period
March 1 - April 30	2% discount period
May 1 - June 30	Face payment period
July 1 - January 15	10% penalty period
January 16	Lien date

In addition, City taxes may be paid in four installments in which the first two quarterly payments aggregating 50% of the face amount are due by June 30. The third and fourth quarterly payments are due on August 31 and October 31, respectively. Any delinquent installment is subject to a penalty of 10%.

The millage rate at January 1, 2005 was 82.122 mills on the assessed value of land and 17.86 mills on the assessed value of improvements.

Real Estate Taxes Receivable: The City utilizes the reserve method for writing off uncollectible real estate taxes.

Allowance for Doubtful Accounts: Accounts Receivable included in the Enterprise Fund represent amounts outstanding from Sewer Authority customer's reported net of an allowance for doubtful accounts of \$1,300,000 at December 31, 2005. The Authority's policy for providing for uncollectible accounts is to charge current year earnings for accounts receivable considered currently uncollectible, based on the historical collection experience of the Sewer Authority and collection percentages applicable to public utilities.

A major portion of the allowance for doubtful accounts is felt to be collectible in future years because of the Authority's power to convert past due accounts into municipal claims. This procedure is an operation of law and the claims have the status of a legal lien or judgment. There are currently in force municipal claims of approximately two million dollars.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 1 Summary of Significant Accounting Policies (Continued)

The Parking Authority utilizes the direct write off method and historically they have been immaterial to the financial statements.

Loans Receivable: Loans receivable consist of economic development loans to third parties that are administered by OECD and the Redevelopment Authority. Most of these loans bear interest, usually at a very low rate. These loans receivable, are reported at the gross principal outstanding. The outstanding loans are considered deferred revenue until collection of the principal is received, Interest income is recorded when received.

Interfund Receivables and Payables: During the course of operations, numerous transactions occur between individual funds that may result in amounts owed between funds. Those related to goods and services type transactions are classified as "due to and from other funds". Short-term interfund loans are reported as "interfund receivables and payables". Long-term interfund loans (noncurrent portion) are reported as "advances from and to other funds". Interfund receivables and payables between funds within governmental activities are eliminated in the Statement of Net Assets.

Grant Funds are considered to be earned to the extent of expenditures made under the provision of the grant and, accordingly, when such funds are received they are recorded as deferred revenues until earned.

Fixed Assets: The accounting treatment over property, plant, and equipment (fixed assets) depends on whether the assets are used in governmental fund operations or proprietary fund operations and whether they are reported in the government-wide or fund financial statements.

Government-wide Statements

In the government-wide financial statements, fixed assets are accounted for as capital assets. All fixed assets are valued at historical cost, or estimated historical cost if actual is unavailable, except for donated fixed assets which are recorded at their estimated fair value at the date of donation. Estimated historical cost was used to value the majority of the assets acquired prior to December 31, 2002.

Depreciation of all exhaustible fixed assets is recorded as an expense in the Statement of Activities, with accumulated depreciation reflected in the Statement of Net Assets. Depreciation is provided over the assets' estimated useful lives using the straight-line method of depreciation. The range of estimated useful lives by type of asset is as follows:

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 1 Summary of Significant Accounting Policies (Continued)

	Sewer Authority Useful Life	Parking Authority Useful Life
Building and Building Improvements		10-50 years
Sewer treatment plant	40 years	
Land improvements	10 years	10-15 years
Operating equipment	10 years	3-10 years
Vehicles	3- 6 years	
Extraordinary repairs:		
Sewer system	20 years	
Equipment	5 years	
	Redevelopment Authority Useful Life	Governmental Funds
Equipment	15 years	
Building and Building Improvements		20-50 years
Land Improvements		10-15 years
Operating Equipment		05-07 years
Vehicles		08-15 years

GASBS No. 34 requires the City to report and depreciate new infrastructure assets effective with implementation of GASB-34. Infrastructure assets include roads, bridges, underground pipe (other than related utilities), traffic signals, etc. These infrastructure assets are likely to be the largest asset class of the City. Neither their historical cost nor related depreciation has historically been reported in the financial statements. The retroactive reporting of infrastructure is subject to an extended implementation period and is first effective for fiscal years ending in 2007. The City hopes to implement the retroactive infrastructure provisions in the fiscal year ending December 31, 2007.

Fund Financial Statements

In the fund financial statements, fixed assets used in governmental fund operations are accounted for as capital outlay expenditures of the governmental fund upon acquisition. Fixed assets used in proprietary fund operations are accounted for the same as in the government-wide statements.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 1 Summary of Significant Accounting Policies (Continued)

Long-term Debt

The accounting treatment of long-term debt depends on whether the assets are used in governmental fund operations or proprietary fund operations and whether they are reported in the government-wide or fund financial statements.

All long-term debt to be repaid from governmental and business-type resources are reported as liabilities in the government-wide statements. The long-term debt consists primarily of notes payable and accrued compensated absences.

Long-term debt for governmental funds is not reported as liabilities in the fund financial statements. The debt proceeds are reported as other financing sources and payment of principal and interest reported as expenditures. The accounting for proprietary fund is the same in the fund statements as it is in the government-wide statements.

Bond issuance cost in the Government-wide and Proprietary are amortized over the terms of the respective bonds using the straight line method. Bond discounts, premium, the reacquisition price, and the net carrying value of refunded debt are capitalized and amortized over the terms of the respective bonds using a method that approximates the effective interest method.

The Government Fund Financial Statements recognizes the proceeds of debt and premiums as other financing sources of the current period. Issuance costs are reported as expenditures.

Government-wide Statements

Equity is classified as net assets and displayed in three components:

- a. Invested in capital assets, net of related debt-Consists of capital assets including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.
- b. Restricted net assets-Consists of net assets with constraints placed on the use either by (1) external groups such as creditors, grantors, contributors, or laws or regulations of other governments; or (2) law through constitutional provisions or enabling legislation.
- c. Unrestricted net assets-all other net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt."

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 1 Summary of Significant Accounting Policies (Continued)

Governmental fund equity is classified as fund balance. Fund balance is further classified as reserved and unreserved, with unreserved further split between designated and undesignated. Proprietary fund equity is classified the same as in the government-wide statements.

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.

Compensated Absences: The City's vacation policy generally provides that unused vacation benefits lapse at year-end. Unused vacation may be carried over only with the approval of the department head. Unused sick pay accumulates to varying maximum amounts for the various classes of City employees. At December 31, 2005 aggregate liability for unused vacation and sick pay is \$2,113,635.

Note 2 Cash and Cash Equivalents and Investments

Pennsylvania Statutes provide for investment of governmental funds into certain authorized investment types including U. S. Treasury bills, other short-term U.S. and Commonwealth of Pennsylvania government obligations and insured or collateralized time deposits and certificates of deposit. The statutes do not prescribe regulations related to demand deposits; however, they do allow the pooling of Governmental Funds for investment purposes.

The deposit policy of the City adheres to state statutes. Deposits of the City are either maintained in demand deposits or invested in certificates of deposit.

Custodial Credit Risk

Custodial credit risk is the risk that, in the event of a bank failure, the government's deposits may not be returned to it. The government does not have a deposit policy for custodial credit risk. As of December 31, 2005, \$41,723,693 of the government's bank balance of \$43,048,007 was exposed to custodial credit risk as follows:

Uninsured and uncollateralized	\$ 8,831,998
Uninsured and collateral held by pledging banks' trust department not in the city's name	<u>32,891,695</u>
Total	<u>\$ 41,723,693</u>

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 2 Cash and Cash Equivalents and Investments (Continued)

As of December 31, 2005, the City had the following investments:

Types of Investments	Fair Value/ Carrying Amount	Cost	Average Credit Quality/ Ratings (1)	Weighted Average Months To Maturity (2)
GOVERNMENTAL FUNDS				
Primary Government:				
Internal Service Fund				
Corporate Obligations:				
Domestic	\$ 974,400	\$ 974,400	A 2	22.80
Domestic	584,432	584,432	A 3	21.38
Domestic	50,074	50,074	Aa 1	14.33
Domestic	1,982,945	1,982,945	Aa 2	19.72
Domestic	1,052,406	1,052,406	Aa 3	28.12
Domestic	2,246,474	2,246,474	Aaa	17.18
Governmental Securities:				
Federal Agency Bonds	1,922,500	1,922,500	Aaa	38.07
Federal Agency Notes	<u>1,879,280</u>	<u>1,879,280</u>	Aaa	59.33
Total Internal Service Fund	<u>\$10,692,511</u>	<u>\$10,692,511</u>		
Capital Projects				
Governmental Securities:				
U.S. Treasury Notes	<u>\$ 3,674,613</u>	<u>\$ 3,674,613</u>	N/A	23.14
Total Capital Projects	<u>\$ 3,674,613</u>	<u>\$ 3,674,613</u>		
TOTAL PRIMARY GOVERNMENT	<u>\$14,367,124</u>	<u>\$14,367,124</u>		
Component Units:				
Redevelopment Authority				
Governmental Securities:				
U.S. Treasury backed money market funds	<u>\$ 809,167</u>	<u>\$ 809,167</u>	N/A	N/A
Total Redevelopment Authority	<u>\$ 809,167</u>	<u>\$ 809,167</u>		
TOTAL GOVERNMENTAL FUNDS	<u>\$15,176,291</u>	<u>\$15,176,291</u>		

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 2 Cash and Cash Equivalents and Investments (Continued)

BUSINESS TYPE ACTIVITIES

Parking Authority

Governmental Securities:

U.S. Government Obligations	<u>\$ 1,173,528</u>	<u>\$ 1,173,528</u>	N/A	N/A
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TOTAL BUSINESS TYPE ACTIVITIES	<u>\$ 1,173,528</u>	<u>\$ 1,173,528</u>		
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TOTAL INVESTMENTS	<u>\$16,349,819</u>	<u>\$16,349,819</u>		
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Fiduciary Funds

Pension Trust Fund

Mutual Funds

Equity Funds	\$53,005,735	\$53,005,735	N/A	N/A
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Bond Funds	<u>19,461,059</u>	<u>19,461,059</u>	N/A	N/A
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Total Pension Trust Fund	<u>\$72,466,794</u>	<u>\$72,466,794</u>		
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The Composition of pension trust fund is shown in the following table.

	Police Pension	Firemen Pension	Non-Uniform Pension	Total
Mutual Funds				
Fixed Income Fund	\$ 873,510	\$ 2,671,850	\$ 187,271	\$ 3,732,631
Diversified Bond Fund	10,695,362	7,887,164	878,533	19,461,059
Small Cap Value Fund	4,563,358	3,275,496	424,084	8,262,938
Large Cap Value Fund	7,555,251	6,009,656	756,165	14,321,072
Small Cap Growth Fund	3,828,267	2,731,141	401,269	6,960,677
Large Cap Growth Fund	6,725,449	4,798,034	923,923	12,447,406
International Value Fund	<u>3,601,707</u>	<u>3,083,068</u>	<u>596,236</u>	<u>7,281,011</u>
Total	<u>\$37,842,904</u>	<u>\$30,456,409</u>	<u>\$ 4,167,481</u>	<u>\$72,466,794</u>

(1) Ratings are provided where applicable to indicate associated Credit Risk. N/A indicates not applicable.

(2) Interest Rate Risk is estimated weighted average months to maturity.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 2 Cash and Cash Equivalents and Investments (Continued)

The City does not have a formal investment policy. Investments are measured through an investment advisor.

Credit Risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation.

Interest Rate Risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Investments held for longer periods are subject to increased risk of adverse interest rate changes. To extent practical, investments are matched with anticipated cash flows.

Concentration of Credit Risk is the risk of loss attributed to the magnitude of the City's investments in a single issuer.

For investments, custodial credit risk is the risk that in the event of the failure of the counterparty the City will not be able to recover the value of its investments or collateral securities in the possession of an outside party.

Note 3 Taxes and Fees Receivable

Taxes and fees receivable in the General Fund consist of the following at December 31, 2005:

Current real estate taxes	\$ 377,321
Delinquent real estate taxes	12,454,868
Act 511 taxes:	
Earned Income	3,844,126
Occupational privilege	31,262
Business privilege/mercantile	63,194
Delinquent refuse disposal fee	<u>5,745,608</u>
Total	\$22,516,379
 Less allowance for uncollectible taxes and fees	 <u>(2,854,620)</u>
 Net	 <u>\$19,661,759</u>

Of the above, the receivables not expected to be collected within one year are \$9,090,000 delinquent real estate taxes and \$3,883,000 delinquent refuse disposal fee.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 4 Due From and Due to Other Funds

A summary of the total amounts due from and due to other funds, by fund, at December 31, 2005 is as follows:

	<u>Due From Other Funds</u>	<u>Due To Other Funds</u>
General Fund	\$ 459,175	\$ 1,269,299
Special Revenue Funds,		
OECD	336,238	151,600
Special City	44,234	298,489
Redevelopment Authority	0	336,238
Internal Source Fund	217,833	0
Capital Projects Fund	1,368,985	447,903
Enterprise Funds,		
Parking Authority	77,064	0
Total	<u>\$ 2,503,529</u>	<u>\$ 2,503,529</u>

Note 5 Capital Assets

Capital asset activity for the year ended December 31, 2005 was as follows:

	<u>Balance at January 1, 2005</u>	<u>Additions</u>	<u>Disposals</u>	<u>Balance at December 31, 2005</u>
Governmental Activities:				
Capital assets not being depreciated				
Land	\$ 4,317,506	\$ 0	\$ 0	\$ 4,317,506
Construction in Progress	14,147,699	2,393,091	(11,436,411)	5,104,379
Total Capital Assets Not Being Depreciated	<u>\$ 18,465,205</u>	<u>\$ 2,393,091</u>	<u>\$ (11,436,411)</u>	<u>\$ 9,421,885</u>
Capital assets being depreciated				
Building	\$ 8,382,008	\$ 3,555,000	\$ 0	\$ 11,937,008
Land & Building Improvements	3,959,558	697,578	0	4,657,136
Infrastructure	4,054,815	16,120,997	0	20,175,812
Vehicles, Furniture & Equipment	11,238,093	1,351,581	(877,861)	11,711,813
Total Capital Assets being Depreciated	<u>\$ 27,634,474</u>	<u>\$ 21,725,156</u>	<u>\$ (877,861)</u>	<u>\$ 48,481,769</u>
Totals at Historical Cost	<u>\$ 46,099,679</u>	<u>\$ 24,118,247</u>	<u>\$ (12,314,272)</u>	<u>\$ 57,903,654</u>
Less: Accumulated Depreciation				
Building	\$ (2,592,609)	\$ (216,164)	\$ 0	\$ (2,808,773)
Land & Building Improvements	(388,220)	(347,343)	0	(735,563)
Infrastructure	(226,277)	(468,289)	0	(694,566)
Vehicles, Furniture & Equipment	(6,440,979)	(766,641)	835,205	(6,372,415)
Total Accumulated Depreciation	<u>\$ (9,648,085)</u>	<u>\$ (1,798,437)</u>	<u>\$ 835,205</u>	<u>\$ (10,611,317)</u>
Governmental Activities Capital Assets, Net	<u>\$ 36,451,594</u>	<u>\$ 22,319,810</u>	<u>\$ (11,479,067)</u>	<u>\$ 47,292,337</u>

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 5 Capital Assets (Continued)

Business - Type Activities:

Capital assets not being depreciated				
Land	\$ 998,293	\$ 35,029	\$ 0	\$ 1,033,322
Construction in Progress	<u>9,222,558</u>	<u>9,417,366</u>	<u>(3,122,603)</u>	<u>15,517,321</u>
Total Capital Assets Not Being Depreciated	<u>\$ 10,220,851</u>	<u>\$ 9,452,395</u>	<u>\$ (3,122,603)</u>	<u>\$ 16,550,643</u>
Capital assets being depreciated				
Land Improvements	\$ 309,045	\$ 0	\$ 0	\$ 309,045
Building & Building Improvements	87,344,678	14,147,630	0	101,492,308
Equipment	<u>7,529,899</u>	<u>352,253</u>	<u>0</u>	<u>7,882,152</u>
Total Capital Assets being Depreciated	<u>\$ 95,183,622</u>	<u>\$ 14,499,883</u>	<u>\$ 0</u>	<u>\$ 109,683,505</u>
Totals at Historical Cost	<u>\$ 105,404,473</u>	<u>\$ 23,952,278</u>	<u>\$ (3,122,603)</u>	<u>\$ 126,234,148</u>
Less: Accumulated Depreciation				
Land Improvements	\$ (292,136)	\$ (5,318)	\$ 0	\$ (297,454)
Building & Building Improvements	(57,086,489)	(2,591,967)	0	(59,678,456)
Equipment	<u>(6,715,957)</u>	<u>(231,547)</u>	<u>0</u>	<u>(6,947,504)</u>
Total Accumulated Depreciation	<u>\$ (64,094,582)</u>	<u>\$ (2,828,832)</u>	<u>\$ 0</u>	<u>\$ (66,923,414)</u>
Business - Type Capital Assets, Net	<u>\$ 41,309,891</u>	<u>\$ 21,123,446</u>	<u>\$ (3,122,603)</u>	<u>\$ 59,310,734</u>

Depreciation Expense was charged to Governmental activities as follows:

General	\$ 36,389
Public Safety	387,621
Public Works	936,593
Parks & Recreation	403,075
Unallocated	<u>34,759</u>
Total Depreciation Expense	<u>\$ 1,798,437</u>

Construction in progress is composed of the following:

Governmental Activities:

Construction in progress of \$5,104,379 consists of expenditures relating to the construction of flood control projects and improvement to various city roads and bridges. Commitments at December 31, 2005 totaled approximately \$23,000,000.

Business Type Activities:

Construction in progress consists of expenditures paid in connection with the construction of a new parking facility and the related capitalized interest of the 2004 Series revenue bond issue. The total cost of the facility is estimated to be \$13,548,000 and will be funded by the 2004 series revenue bond issue of which \$5,974,263 are recorded as construction in progress at December 31, 2005.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 5 Capital Assets (Continued)

At March 31, 2005, expenditures amounting to \$6,532,738 are recorded as construction in progress. Total contracts signed at March 31, 2005 amounted to approximately \$4,500,000.

In December, 2002, the Environmental Protection Agency issued a compliance order requiring the Authority to make certain capital improvements. Initial costs are estimated to be approximately \$5,500,000 for the planning phase of the project. The total cost of the capital improvements cannot be estimated until the planning phase is complete. The Authority expects to obtain funding for this project through a bond issue and available grant funding.

During the year ended March 31, 2004, the Authority entered into a subgrant agreement with Lackawanna County as partial funding for the project. The total amount of the subgrant is \$4,022,995, as amended, with the Authority responsible for 45%. For the year ended March 31, 2005, the County invoiced the Authority for \$1,003,610, resulting in the recording of \$1,226,634 as grant revenue and \$2,230,244 as construction-in-progress. Total construction-in-progress for this project at March 31, 2005 amounted to \$3,010,320.

Note 6 Short-Term Debt

The following summarizes the changes in short-term debt of the Enterprise Fund for the year ended December 31, 2005:

	<u>Balance</u> <u>01/01/05</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance</u> <u>12/31/05</u>
Sewer Authority:				
Line of Credit	\$1,864,103	\$ 0	\$(1,139,913)	\$ 724,190
Line of Credit	0	18,837	0	18,837
Demand Note Payable	12,689	0	(12,689)	0
	<u>\$1,876,792</u>	<u>\$ 18,837</u>	<u>\$(1,152,602)</u>	<u>\$ 743,027</u>

Line of Credit: In August 2000, the Sewer Authority obtained a \$4,000,000 line of credit to provide interim financing for a capital improvement program. Interest is payable monthly at a variable rate equal to 70% of the prime rate. Security for the line of credit is all receipts and accounts receivable. The line of credit matures sixty months after the closing date of the long-term financing.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 6 Short-Term Debt (Continued)

In February 2005, the Authority obtained a \$2,000,000 line of credit to fund various emergency projects and to provide general working capital. The line of credit matures December 31, 2005, with interest at the prime rate. Security for the line of credit is all receipts and accounts receivable, subordinated to the PENNVEST loans.

Demand Note Payable: The Sewer Authority had a demand note payable secured by a vehicle, with interest at 3.15%. If no demand is made, monthly payments of \$1,174, including principal and interest, are due until February, 2005.

Note 7 Long-Term Debt

The following summarizes the changes in long-term debt for the year ended December 31, 2005

	Balance 01/01/05	Additions	(Amortization) Accretion	Retirements	Balance 12/31/05
GOVERNMENTAL ACTIVITIES					
General Obligations Bonds:					
Emmaus General Authority Series 2	\$ 7,310,000	\$ 0	\$ 0	\$ 200,000	\$ 7,110,000
Series A of 2003	4,615,000	0	0	420,000	4,195,000
Series B of 2003	34,970,000	0	0	690,000	34,280,000
Series C of 2003	17,835,000	0	0	320,000	17,515,000
Series D of 2003	13,005,000	0	0	480,000	12,525,000
(Amortization) / Accretion	(483,403)	0	27,664	0	(455,739)
Total General Obligation Bonds	<u>\$ 77,251,597</u>	<u>\$ 0</u>	<u>\$ 27,664</u>	<u>\$ 2,110,000</u>	<u>\$ 75,169,261</u>
Lease Obligations Payable					
Capitalized Lease Vehicles	\$ 59,780	\$ 0	\$ 0	\$ 59,780	\$ 0
Capitalized Lease Vehicles	0	332,247	0	72,424	259,823
Capitalized Lease Vehicles	0	252,202	0	21,081	231,121
Capitalized Lease Buildings	4,000,000	0	0	0	4,000,000
Capitalized Lease Buildings	0	5,500,000	0	0	5,500,000
Total Lease Obligations Payable	<u>\$ 4,059,780</u>	<u>\$ 6,084,449</u>	<u>\$ 0</u>	<u>\$ 153,285</u>	<u>\$ 9,990,944</u>
Redevelopment Authority:					
Bond Payable	\$ 12,295,000	\$ 0	\$ 0	\$ 0	\$ 12,295,000
Note Payable	1,314,423	0	0	226,859	1,087,564
Total Redevelopment Authority	<u>\$ 13,609,423</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 226,859</u>	<u>\$ 13,382,564</u>
TOTAL GOVERNMENTAL ACTIVITIES	<u>\$ 94,920,800</u>	<u>\$ 6,084,449</u>	<u>\$ 27,664</u>	<u>\$ 2,490,144</u>	<u>\$ 98,542,769</u>

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 7 Long-Term Debt (Continued)

BUSINESS-TYPE ACTIVITIES

Revenue Bonds:

Major Enterprise Fund:

Parking Authority

1995 Series	\$ 1,960,000	\$ 0	\$ 0	\$ 155,000	\$ 1,805,000
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2004 Series	15,845,000	0	0	175,000	15,670,000
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Sewer Authority

2002 Series	4,623,101	86,866	0	221,346	4,488,621
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2002 Series	3,357,841	491,737	0	155,675	3,693,903
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2003 Series	0	1,884,378	0	0	1,884,378
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2005 Series	0	0	0	0	0
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Total Revenue Bonds	<u>\$ 25,785,942</u>	<u>\$ 2,462,981</u>	<u>\$ 0</u>	<u>\$ 707,021</u>	<u>\$ 27,541,902</u>
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Notes Payable:

Major Enterprise Fund:

Sewer Authority	\$ 109,389	\$ 0	\$ 25,621	\$ 83,768
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Sewer Authority	<u>246,173</u>	<u>0</u>	<u>0</u>	<u>46,436</u>
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TOTAL BUSINESS-TYPE ACTIVITIES	<u>\$ 26,141,504</u>	<u>\$ 2,462,981</u>	<u>\$ 0</u>	<u>\$ 779,078</u>	<u>\$ 27,825,407</u>
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TOTAL LONG-TERM DEBT	<u>\$ 121,062,304</u>	<u>\$ 8,547,430</u>	<u>\$ 27,664</u>	<u>\$ 3,269,222</u>	<u>\$ 126,368,176</u>
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A summary of long-term debt outstanding at December 31, 2005 is as follows:

Emmaus General Authority Series 2002:

Variable rate demand bonds, Series of 1996 of Emmaus General Authority, due in annual principal installments of \$190,000 to \$440,000 commencing August 2004 through August 2028. Monthly payments of interest based upon a pro rata share of the interest accrued on the variable rate bonds calculated by the administrator based on the interest rates determined by the remarketing agent for the current month plus interest at the rate estimated by the administrator for the remaining portion of the month which has not been determined by the Remarketing Agent, plus 55 basis points.

General Obligation Bonds, Series A of 2003:

On August 1, 2003 the City of Scranton in accordance with the local government Unit Debt Act of the Commonwealth of Pennsylvania, Act 52, of 1978 issued \$5,025,000. Of 1.00% to 3.50% General Obligation Bonds, Series A of 2003 to provide funds to advance refund the City's General Obligation Bonds, Series of 2001 A, capitalize a portion of the interest on the bonds and pay the costs and expenses related to issuing and insuring the bonds. Interest is payable on March 1, and September 1, each year with final maturity September 1, 2014. The bonds maturing

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 7 Long-Term Debt (Continued)

after September 1, 2006 are subject to extraordinary mandatory redemption prior to maturity on March 1, 2006 at the direction of the City at 100% to the extent that there are available amounts generated in the preceding fiscal year as determined under IRC section 1.148-6(d)(3)(iii) of the 1986 code. The bonds maturing on or after September 1, 2014 are subject to redemption prior to their stated dates of maturity at the option of the City on or after September 1, 2013 at a redemption price of 100%.

General Obligation Bonds, Series B of 2003:

On August 1, 2003 the City of Scranton in accordance with the local government Unit Debt Act of the Commonwealth of Pennsylvania, Act 52, of 1978 issued \$35,650,000. Of 1.30% to 4.50% General Obligation Bonds, Series B of 2003 to provide funds to advance refund the City's General Obligation Bonds, Series of 1997 A, to advance refund the City's General Obligation Bonds, Series of 2001C, to fund various capital projects within the City, capitalize a portion of the interest on the bonds and pay the costs and expenses related to issuing and insuring the bonds. Interest is payable on March 1, and September 1, each year with final maturity September 1, 2031. The bonds maturing on or after September 1, 2014 are subject to redemption prior to their stated dates of maturity at the option of the City on or after September 1, 2013 at a redemption price of 100%.

General Obligation Bonds, Series C of 2003:

On August 1, 2003 the City of Scranton in accordance with the local government Unit Debt Act of the Commonwealth of Pennsylvania, Act 52, of 1978 issued \$18,145,000. Of 1.40% to 5.60% Federally Taxable General Obligation Bonds Pension Funding, Series C of 2003 to pay off pension management termination fee, fund the pension actuarial accrued liability, capitalize a portion of the interest on the bonds and pay the costs and expenses related to issuing and insuring the bonds. Interest is payable on March 1, and September 1, each year with final maturity September 1, 2033. The bonds maturing on or after September 1, 2014 are subject to redemption prior to their stated dates of maturity at the option of the City on or after September 1, 2013 at a redemption price of 100%.

General Obligation Bonds, Series D of 2003:

On August 1, 2003 the City of Scranton in accordance with the local government Unit Debt Act of the Commonwealth of Pennsylvania, Act 52, of 1978 issued \$13,480,000. Of 1.40% to 5.50% Federally Taxable General Obligation Bonds, Series D of 2003 to fund the actuarial accrued workmen's compensation liability, capitalize a portion of the interest on the bonds and pay the costs and expenses related to issuing and insuring the bonds. Interest is payable on March 1, and September 1, each year with final maturity September 1, 2023. The bonds maturing on or after September 1,

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 7 Long-Term Debt (Continued)

2014 are subject to redemption prior to their stated dates of maturity at the option of the City on or after September 1, 2013 at a redemption price of 100%.

Redevelopment Authority:

Note Payable: the Authority has a note payable with a Fidelity Deposit and Discount Bank with maximum borrowings of \$2,500,000, dated November 1998, maturing in November of 2013. The note carries an interest rate that will adjust every five years to a rate equal to 51.65 percent of the New York Prime Rate on each adjustment date. The rate was adjusted in November 2003 to 2.066%. The outstanding debt is secured by the assignment of the repayments on seven loans held by the City of Scranton related to certain grant programs. The note is payable in monthly installments of \$14,000, including principal and interest, and an annual principal installment of \$84,000. The balance of the loan at December 31, 2005 was \$1,087,564. Interest payments in 2005 totaled \$25,141.

Variable Rate Demand Lease Revenue Bonds, Series 2004: During 2004, the Authority issued Guaranteed Variable Rate Demand Lease Revenue Bonds, Series of 2004, in the amount of \$12,295,000 for the benefit of the Parking Authority of the City of Scranton pursuant to a lease agreement dated April 15, 2004. The proceeds of the Bonds will be used to provide funds for the construction and development of a parking facility with commercial retail space on a parcel of land owned by the Redevelopment Authority in the City of Scranton.

The Guaranteed Variable Rate Demand Lease Revenue Bonds will bear interest at a weekly rate or a term rate, as determined in accordance with the Trust Indenture. The Bonds have a variable interest rate not to exceed 5% for the initial five year period and, thereafter, 12% for the weekly rate bonds and 25% for the term rate bonds. The interest rate is determined by a Remarketing Agent responsible for the remarketing of the tendered bonds. As such, the interest maturities have been estimated using an interest rate of 4.25% for the remaining term of the Bonds.

Parking Authority:

1969 Parking Authority Bonds, due in annual installments through 2009, bearing interest rates of 4.75% to 5.85%. In January 2004, the Authority used a portion of the proceeds from the 2004 series bonds to redeem and retire the 1969 series bonds. The loss resulting from this transaction amounted to \$68,683 recorded as a deferred charge. Amortization is recorded on the straight-line method as a component of interest expense and amounted to \$13,094 for the year ended December 31, 2005.

1995 Parking Revenue Bonds, due in annual installments through 2020, bearing interest rate of 5.00% to 7.15%. In January 2004, the Authority used a portion of the

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 7 Long-Term Debt (Continued)

proceeds from the 2004 series bonds to advance refund \$4,580,000 of the outstanding 1995 series bonds. The Authority established an escrow account with the Trustee in the amount of \$5,087,024. The investments in the trust and fixed earnings from the investments are sufficient to fully service the defeased debt until the debt is called or matures. The loss resulting from this transaction amounted to \$683,063 and has been recorded as a deferred charge. Amortization is recorded on the straight-line method as a component of interest expense and amounted to \$40,984 for the year ended December 31, 2005.

2004 Parking Revenue Bonds:

On January 1, 2004, the Authority issued \$16,145,000 of Guaranteed Parking Revenue Bonds through the Third Supplemental Trust Indenture. The Bonds carry interest rates of 1.1% to 5.0%. The proceeds from the issue will be used to acquire, construct and equip a new parking facility, renovate existing parking facilities, redeem the remaining 1969 Series Bonds outstanding and establish an escrow account to advance refund \$4,590,000 of the 1995 Series Bonds.

Optional Redemption:

The 2004 Series Bonds maturing on or after September 15, 2014, are subject to redemption at the option of the Authority beginning September 15, 2013, out of monies deposited with or held by the Trustee for such purposes as a whole or in part at any time, and, in any order of maturities selected by the Authority, 100% of the par amount, plus accrued interest thereon upon thirty days notice.

Mandatory Redemption of Term Bonds:

The 2004 Bonds stated to mature on September 15, 2025 (the "2025 Bonds"), September 15, 2028 (the "2028 Bonds"), and September 15, 2033 (the "2033 Bonds"), are subject to mandatory redemption by the Authority prior to maturity, in part by lot, on September 15th of the years 2024 through 2033, inclusive, from monies in the Series of 2004 Sinking Fund, at a redemption price equal to 100% of the principal amount thereof, plus interest accrued to the redemption date. The Authority covenants and directs the Trustee to redeem according to the bond document the principal amount of 2004 Series Bonds.

Sewer Authority:

Sewer Authority 2002 Series (PENNVEST Loan):

The balance outstanding at March 31, 2005 amounted to \$4,488,621. The loan is secured by the gross revenues of the Authority and the guarantee of the City of

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 7 Long-Term Debt (Continued)

Scranton. Interest only was payable on advances until July 1, 2003, when monthly principal and interest payments are due up to and including January 2004. Interest is at 1.522% for the first 75 months and 3.045% thereafter. Legal fees relating to + obtaining the financing amounted to \$44,338 and have been recorded as deferred charges. Construction was completed for this phase in July 2003, and the final disbursement on this loan was received June 2004 in the amount of \$86,866.

Sewer Authority 2002 Series (PENNVEST Loan):

The balance outstanding at March 31, 2005 amounted to \$3,693,903. This loan closed in October 2002 in the amount of \$4,947,000. The security is the same as above. Interest only is payable on advances until August 1, 2004, when monthly principal and interest payments are due up to and including July 1, 2024. Interest is at 1.387% for the first 81 months and 2.774% thereafter.

Sewer Authority 2003 Series (PENNVEST Loan):

The loan closed in December 2003, in the amount of \$2,806,264. The balance outstanding at March 31, 2005 amounted to \$1,884,378. The security is the same as above. Interest only is payable on advances until February 1, 2005, when monthly principal and interest payments are due up to and including January 1, 2025. Interest is at 1.387% for the first 73 months and 2.774% thereafter.

During 2005, the Authority closed on a fourth loan in the amount of \$3,944,160. There was no balance outstanding at March 31, 2005. The security is the same as above, with similar terms.

The PENNVEST loans are federally funded and therefore subject to various compliance requirements, Refer to loan documents for complete details.

Capitalized Lease Obligation:

On December 27, 2004, the Sewer Authority issued \$4,000,000 5.99% Guaranteed Lease Revenue Bonds for the benefit of the City of Scranton pursuant to a sale/lease back agreement entered into between the Sewer Authority and the City. The Sewer Authority purchased the new DPW complex located on Popular Street and leased the complex back to the City at the same terms as the Guaranteed Lease Revenue Bonds. The City will purchase the complex for \$1 at the end of the lease term. Interest is payable on June 15th and December 15th each year with final maturity on December 16, 2016. Principal is payable annually starting on December 15, 2006. The City has guaranteed the Sewer Authority Debt. The sale/lease back transaction of December 27, 2004 is not included in their financial statements.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 7 Long-Term Debt (Continued)

Therefore, the debt is listed as a capitalized lease obligation on the primary government at December 31, 2005.

On December 29, 2005, the Sewer Authority issued \$5,500,000 6.99% Guaranteed Lease Revenue Notes for the benefit of the City of Scranton pursuant to a Sublease and Guaranty agreement entered into between the Sewer Authority and the City. In 2004, the Sewer Authority had purchased the new DPW complex located on Popular Street and leased the complex back to the City at the same terms as the Guaranteed Lease Revenue Bonds. The City will purchase the complex for \$1 at the end of the lease term. Interest is payable on June 15th and December 15th each year with final maturity on December 16, 2008. Principal is payable annually starting on December 15, 2006. The City has guaranteed the Sewer Authority Debt.

Capitalized Vehicles:

In 2005, the City entered into two capitalized leases for equipment purchases. The lease interest rates are 4.41% and 9.0% respectively. The leases contain quarterly and annual payments of \$72,424 and 13,279 respectively.

The Sewer Authority and Parking Authority have restricted certain cash balances, investments, and related accounts for the retirement of long-term debt.

Future Debt Service Requirements as of December 31, 2005 are as follows:

Year Ending December 31,	Governmental Activities City General Obligation Bonds			Year Ending December 31,	Governmental Activities Redevelopment Authority General Obligation Bonds		
	Principal	Interest	Total		Principal	Interest	Total
2006	\$ 2,145,000	\$ 3,296,695	\$ 5,441,695	2006	225,000	522,538	\$ 747,538
2007	2,185,000	3,252,659	5,437,659	2007	240,000	512,975	752,975
2008	2,235,000	3,199,045	5,434,045	2008	250,000	502,775	752,775
2009	2,295,000	3,137,225	5,432,225	2009	260,000	492,150	752,150
2010	2,360,000	3,066,634	5,426,634	2010	270,000	481,100	751,100
2011-2015	12,705,000	13,919,657	26,624,657	2011-2015	1,555,000	2,221,900	3,776,900
2016-2020	14,680,000	11,065,779	25,745,779	2016-2020	1,935,000	1,860,225	3,795,225
2021-2025	16,665,000	7,216,870	23,881,870	2021-2025	2,410,000	1,410,788	3,820,788
2026-2030	16,305,000	3,413,336	19,718,336	2026-2030	3,005,000	850,000	3,855,000
2031-2033	4,050,000	411,075	4,461,075	2031-2033	2,145,000	184,875	2,329,875
	<u>\$ 75,625,000</u>	<u>\$ 51,978,975</u>	<u>\$ 127,603,975</u>		<u>\$ 12,295,000</u>	<u>\$ 9,039,326</u>	<u>\$ 21,334,326</u>

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 7 Long-Term Debt (Continued)

Governmental Activities Redevelopment Authority
Note Payable

Year Ending December 31,	Principal	Interest	Total
2006	\$ 231,495	\$ 20,505	\$ 252,000
2007	236,323	15,677	252,000
2008	240,294	11,706	252,000
2009	237,894	14,106	252,000
2010	141,558	3,144	144,702
	<u>\$ 1,087,564</u>	<u>\$ 65,138</u>	<u>\$ 1,152,702</u>

Business-Type Activities
Revenue Bonds
Parking Authority

Year Ending December 31,	Principal	Interest	Total
2006	\$ 340,000	\$ 831,828	\$ 1,171,828
2007	355,000	818,528	1,173,528
2008	370,000	803,318	1,173,318
2009	385,000	786,465	1,171,465
2010	405,000	767,900	1,172,900
2011-2015	2,355,000	3,505,190	5,860,190
2016-2020	2,940,000	2,916,130	5,856,130
2021-2025	3,295,000	2,229,550	5,524,550
2026-2030	4,070,000	1,370,500	5,440,500
2031-2033	2,960,000	300,750	3,260,750
	<u>\$ 17,475,000</u>	<u>\$ 14,330,159</u>	<u>\$ 31,805,159</u>

Business-Type Activities
Revenue Bonds
Sewer Authority

Year Ending December 31,	Principal	Interest	Total
2006	\$ 627,405	\$ 178,589	\$ 805,994
2007	647,257	167,840	815,097
2008	658,217	156,879	815,096
2009	619,839	188,256	808,095
2010	555,681	230,409	786,090
2011-2015	2,914,396	1,125,964	4,040,360
2016-2020	3,294,562	671,561	3,966,123
2021-2025	1,033,050	118,708	1,151,758
	<u>\$ 10,350,407</u>	<u>\$ 2,838,206</u>	<u>\$ 13,188,613</u>

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 7 Long-Term Debt (Continued)

The debt service for capitalized leases is as follows for governmental activities:

Year Ending December 31,	Principal	Interest	Total
2006	\$ 293,876	\$ 649,310	\$ 943,186
2007	319,718	646,221	965,939
2008	5,840,975	628,216	6,469,191
2009	382,679	215,888	598,567
2010	383,696	191,318	575,014
2011-2015	2,170,000	607,420	2,777,420
2016-2020	600,000	36,539	636,539
TOTAL	<u>\$ 9,990,944</u>	<u>\$ 2,974,912</u>	<u>\$ 12,965,856</u>

The total principal and interest equals the required minimum payments for the period shown.

The interest rate on the capital leases is 5.99% & 6.99% for the lease with The Scranton Sewer Authority and 4.41% & 9.0% For the capitalized vehicles

The cost of the assets is	\$ 4,707,468
The accumulated depreciation expense through December 31, 2005 is	<u>(158,793)</u>
The net book value of the capitalized leased building and vehicles is	<u>\$ 4,548,675</u>

Advance Refunding:

On August 7, 2003 the City issued \$ 5,025,000 in General Obligation Bonds Series A dated August 1, 2003 with an average interest rate (coupon) of 2.934% to advance refund \$4,885,000 of outstanding 2001 A series bonds with an average interest rate of 5.620%. Total proceeds including bond discount and accrued interest was \$ 5,000,406. Underwriting fees and other issuance cost were \$ 123,247. Net proceeds of \$ \$ 4,875,047 were used to purchase United States Treasury Securities – State and Local Governments deposited in an irrevocable trust with an escrow agent. An additional \$ 504,997 from the debt service fund (sinking fund) and an additional \$ 233,318 from the 2004 B issue were deposited in the irrevocable trust with subsequent debt service payments on the refunded bond issue to be paid from the irrevocable trust. As a result, refunded series 2001 A is considered to be defeased as of the issuance date and the liability for those bonds removed from the financial statements in the period of defeasance. Comparative debt service cash flows on the old and new debt show a cash flow benefit of \$ 540,303. In 2005, the United States Treasury Securities - State and Local Government were refinanced and the City

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 7 Long-Term Debt (Continued)

received an additional \$108,435. from the escrow account. Amortization is recorded on the straight-line method as a component of interest expense and amounted to \$58,748 for the year ended December 31, 2005.

On August 7, 2003 the City issued \$ 20,870,000 in General Obligation Bonds Series B dated August 1, 2003 with an average interest rate (coupon) of 4.407% to advance refund \$17,440,000 of outstanding 2001 C series bonds with an average interest rate of 6.407%. Total proceeds included bond discount and accrued interest was \$20,792,205. Underwriting fees and other issuance cost were \$ 645,712. Net proceeds of \$ 19,516,640 were used to purchase United States Treasury Securities – State and Local Governments deposited in an irrevocable trust with an escrow agent. An additional \$ 1,700,162 from the debt service fund (sinking fund) and \$355,629 from the sinking fund applicable to the 2001 C bonds were deposited in the irrevocable trust. Additional proceeds of \$233,318 were deposited in the irrevocable trust to advance refund the 2001 A bonds noted above. Additional proceeds of \$207,611 were deposited in the irrevocable trust to advance refund the 1997 A bonds noted below. Additional proceeds of \$174,232 were deposited into the 2004 sinking fund to fund the September 1, 2003 interest payments. Subsequent debt service payments on the refunded bond issue will be paid from the irrevocable trust, as a result, refunded series 2001 C is considered to be defeased as of the issuance date and the liability for those bonds removed from the financial statements in the period of defeasance. Comparative debt service cash flows on the old and new debt show cash flow benefit of \$3,992,959. In 2005, the United States Treasury Securities - State and Local Government were refinanced and the City received an additional \$387,123. from the escrow account. Amortization is recorded on the straight-line method as a component of interest expense and amounted to \$394,377 for the year ended December 31, 2005.

The amount of defeased debt outstanding at December 31, 2005 is as follows:

2001 Series A General Obligation Bonds	\$ 4,040,000.
2001 Series C General Obligation Bonds	\$ 17,295,000.

Bond Closing Cost were incurred for the 2005 Capitalized Lease in the amount of \$67,500 as follows:

Bond Counsel	\$ 30,000
Underwriters Counsel	3,500.
Trustee & Counsel Fees	8,000.
Rating Agency Fees	15,000.
Commitment Fee	11,000.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 7 Long-Term Debt (Continued)

The breakdown of interest expense as of December 31, 2005 is as follows:

	<u>Interest Expense Charged to Expense</u>	<u>Interest Expense Capitalized</u>
City of Scranton	\$ 3,645,288	\$ 0
Sewer Authority of the City of Scranton	73,252	101,415
Parking Authority of the City of Scranton	416,307	428,046
Redevelopment Authority of the City of Scranton	<u>25,141</u>	<u>0</u>
	<u>\$ 4,159,988</u>	<u>\$ 529,461</u>

Note 8 Risk Management

The City's risk management activities are reported with governmental activities and recorded in the Workman's Compensation Internal Service Fund. The purpose of this fund is to administer a Self-Insured Retention Program (SIR). Claims in excess of SIR limit of \$350,000 are covered through third party insurance policies. Payments of actual claim costs are made by a third party administrator and are billed to the City and reimbursed by the General Fund. The claims costs are reflected as revenues in the Internal Service Fund.

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 retains the risk up to various levels depending on the type of risk. Excess loss coverage is purchased for coverage on claims exceeding the retention level.

At December 31, 2005, the City's self-insured retention limits are as follows:

<u>Type of Coverage</u>	<u>Self-Insurance Retention (SIR) (All Claims Up To)</u>	<u>Excess Coverage Policy (From SIR Up To)</u>
General liability	\$ 50,000	\$ 950,000
Law enforcement liability	\$ 50,000	\$ 950,000
Public officials liability	\$ 50,000	\$ 950,000
Property	\$ 50,000	\$15,000,000
Automobile Liability	\$ 50,000	\$ 950,000
Excess worker's compensation	\$350,000	\$ Unlimited
Boiler and machinery	\$ 50,000	\$15,000,000

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 8 Risk Management (Continued)

Accrued Worker's Compensation Claims:

The Accrued Worker's Compensation Claim loss reserve of \$20,607,305 at December 31, 2005 was determined by an actuary and represents the discounted present value of expected losses using a 5.00% interest factor. The actuarial value was determined as of August 31, 2005 and in prior years the actuarial valuation was determined as of December, 31. The amount of Worker's Compensation Claims operating expense for the Internal Service Fund for the year ended December 31, 2005 is calculated as follows:

Claims and Costs Paid	\$3,888,076
Increase in Actuarial	
Discounted Loss Reserve	24,610
Buyout Settlement Payments	<u>80,000</u>
Worker's Compensation Claims	<u>\$3,992,686</u>

The reconciliation of changes in the aggregate liabilities for the current year and the prior year are as follows:

Calendar Year Ended	Balance Beginning of Calendar Year	Current Year Claims and Changes In Estimates	Claim Payments	Balance End of Calendar Year
31-Dec-05	\$ 20,582,695	\$ 3,912,686	\$ 3,888,076	\$20,607,305
31-Dec-04	\$ 18,335,089	\$ 6,036,571	\$ 3,788,965	\$20,582,695

Note 9 Interfund Transfers

Interfund transfers during the year ended December 31, 2005 were as follows:

	<u>Operating Transfers in</u>	<u>Operating Transfers Out</u>
General Fund	\$ 1,534,313	\$ 5,887,364
Special Revenue Fund:		
Liquid Fuels	0	1,245,390
Special City	44,234	1,417,931

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 9 Interfund Transfers (Continued)

	<u>Operating Transfers in</u>	<u>Operating Transfers Out</u>
Debt Service Fund	5,232,238	0
Capital Projects	<u>1,776,304</u>	<u>36,404</u>
TOTAL	<u>\$ 8,587,089</u>	<u>\$ 8,587,089</u>

Note 10 Pension Plans/Other Postemployment Benefits

Defined Benefit Plans: The City sponsors and administers three single employer defined benefit pension plans covering substantially all full-time employees. These plans are the Police, Fireman, and Nonuniformed pension plans (the "Plans"). Pennsylvania Act 205 and the City's Home Rule Charter assign the authority to establish and amend benefit provisions to the Pension Fund Board as authorize by City Council. The Plans have been designated as severely distressed under Pennsylvania Act 205

The Police pension plan provides for normal retirement with 25 years of credited service with a retirement age of 55 years for the members hired on or after July 1, 1987. For members hired prior to July 1, 1987, the Plan provides for normal retirement with 25 years of credited service with a retirement age of 65 years. The Fireman's pension plan provides for normal retirement at age 55 with 25 years of credited service for members hired on or after July 1, 1987. For members hired prior to July 1, 1987, the Plan provides for normal retirement with 25 years of credited service. The Nonuniformed pension plan provides for normal retirement at age 55 with 20 years of credited service including continuous service of 15 years. Members are 100% vested when eligible.

Information regarding the plans can be obtained from the City. The plans do not issue separate financial statements but are included in the City's fund financial statements as a fiduciary fund type – Pension Trust Funds.

Police are required to contribute 3.5% of covered payroll for members hired on or after July 1, 1987. For members hired prior to July 1, 1987, the police are required to contribute 4.0% of covered payroll. Firemen are required to contribute 3.5% of covered payroll for members hired on or after July 1, 1987. For members hired prior to July 1, 1987, the Fireman are required to contribute 4.0% of covered payroll. Nonuniformed nonunion employees are required to contribute 3% of covered payroll but not more than \$22 per month if hired after July 1, 1987. Nonuniformed union employees shall contribute \$24 per month if hired before July 1, 1987 or amounts as determined by ordinance.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 10 Pension Plans/Other Postemployment Benefits (Continued)

Pennsylvania Act 205 of 1984, the Municipal Pension Plan Funding Standard and Recovery Act of the Commonwealth of Pennsylvania (as amended) (Act 205) requires that annual contributions be based upon the Minimum Municipal Obligation (MMO), which is based on the Plans' biennial actuarial valuation. According to Act 205, actuarial valuations may be made biennially and the most recent valuation for all of the City's plans was completed as of January 1, 2005. The MMO includes the normal cost, estimated administrative expenses and an amortization of the unfunded actuarial accrued liability, less estimated member contributions, and a credit equal to 10 percent of the excess (if any) of the actuarial value of assets over the actuarial accrued liability. The Commonwealth of Pennsylvania provides an allocation of funds which must be used for pension funding. Any financial requirements established by the MMO which exceeds Commonwealth and member contributions must be funded by the City.

Contributions, based on the MMO, in 2005 consisted of the following:

	<u>POLICE</u>	<u>FIREMEN</u>	<u>NON- UNIFORMED</u>	<u>TOTAL</u>
City/Commonwealth	\$1,378,746	\$3,551,933	\$ 314,212	\$ 5,244,891
Employees	<u>231,140</u>	<u>222,458</u>	<u>52,380</u>	<u>505,978</u>
Total	<u>\$1,609,886</u>	<u>\$3,774,391</u>	<u>\$ 366,592</u>	<u>\$ 5,750,869</u>

A summary of the change in the net pension obligation as of January 1, 2005, 2003, and 2002 is presented below:

	<u>January 1, 2005</u>			
	<u>Police</u>	<u>Firemen</u>	<u>Non- Uniformed</u>	<u>Total</u>
Annual required contribution	\$ 1,925,986	\$ 1,633,392	\$ 247,633	\$ 3,807,011
Interest on pension benefit obligation	<u>3,475,491</u>	<u>7,407,537</u>	<u>511,164</u>	<u>11,394,192</u>
Annual pension costs	\$ 5,401,477	\$ 9,040,929	\$ 758,797	\$15,201,203
Bond Proceeds Deposited in the Plan	(5,382,726)	(3,948,919)	(690,736)	(10,022,381)
Contributions made	(3,595,385)	(8,120,276)	(776,706)	(12,492,367)
Increase for plan amendment	0	0	1,843,708	1,843,708
Net actuarial gain on plan assets	<u>(583,597)</u>	<u>(8,966,193)</u>	<u>1,040,248</u>	<u>(8,509,542)</u>
Net increase (decrease) in pension benefit obligation	\$ (4,160,231)	\$(11,994,459)	\$ 2,175,311	\$(13,979,379)
Pension benefit obligation, beginning	<u>26,103,381</u>	<u>49,590,010</u>	<u>3,797,770</u>	<u>79,491,161</u>
Pension benefit obligation, ending	<u>\$21,943,150</u>	<u>\$ 37,595,551</u>	<u>\$ 5,973,081</u>	<u>\$ 65,511,782</u>

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 10 Pension Plans/Other Postemployment Benefits (Continued)

	<u>January 1, 2003</u>			
	<u>Police</u>	<u>Firemen</u>	<u>Non-Uniformed</u>	<u>Total</u>
Annual required contribution	\$ 824,602	\$ 788,789	\$ 140,983	\$ 1,754,374
Interest on pension benefit obligation	1,113,188	3,250,691	125,461	4,489,340
Adjustment to annual required contribution	<u>853,473</u>	<u>1,039,706</u>	<u>14,778</u>	<u>1,907,957</u>
Annual pension costs	\$ 2,791,263	\$ 5,079,186	\$ 281,222	\$ 8,151,671
Contributions made	(1,380,194)	(4,315,202)	(242,085)	(5,937,481)
Net actuarial loss on plan assets	<u>10,777,467</u>	<u>8,192,385</u>	<u>2,190,365</u>	<u>21,160,217</u>
Net increase in pension benefit obligation	\$12,188,536	\$ 8,956,369	\$ 2,229,502	\$23,374,407
Pension benefit obligation, beginning	<u>13,914,845</u>	<u>40,633,641</u>	<u>1,568,268</u>	<u>56,116,754</u>
Pension benefit obligation, ending	<u>\$26,103,381</u>	<u>\$49,590,010</u>	<u>\$ 3,797,770</u>	<u>\$79,491,161</u>

	<u>January 1, 2002</u>			
	<u>Police</u>	<u>Firemen</u>	<u>Non-Uniformed</u>	<u>Total</u>
Annual required contribution	\$ 785,948	\$ 839,678	\$ 127,116	\$ 1,752,742
Interest on pension benefit obligation	1,066,190	3,205,551	74,969	4,346,710
Adjustment to annual required contribution	<u>(6,973)</u>	<u>146,239</u>	<u>(11,065)</u>	<u>128,201</u>
Annual pension costs	\$ 1,845,165	\$ 4,191,468	\$ 191,020	\$ 6,227,653
Contributions made	(454,768)	(3,476,808)	(81,273)	(4,012,849)
Net actuarial (gain)/loss on plan assets	<u>(802,924)</u>	<u>(150,408)</u>	<u>521,409</u>	<u>(431,923)</u>
Net increase in pension benefit obligation	\$ 587,473	\$ 564,252	\$ 631,156	\$ 1,782,881
Pension benefit obligation, beginning	<u>13,327,372</u>	<u>40,069,389</u>	<u>937,112</u>	<u>54,333,873</u>
Pension benefit obligation, ending	<u>\$13,914,845</u>	<u>\$ 40,633,641</u>	<u>\$ 1,568,268</u>	<u>\$56,116,754</u>

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 10 Pension Plans/Other Postemployment Benefits (Continued)

The pension benefit obligations were determined as part of an actuarial valuation at January 1, 2005. The actuarial cost method used is the Entry Age Normal Cost Valuation Method. Significant assumptions used include a rate of return on investment of present and future assets of 8% per year, projected salary increases of 5% per year and no post-retirement benefit increases. Plan assets are valued using a four year smoothing method described in Internal Revenue Service Procedure 2000-40, Approval 15. The unfunded actuarial liability is being amortized as a level percentage of projected payroll on an open basis over a period of approximately 15 year. Effective in 2004, the unfunded actual liability calculation for the years 2002 and 2003 was revised to be amortized as a level percentage of projected payroll on an open basis over a period of 30 of years.

	<u>January 1, 2005</u>			
	<u>Police</u>	<u>Firemen</u>	<u>Non-Uniformed</u>	<u>Total</u>
Actuarial accrued liability	\$60,538,073	\$67,678,929	\$10,259,212	\$138,476,214
Actuarial value of assets	<u>38,594,923</u>	<u>30,083,378</u>	<u>4,286,131</u>	<u>72,964,432</u>
Pension benefit obligation	<u>\$21,943,150</u>	<u>\$37,595,551</u>	<u>\$ 5,973,081</u>	<u>\$ 65,511,782</u>
Funded ratio	<u>64%</u>	<u>44%</u>	<u>42%</u>	<u>53%</u>
Covered payroll	<u>\$6,574,028</u>	<u>\$5,955,465</u>	<u>\$ 4,997,027</u>	<u>17,526,520</u>
Pension benefit obligation to covered payroll	<u>334%</u>	<u>631%</u>	<u>120%</u>	<u>374%</u>

	<u>January 1, 2003</u>			
	<u>Police</u>	<u>Firemen</u>	<u>Non-Uniformed</u>	<u>Total</u>
Actuarial accrued liability	\$61,062,272	\$75,535,426	\$ 8,371,444	\$ 144,969,142
Actuarial value of assets	<u>34,958,891</u>	<u>25,945,416</u>	<u>4,573,674</u>	<u>65,477,981</u>
Pension benefit obligation	<u>\$26,103,381</u>	<u>\$49,590,010</u>	<u>\$ 3,797,770</u>	<u>\$ 79,491,161</u>
Funded ratio	<u>57%</u>	<u>34%</u>	<u>55%</u>	<u>45%</u>
Covered payroll	<u>\$ 5,578,090</u>	<u>\$ 4,833,264</u>	<u>\$ 5,296,284</u>	<u>\$ 15,707,638</u>
Pension benefit obligation to covered payroll	<u>468%</u>	<u>1026%</u>	<u>72%</u>	<u>506%</u>

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 10 Pension Plans/Other Postemployment Benefits (Continued)

January 1, 2002

	<u>Police</u>	<u>Firemen</u>	<u>Non-Uniformed</u>	<u>Total</u>
Actuarial accrued liability	\$54,850,759	\$69,802,104	\$ 7,077,504	\$ 131,730,367
Actuarial value of assets	<u>40,935,914</u>	<u>29,168,463</u>	<u>5,509,236</u>	<u>75,613,613</u>
Pension benefit obligation	<u>\$13,914,845</u>	<u>\$40,633,641</u>	<u>\$ 1,568,268</u>	<u>\$ 56,116,754</u>
Funded ratio	<u>75%</u>	<u>42%</u>	<u>78%</u>	<u>57%</u>
Covered payroll	<u>\$ 6,814,392</u>	<u>\$5,904,732</u>	<u>\$ 5,781,576</u>	<u>\$ 18,500,700</u>
Pension benefit obligation to covered payroll	<u>204%</u>	<u>688%</u>	<u>27%</u>	<u>303%</u>

Historical trend information for the Plans is presented below:

Three-Year Trend Information for the City of Scranton Pension Plans

Police Pension Fund

	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
01/01/02	\$1,845,165	24.6%	\$13,914,845
01/01/03	\$2,791,263	49.4%	\$26,103,381
01/01/05	\$5,401,477	166.2%	\$21,943,150

Firemen Pension Fund

	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
01/01/02	\$4,191,468	82.9%	\$40,633,641
01/01/03	\$5,079,186	85.0%	\$49,590,010
01/01/05	\$9,040,929	133.5%	\$37,595,551

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 10 Pension Plans/Other Postemployment Benefits (Continued)

Non-Uniformed Pension Fund

	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
01/01/02	\$ 191,020	42.5%	\$ 1,568,268
01/01/03	\$ 281,222	86.1%	\$ 3,797,770
01/01/05	\$ 758,797	193.4%	\$ 5,973,081

Defined Contribution Plan: The City contributes to a union sponsored, multi-employer plan for certain of its employees. The Plan is not administered by the City and contributions are determined in accordance with labor contracts. Pension expense was \$208,745. in 2005.

The Parking Authority sponsors a defined contribution pension plan covering all eligible employees. Pension expense was \$25,880 for the year ended December 31, 2005.

The Authority contributes to the Central Pennsylvania Teamsters Pension Fund, a defined contribution pension plan covering substantially all of its full time employees. Employees become eligible after they have been on the payroll for thirteen weeks. Contributions made by the Authority were \$321 per month for the year ended March 31, 2005 for each covered employee; contributions vest according to the Plan's schedule. Pension expense for the year ended March 31, 2005, amounted to \$75,999.

Other Postemployment Benefits: Under the terms of its collective bargaining agreements with its police, firemen, clerical, and public works employees, the City is required to provide health insurance to retiring employees who meet the criteria specified in each contract.

Under the police, firemen, and clerical contracts, the City is responsible for providing health insurance to retirees and spouses for the remainder of their lives if the employee was hired or retired prior to December 31, 1993. Employees hired after December 31, 1993 are not eligible for these benefits. The City's contribution for retiree health insurance is equal to the cost in effect in 1993 plus 75% of any increase above that cost. The retiree pays the other 25%.

Under the public works contract, the City will provide health insurance to retirees and spouses only from age 62 to 65. The City's contribution is equal to the cost in effect in 1994 plus 75% of any increase above that costs. The retiree pays the other 25%.

The City uses the cash basis to account for these expenditures. The City has not determined the amount of such expenditures for 2005 nor the number of participants eligible for these benefits.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 11 Credit Risk and Market Risk

The City uses its authority to levy certain general purpose taxes. Major taxing revenue sources include real estate, earned income, mercantile, and business privilege taxes. These taxes account for approximately 90% of the total taxes collected by the City in 2005. Although the City has a diversified taxing base, its citizens' ability to honor their taxing obligations is substantially dependent upon the general economic condition of the region.

The market value of the City's investments are subject to fluctuations in the prevailing market prices of those investments.

Note 12 Related Party Transactions

The City paid approximately \$603,000 to the Single Tax Office to subsidize certain operating costs of this entity. The Single Tax Office collected approximately \$33,145,000 of tax revenues on behalf of the City in 2005.

Note 13 Commitments and Contingencies

Litigation: Currently, there are various claims and suits pending against the City, the more significant of which are summarized below:

Various lawsuits have been instituted against the City resulting mainly from injuries sustained in accidents on City properties. Legal counsel cannot estimate the probability of successful outcome and the amount of the potential liability from these matters at this time. However, the City has affirmed that it has adequate insurance to cover any possible claim or judgment.

The City is a defendant in various labor and employment matters. Counsel for the City cannot determine the likelihood of success at the present time. The City believes the suits are without merit and is vigorously defending its position. The liability, if any, will not have a material impact on the financial statements as presented. The City is involved in arbitration proceeding with its fire fighter's union seeking reimbursement of alleged inaccurately assessed health care co-payments assessed under its collective bargaining agreement. If co-payments are found to be inaccurate potential exposure could be material to the financial statements. Counsel for the City cannot determine the likelihood of success at the present time. The City believes the suit is without merit and is vigorously defending its position.

The City is involved in arbitration proceedings with its civilian police clerks for the reassignment of personnel of the Police Department. In 2004, a judgment was recorded against the City which the City is appealing. Counsel for the City cannot determine the likelihood of success at the present time. The City believes the suit is without merit and is vigorously defending its position.

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 13 Commitments and Contingencies (Continued)

The City and its Fire Fighters Union are involved in a pay period arbitration process. The arbitration found that the City's method of payment violates the collective bargaining agreement. The City has petitioned to vacate the award. Counsel for the City cannot determine the likelihood of success at the present time. The City believes the suit is without merit and is vigorously defending its position. If the award is not vacated, the potential exposure could be material to the financial statements.

The City and its police and firefighters were unable to agree at an amicable collective bargaining agreement. The arbitration panel issued an award covering the 2003-2007 contract year. The City is appealing the award as it exceeds the parameters of its revised recovery plan and would be in violation of Act 47 Recovery Plan. Counsel for the City cannot determine the likelihood of success at the present time. The City believes that the suit is without merit and is vigorously defending its position. If the award stands, the potential exposure could be material to the financial statements.

The City is involved in an arbitration proceeding with the police union. The Union is alleging that the City failed to maintain appropriate manning in accordance with its collective bargaining agreement. Counsel for the City cannot determine the likelihood of success at the present time. The City believes the suit is without merit and is vigorously defending its position.

Collective Bargaining Agreements: Substantially all of the City's nonmanagement employees are covered by collective bargaining agreements between the City and various unions. The Police and Fire Departments agreements expired at the end of 2002 and continue to be negotiated.

Fund Deficit Self-Insurance Fund Settlement Agreement: On December 18, 2001, the City entered into a Settlement Agreement and Release with the Commonwealth of Pennsylvania Department of Labor and Industry, Bureau of Worker's Compensation (Bureau) in order to maintain its ability to self-insure.

The settlement requires the City to correct various program deficiencies and to provide for unfunded outstanding claims in various annual increments beginning in 2004 through 2012 and to keep current on annual costs for claims, administration, and operating expenses.

During 2003, the City funded the Internal Service Fund with \$13,000,000 from the 2003 debt issuance, thereby meeting the various annual increments through 2013. However, in 2004 the City was not current on annual cost for claims, administration, and operating expenses and is in default under the terms of the Settlement Agreement.

In February 2006, the Bureau and the City entered into the third amendment to irrevocable agreement of trust modification of the December 2001 Settlement Agreement

CITY OF SCRANTON, PENNSYLVANIA
NOTES TO FINANCIAL STATEMENTS

Note 13 Commitments and Contingencies (Continued)

and Release. The agreement modification to allow a deficit of no more than 25% between the city's outstanding liability and asset value of the Reserve Account of the City's Worker's Compensation Trust Fund and will require that any shortfall above the permitted 25% deficit amount be funded over a five-year period.

Note 14 Distressed Municipality Status

In 1992, the Pennsylvania Department of Community and Economic Development (DCED) declared the City a distressed municipality under the Financially Distressed Municipalities Act (Act). DCED then appointed the Pennsylvania Economy League as coordinator to administer a recovery plan for the City pursuant to this Act. While the City has improved its financial situation since this designation, the City still remains a distressed municipality pursuant to the Act.

Note 15 Current Real Estate Taxes

Current real estate taxes collected at December 31, 2005

	<u>Land</u>	<u>Building</u>	<u>Total</u>
Total Assessed Value	94,248,378	292,895,738	387,144,116
Millage Rates	<u>0.082122</u>	<u>0.017860</u>	
Total Original Taxes Levied	7,739,865	5,231,118	\$12,970,983
Add: Additions			1,558
Less: Abatements			<u>(59,413)</u>
Real Estate Taxes To be Collected At Face			\$12,913,128
Add: Penalties Collected			<u>72,478</u>
Total Before Deductions			\$12,985,606
Less: Discounts Taken			(195,207)
Less: Home Vouchers			(275,194)
Less: Delinquent Taxes Returned			<u>(1,625,288)</u>
TOTAL REAL ESTATE TAXES COLLECTED			<u><u>\$10,889,917</u></u>

SUPPLEMENTARY INFORMATION

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

October 6, 2006

To Honorable Members of City Council
The City of Scranton, Pennsylvania

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Scranton, Pennsylvania as of and for the year ended December 31, 2005, which collectively comprise the City of Scranton, Pennsylvania basic financial statements and have issued our report thereon dated October 6, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *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 of Scranton, Pennsylvania 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 assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the City of Scranton, Pennsylvania ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying schedule of findings and questioned costs as item 2005-1.

A material weakness is a 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 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. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that the reportable condition described above is not a material weakness. We also noted other matters involving the internal control over financial reporting that we have reported to management of the City of Scranton, Pennsylvania in a separate letter dated October 6, 2006.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Scranton, Pennsylvania financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, 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 that are required to be reported under Government *Auditing Standards*.

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

In Accordance with *Government Auditing Standards*, we have issued a report dated October 6, 2006 on our consideration of the City of Scranton's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

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

October 6, 2006

The Honorable Members of City Council of
the City of Scranton, Pennsylvania

COMPLIANCE

We have audited the compliance of the City of Scranton, Pennsylvania 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 programs for the year ended December 31, 2005. The City of Scranton, Pennsylvania's major federal 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 programs is the responsibility of the City of Scranton, Pennsylvania's management. Our responsibility is to express an opinion on the City of Scranton, Pennsylvania's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Those standards and OMB Circular A-133 require that we plan and perform the audit to 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 program occurred. An audit includes examining, on a test basis, evidence about the City of Scranton, Pennsylvania 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 of the City of Scranton, Pennsylvania's compliance with those requirements.

As described in item 2005-2 in the accompanying schedule of findings and questioned cost the City of Scranton, Pennsylvania did not comply with requirements regarding recordkeeping and reporting that are applicable to its Cops Ahead Program. Compliance with such requirements is necessary, in our opinion, for the City of Scranton, Pennsylvania to comply with requirements applicable to those programs.

In our opinion, except for the noncompliance described in the preceding paragraph, the City of Scranton, Pennsylvania complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended December 31, 2005.

INTERNAL CONTROL OVER COMPLIANCE

The management of the City of Scranton, Pennsylvania is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the City of Scranton, Pennsylvania's internal control over compliance with requirements that could have a direct and material effect on a major federal 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 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 that would be material in relation to a major federal program 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 Mayor, City Council, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

CITY OF SCRANTON, PENNSYLVANIA
 SCHEDULE OF FINDINGS AND QUESTIONED COSTS
 FOR THE YEAR ENDED DECEMBER 31, 2005

Section I – Auditor’s Result Section

- (1) A qualified opinion was expressed on the aggregate remaining fund information of the auditee. An unqualified opinion was expressed on the remaining Governmental-Activities, Business Activities, and each major fund.
- (2) Reportable condition was disclosed by the audit of the financial statements in Internal Control. The condition is not reported as a material weakness.
- (3) The audit did not disclose any noncompliance which is material to the financial statements of the auditee.
- (4) No reportable conditions relating to the audit of the Major Federal Award Programs are reported.
- (5) The Auditor’s Report on compliance for Cops Ahead Program, expresses a qualified opinion; the report on the remaining programs are unqualified.
- (6) Audit findings that are required to be reported in accordance with Section 510(A) OMB Circular A-133 are reported in this schedule.
- (7) Identification of major programs is as follows:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
14.218	CDBG/Entitlement Grants
14.239	Home Investment Partnerships Program
14.231	Emergency Shelter Grant Program
20.205	Highway Planning and Construction

- (8) The dollar threshold used to distinguish Type A and Type B programs as described in Section 520(B) of OMB Circular A-133 was \$300,000.
- (9) The auditee did not qualify as a low-risk auditee under Section 530 of OMB Circular A-133.

CITY OF SCRANTON, PENNSYLVANIA
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED DECEMBER 31, 2005

Section II – Findings relating to the Financial Statements which are required to be reported in accordance with Generally Accepted Government Auditing Standards.

2005-1

Condition: There is no segregation of duties regarding the system for processing accounts payable. One person is responsible for matching invoices to purchase orders, enters invoices into the general ledger, processes the checks for payment, has access to the signature machine, and mails the checks to vendors.

Effect: Because of the lack of segregation of duties the possibility of error and omissions to go undetected exist when one person has complete control over all these functions.

Recommendation: Procedures should be implemented whereby one person does not have complete control over these functions.

Section III – Findings and questioned cost for Federal Awards which shall include audit findings as defined in Section 510(A) of OMB Circular A – 133

2005-2

Department of Justice:
Universal Hiring Program CFDA 16.710
Cops in School CFDA 16.710

Condition: The Police Department does not maintain adequate written accounting procedures needed to ensure proper control, monitoring, reporting, and receiving of grant funds.

Criteria: Documented financial procedures should be prepared to describe all accounting functions and related activities to ensure adequate control of grant funds.

Effects: Due to a change over in staff and lack of detailed procedures, the following deficiencies were noted:

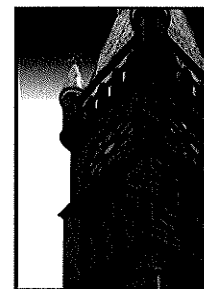
1. Office of Justice Department records reflect that a grant expired on January 31, 2005. However, status reports were filed for the quarter ended June 30, 2005 through December 31, 2005 with eligible federal expenditures. The status reports for the first quarter and third quarters of 2005 were filed more than forty-five days after the end of the quarter. We were not provided with an approved request extending this grant beyond a January 31, 2005 funding period. Per reports filed for

CITY OF SCRANTON, PENNSYLVANIA
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED DECEMBER 31, 2005

December 31, 2004 through September 30, 2005, eligible federal expenditure were \$71,811.32. The City only received one reimbursement of \$51,806.39 in August 2005. This grant has expired and a final status report has been filed. No actions are required at this time.

2. Office of Justice Department records reflect that a grant expired on March 31, 2004. However, status reports were filed for the periods ended March and June 2005 with eligible federal expenditures. The status reports for the first quarter was filed more than forty-five days after the end of the quarter. We were not provided with a request extending this grant beyond the March 31, 2004 funding period. Per reports filed for December 31, 2004 through June 30, 2005, eligible federal expenditures were \$11,472.46. The City only received one reimbursement of \$10,372.00 in August 2005. This grant has expired and a final status report has been filed. No actions are required at this time.

Recommendation: Procedures should be implemented to ensure that all necessary reports are filed timely and accurately. The City has access to authorized funds when available and upon completion of a grant the final completion report is prepared and all funds have been expended within the allotted ninety (90) days after the grant period has ended.



CORRECTIVE ACTION PLAN

Cognizant or Oversight Agencies for Audit: Department of Justice

The City of Scranton, Pennsylvania respectfully submits the following corrective action plan for the year ended December 31, 2005:

Name and address of independent public accounting firm:

Robert Rossi & Co.
299 Main Street – Sturges
Olyphant, PA 18447

Audit period: January 1, 2005 to December 31, 2005

The findings from the December 31, 2005 schedule of findings and questioned costs are discussed below. The findings are numbered consistently with the numbers assigned in the schedule.

FINDINGS – FINANCIAL STATEMENT AUDIT

REPORTABLE CONDITIONS

2005-1 Accounts Payable Segregation of Duties

Recommendation: Procedures should be implemented whereby one person does not have complete control over these functions.

Action Taken: We agree with the finding of the independent auditor and will take steps to implement procedures to address this issue.

FINDINGS – FEDERAL AWARDS PROGRAM AUDIT

DEPARTMENT OF JUSTICE

2005-2 Universal Hiring Program CFDA 16.710
Cops in School CFDA 16.710

Recommendation: Procedures should be implemented to ensure that all necessary reports are filed timely and accurately. The City has access to authorized funds when available and upon completion of a grant the final completion report is prepared and all funds have been expended within the allotted ninety (90) days after the grant has ended.

Action Taken: We agree with the finding of the independent auditor and will take steps to implement procedures to address this issue.



LEONARD A. KRESEFSKI
Business Administrator

CITY OF SCRANTON, PENNSYLVANIA
STATUS OF CORRECTIVE ACTION AND PRIOR AUDIT FINDINGS

Findings and questioned cost for Federal Awards which shall include audit findings as defined in Section 510(a) of OMS Circular A-133.

Findings 2005-2

1. Quarterly financial status reports are due within forty-five (45) days after the end of a quarter. The first quarter of the 2004 quarterly reports were filed within forty-five days after the quarter's end. For one grant we were not provided with a filed fourth quarter report. This finding still exists for reports filed in 2005.
2. To draw down money from the program requires the use of PIN (personnel identification number) after quarterly reports were filed. The new personnel was not aware of this requirement or where such PIN was located. As a result, the City did not receive any Federal reimbursement in 2004 for the COPS program until September 2004. This finding still existed for 2005 as the City only received one draw down in August 2005 for 2004 and 2005 revenue.
3. Upon completion of the grant, the grantee is required to file a final financial status report within (90) days. One grant expired in August 2003 and another in April 2004 the City requested an extension for this grant. However, we were not provided with an approved extension request. Per the Department of Justice their grants are finalized and no further action is needed.
4. For one grant, the total Federal expenditures are listed as \$250,000. However, Federal records only indicate payments of \$209,635. This grant expired in April 2004. Per the Department of Justice their grants are finalized and no further action is needed.
5. For one grant, the total Federal expenditures are listed as \$625,000. However, Federal records only indicate payments of \$608,457. This grant expired in August 2003. Per the Department of Justice their grants are finalized and no further action is needed.