

STATE BOARD OF ACCOUNTS
302 West Washington Street
Room E418
INDIANAPOLIS, INDIANA 46204-2765

ANNUAL FINANCIAL REPORT

2005

SANITARY DISTRICT

CITY OF HAMMOND

LAKE COUNTY, INDIANA



FILED
08/10/2006

TABLE OF CONTENTS

<u>Description</u>	<u>Page</u>
Officials	2
Independent Auditor's Report.....	3
Statement of Net Assets.....	4
Statement of Revenues, Expenses and Other Changes in Fund Net Assets	5
Statement of Cash Flows	6
Notes to Financial Statements	7-18
Required Supplementary Information:	
Schedule of Funding Progress	19
Audit Result and Comment:	
Penalties not Assessed	20
Exit Conference	21

OFFICIALS

<u>Office</u>	<u>Official</u>	<u>Term</u>
Controller	Barbara Cardwell	01-01-05 to 12-31-06
Mayor	Thomas McDermott, Jr.	01-01-04 to 12-31-07
President of the Board of Sanitary Commissioners	Stanley Dostatni	01-01-05 to 12-31-06
President of the Board of Public Works and Safety	William J. O'Connor	01-01-05 to 12-31-06
President of the Common Council	Daniel Repay Alfonso Salinas	01-01-05 to 12-31-05 01-01-06 to 12-31-06
District Manager	Michael T. Unger, PhD.	01-01-05 to 12-31-06
Business Manager	William Biller	01-01-05 to 12-31-06



STATE OF INDIANA
AN EQUAL OPPORTUNITY EMPLOYER

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INDEPENDENT AUDITOR'S REPORT

TO: THE OFFICIALS OF THE SANITARY DISTRICT, CITY OF HAMMOND, LAKE COUNTY, INDIANA

We have audited the accompanying financial statements of the business-type activities of the Sanitary District, a department of the City of Hammond, as of and for the year ended December 31, 2005. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

As discussed in Note I, the financial statements of the Sanitary District, City of Hammond, are intended to present the financial position, and the changes in financial position and cash flows of only that portion of the business-type activities of the City that is attributable to the transactions of the District. They do not purport to, and do not, present fairly the financial position of the City of Hammond as of December 31, 2005, and the changes in its financial position and its cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of the Sanitary District as of December 31, 2005, and the respective changes in financial position and cash flows, where applicable, thereof and for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

The Schedule of Funding Progress, as listed in the table of contents is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

STATE BOARD OF ACCOUNTS

June 22, 2006

SANITARY DISTRICT
CITY OF HAMMOND
STATEMENT OF NET ASSETS
December 31, 2005

Assets

Current assets:	
Cash and cash equivalents	\$ 545,304
Cash with fiscal agent	142,938
Accounts receivable (net of allowance)	853,888
Taxes receivable (net of allowance)	2,058,558
Intergovernmental receivables	18,915
Inventories	670,793
Prepaid items	<u>258,899</u>
 Total current assets	 <u>4,549,295</u>
Noncurrent assets:	
Restricted assets:	
Bond and interest cash and investments	1,530,457
Construction cash and investments	2,052,899
Bond and interest receivable	36,745
Taxes receivable (net of allowance)	3,077,412
Intergovernmental receivable	<u>18,715</u>
 Total restricted assets:	 <u>6,716,228</u>
 Deferred charges	 <u>466,217</u>
Capital assets:	
Land, improvements to land and construction in progress	7,334,878
Other capital assets (net of accumulated depreciation)	<u>107,971,714</u>
 Total capital assets	 <u>115,306,592</u>
 Total noncurrent assets	 <u>122,489,037</u>
 Total assets	 <u>127,038,332</u>

Liabilities

Current liabilities:	
Accounts payable	305,236
Accrued payroll and withholdings payable	182,511
Intergovernmental payable	677,356
Current liabilities payable from restricted assets:	
Contracts payable	264,267
General obligation bond payable	205,000
Loans payable	2,415,000
Accrued interest payable	<u>575,165</u>
 Total current liabilities	 <u>4,624,535</u>
Noncurrent liabilities:	
General obligation bonds payable	1,835,000
Loans payable	<u>26,927,507</u>
 Total noncurrent liabilities	 <u>28,762,507</u>
 Total liabilities	 <u>33,387,042</u>

Net Assets

Invested in capital assets, net of related debt	84,108,427
Restricted for debt service	4,088,164
Restricted for capital improvements	1,788,632
Unrestricted	<u>3,666,067</u>
 Total net assets	 <u>\$ 93,651,290</u>

The notes to the financial statements are an integral part of this statement.

SANITARY DISTRICT
CITY OF HAMMOND
STATEMENT OF REVENUES, EXPENSES AND OTHER CHANGES IN FUND NET ASSETS
As Of And For The Year Ended December 31, 2005

Operating revenues:	
Residential sales	\$ 3,610,349
Commercial and industrial sales	6,222,153
Municipal sales	954,656
Local tax distributions for sewer maintenance	4,388,190
Other charges for services	497,855
Other	<u>521,679</u>
 Total operating revenues	 <u>16,194,882</u>
Operating expenses:	
Sewer maintenance operations:	
Salaries and wages	746,781
Employee pensions and benefits	341,631
Materials and supplies	53,312
Repairs and maintenance	63,656
Contractual services	1,269,447
Fuel purchased	37,189
Utilities	50,076
Insurance	70,669
Miscellaneous	77,804
Pretreatment:	
Salaries and wages	152,755
Employee pensions and benefits	73,892
Materials and supplies	1,008
Contractual services	20,947
Fuel purchased	5,025
Insurance	4,405
Miscellaneous	396
Plant maintenance and operations:	
Salaries and wages	883,716
Employee pensions and benefits	625,865
Chemicals	177,845
Materials and supplies	2,132
Repairs and maintenance	1,124,452
Utilities	1,727,001
Sludge removal	409,086
Insurance	220,060
Miscellaneous	16,227
Collection system:	
Salaries and wages	472,871
Employee pensions and benefits	334,897
Materials and supplies	2,215
Repairs and maintenance	733,117
Utilities	557,140
Insurance	72,726
Miscellaneous	18,739
Administration and general:	
Salaries and wages	876,789
Employee pensions and benefits	620,960
Materials and supplies	94,178
Repairs and maintenance	31,382
Contractual services	230,443
Utilities	113,340
Insurance	95,593
Miscellaneous	420,313
Depreciation	<u>3,635,554</u>
 Total operating expenses	 <u>16,465,634</u>
 Operating loss	 <u>(270,752)</u>
Nonoperating revenues (expenses):	
Local tax distributions restricted for debt service	6,601,755
Interest expense	(1,377,291)
Amortization of debt issuance costs	<u>(48,351)</u>
 Total nonoperating revenues	 <u>5,176,113</u>
 Income before contributions and transfers	 4,905,361
Capital contributions	4,188,899
Transfers to City	<u>(501,867)</u>
 Change in net assets	 8,592,393
Total net assets - beginning	86,518,578
Prior period adjustment (See Note II. G.)	<u>(1,459,681)</u>
Total net assets - beginning, restated	<u>85,058,897</u>
Total net assets - ending	<u>\$ 93,651,290</u>

The notes to the financial statements are an integral part of this statement.

SANITARY DISTRICT
CITY OF HAMMOND
STATEMENT OF CASH FLOWS
As Of And For The Year Ended December 31, 2005

Cash flows from operating activities:	
Receipts from customers and users	\$ 15,515,436
Payments to suppliers and contractors	(7,803,707)
Payments to employees	<u>(5,128,986)</u>
Net cash provided by operating activities	<u>2,582,743</u>
Cash flows from noncapital financing activities:	
Proceeds from tax anticipation notes	1,751,012
Transfer to City	(501,867)
Principal paid on tax anticipation notes	(2,364,901)
Interest paid on notes	<u>(62,549)</u>
Net cash used by noncapital financing activities	<u>(1,178,305)</u>
Cash flows from capital and related financing activities:	
Local tax distributions	5,953,983
Proceeds from capital debt	1,985,666
Proceeds from tax anticipation notes	2,857,458
Acquisition and construction of capital assets	(3,918,450)
Principal paid on capital debt	(3,120,000)
Principal paid on tax anticipation notes	(3,107,821)
Interest paid on capital debt	<u>(1,308,864)</u>
Net cash used by capital and related financing activities	<u>(658,028)</u>
Net increase in cash and cash equivalents	746,410
Cash and cash equivalents, January 1	<u>3,525,188</u>
Cash and cash equivalents, December 31	<u>\$ 4,271,598</u>
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	\$ (270,752)
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation expense	3,635,554
(Increase) decrease in assets:	
Accounts receivable	(186,507)
Taxes receivable	(462,450)
Intergovernmental receivable	26,887
Bond and interest receivable	2,337
Deferred debits	(59,713)
Inventories	(71,511)
Prepaid items	(117,435)
Increase (decrease) in liabilities:	
Accounts payable	47,680
Accrued payroll and withholdings payable	1,170
Intergovernmental payable	<u>37,483</u>
Total adjustments	<u>2,853,495</u>
Net cash provided by operating activities	<u>\$ 2,582,743</u>
Noncash investing, capital and financing activities:	
Acquisition of capital assets through contracts payable (net)	\$ 246,215
Contributions of capital assets from government	4,188,899
Transfer of construction in progress to capital assets	2,559,070

The notes to the financial statements are an integral part of this statement.

SANITARY DISTRICT
CITY OF HAMMOND
NOTES TO FINANCIAL STATEMENTS

I. Summary of Significant Accounting Policies

A. Reporting Entity

The financial statements reflect only the activity of the District and are not intended to present fairly the position of the City of Hammond (City), and the results of its operations and cash flows of its enterprise funds. The District, whose operations are controlled by the City, represents a substantial portion of the City's enterprise funds.

B. Fund Financial Statements

Business-type activity financial statements consist of the Statement of Net Assets; Statement of Revenues, Expenses, and Other Changes in Fund Net Assets; and the Statement of Cash Flows. Business-type activities rely to a significant extent on fees and charges for support.

C. Measurement Focus, Basis of Accounting and Financial Statement Presentation

The accounts of the business-type activity are maintained and the financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized when incurred.

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

D. Assets, Liabilities and Net Assets

1. Deposits and Investments

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

State statute (IC 5-13-9) authorizes the District to invest in securities, including but not limited to, federal government securities, repurchase agreements, and certain money market mutual funds. Certain other statutory restrictions apply to all investments made by local governmental units.

2. Property Taxes

Property taxes levied are collected by the County Treasurer and are distributed to the government in June and in December. State statutes (IC 6-1.1-17-16) require the Indiana Department of Local Government Finance to establish property tax rates and levies by February 15. These rates were based upon the preceding year's March 1 (lien date) assessed valuations adjusted for various tax credits. Taxable property is assessed at 100% of the true tax value (determined in

SANITARY DISTRICT
CITY OF HAMMOND
NOTES TO FINANCIAL STATEMENTS
(Continued)

accordance with rules and regulations adopted by the Indiana Department of Local Government Finance). Taxes may be paid in two equal installments that become delinquent if not paid by May 10 and November 10, respectively. Delinquent property taxes outstanding at year end, net of allowances for uncollectible accounts, are recorded as a receivable. The property taxes collected for the sewer maintenance function are classified as operating revenue since the expenses are an operating expense. The property taxes collected for debt repayment are classified as nonoperating. See note III. D., for further discussion regarding the delay of property tax collections.

3. Inventories, Prepaid Items and Deferred Debits

All inventories are valued at cost using the first in/first out (FIFO) method. Inventories are recorded as expenditures when consumed rather than when purchased.

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

Based upon an agreement between user cities and the District, a set rate is paid. Annually, a study is performed to determine if the user cities have underpaid or overpaid. The underpayments are reflected as deferred debits in addition to the amortization of debt issuance costs.

4. Restricted Assets

Certain resources set aside for repayment of debt and District improvements are classified as restricted assets on the statement of net assets in accordance with the debt instruments and grant agreements.

5. Capital Assets

Capital assets, which include property, plant, and equipment, are reported in the financial statements.

Capital assets are reported at actual or estimated historical cost based on appraisals or deflated current replacement cost. Contributed or donated assets are reported at estimated fair value at the time received.

Capitalization thresholds (the dollar values above which asset acquisitions are added to the capital asset accounts), depreciation methods and estimated useful lives of capital assets are as follows:

	<u>Capitalization Threshold</u>	<u>Depreciation Method</u>	<u>Estimated Useful Life</u>
Land improvements	\$ 5,000	Straight-line	25 to 60 years
Buildings	5,000	Straight-line	60 years
Building improvements	5,000	Straight-line	20 to 40 years
Major equipment	5,000	Straight-line	10 to 40 years
Minor equipment	5,000	Straight-line	3 to 10 years

For depreciated assets, the cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized.

SANITARY DISTRICT
CITY OF HAMMOND
NOTES TO FINANCIAL STATEMENTS
(Continued)

6. Compensated Absences

- a. Sick Leave – District employees earn sick leave at the rate of 1 day per month. Unused sick leave may be accumulated to a maximum of 75 days. For each 5 days earned in excess of the allowable accumulation, the excess days shall be converted to equal 1 extra regular vacation day. One week of accumulated sick leave is paid to employees through cash payments upon termination if the employee has accumulated 75 days.
- b. Vacation Leave – District employees earn vacation leave at rates from 10 days to 30 days per year based upon the number of years of service. Vacation leave does not accumulate from year to year.
- c. Personal Leave – District employees earn personal leave at the rate of 3 days per year. Personal leave does not accumulate from year to year.

No liability is reported for vacation, sick, or personal leave.

7. Long-Term Obligations

Long-term debt and other long-term obligations are reported as liabilities in the statement of net assets. Issuance costs are reported as deferred charges and amortized over the life of the related debt using the straight-line method.

II. Detailed Notes on All Funds

A. Deposits and Investments

Deposits, made in accordance with Indiana Code 5-13, with financial institutions in the State of Indiana at year end were entirely insured by the Federal Depository Insurance Corporation or by the Indiana Public Deposit Insurance Fund. This includes any deposit accounts issued or offered by a qualifying financial institution.

B. Capital Assets

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

	Beginning Balance	Prior Period Adjustment	Restated Beginning Balance	Increases	Decreases	Reclassified	Ending Balance
Capital assets, not being depreciated:							
Land	\$ 497,919	\$ -	\$ 497,919	\$ -	\$ -	\$ -	\$ 497,919
Construction in progress	5,609,705	-	5,609,705	3,786,324	2,559,070	-	6,836,959
 Total capital assets, not being depreciated	 6,107,624	 -	 6,107,624	 3,786,324	 2,559,070	 -	 7,334,878

SANITARY DISTRICT
CITY OF HAMMOND
NOTES TO FINANCIAL STATEMENTS
(Continued)

	Beginning Balance	Prior Period Adjustment	Restated Beginning Balance	Increases	Decreases	Reclassified	Ending Balance
Capital assets, being depreciated:							
Land improvements	90,288,639	-	90,288,639	5,765,553	-	(3,686,641)	92,367,551
Buildings	37,552,640	-	37,552,640	-	-	3,686,641	41,239,281
Building improvements	6,597,528	-	6,597,528	-	-	-	6,597,528
Major equipment	40,461,662	-	40,461,662	1,349,083	-	-	41,810,745
Minor equipment	1,461,618	-	1,461,618	11,674	-	-	1,473,292
Totals	176,362,087	-	176,362,087	7,126,310	-	-	183,488,397
Less accumulated depreciation for:							
Land improvements	30,904,060	957,402	31,861,462	1,553,765	-	-	33,415,227
Buildings	16,231,494	74,959	16,306,453	692,593	-	-	16,999,046
Building improvements	3,780,206	60,256	3,840,462	168,504	-	-	4,008,966
Major equipment	18,426,683	268,846	18,695,529	1,125,935	-	-	19,821,464
Minor equipment	1,079,004	98,218	1,177,222	94,758	-	-	1,271,980
Totals	70,421,447	1,459,681	71,881,128	3,635,555	-	-	75,516,683
Total capital assets, being depreciated, net	105,940,640	(1,459,681)	104,480,959	3,490,755	-	-	107,971,714
Total capital assets, net	<u>\$ 112,048,264</u>	<u>\$ (1,459,681)</u>	<u>\$ 110,588,583</u>	<u>\$ 7,277,079</u>	<u>\$ 2,559,070</u>	<u>\$ -</u>	<u>\$ 115,306,592</u>

C. Construction Commitments

Construction work in progress is composed of the following:

Project	Total Project Authorized	Expended to December 31, 2005	Committed
Schoon Ditch CSO Phase II	\$ 1,409,888	\$ 1,211,058	\$ 198,830
SCADA	1,716,500	1,477,779	238,721
CSO Storage Basin	425,000	407,669	17,331
WTPP Projects	3,294,998	2,013,153	1,281,845
Gas Engine	2,000,000	856,126	1,143,874
Boreman Expressway	400,000	336,700	63,300
LCR CSO Viscloskey	5,000,000	534,474	4,465,526
Totals	<u>\$ 14,246,386</u>	<u>\$ 6,836,959</u>	<u>\$ 7,409,427</u>

SANITARY DISTRICT
CITY OF HAMMOND
NOTES TO FINANCIAL STATEMENTS
(Continued)

D. Short-Term Liabilities

The District issues tax anticipation notes in advance of property tax collections. These notes are necessary because the government has cash flow needs before property tax collections are received.

Short-term debt activity for the year ended December 31, 2005, was as follows:

	Beginning Balance	Issued/ Draws	Redeemed Repayments	Ending Balance
Notes payable	\$ 864,252	\$ 4,608,470	\$ 5,472,722	\$ -

E. Long-Term Liabilities

1. General Obligation Bonds

The District issues general obligation bonds to provide funds for the acquisition and construction of major capital facilities.

General obligation bonds are direct obligations and pledge the full faith and credit of the government. General obligation bonds currently outstanding at year end are as follows:

Purpose	Interest Rates	Amount
2003 Special taxing district refunding bonds	5.72% to 6.12%	\$ 2,040,000

Annual debt service requirements to maturity for the general obligation bond is as follows:

Year Ended December 31	Principal	Interest
2006	\$ 205,000	\$ 117,989
2007	220,000	105,405
2008	230,000	91,800
2009	245,000	77,265
2010	260,000	61,812
2011-2013	880,000	82,926
Totals	\$ 2,040,000	\$ 537,197

SANITARY DISTRICT
CITY OF HAMMOND
NOTES TO FINANCIAL STATEMENTS
(Continued)

2. Loans Payable

The District has entered into various loans with the State Revolving Loan Fund. Under the terms of the loans, revenue bonds have been purchased by the Indiana Bond Bank, the proceeds of which are set aside to finance District improvements. Funds are loaned to the District as costs are accrued, to the maximum allowed. The District has drawn down all of the 1993, 1997, and 1998 Loan Program Funds, however, the 2001A and 2001B Loan Program Funds for \$9,500,000 and \$10,500,000, respectively, are still being drawn down. Annual debt service requirements to maturity for the loans are as follows:

Year Ended December 31	Principal	Interest
2006	\$ 2,415,000	\$ 1,240,313
2007	2,460,000	1,146,300
2008	2,500,000	1,050,713
2009	2,545,000	953,563
2010	2,585,000	854,838
2011-2015	11,000,000	2,838,925
2016-2020	4,545,394	1,204,200
2021-2024	<u>1,292,113</u>	<u>103,800</u>
Totals	<u>\$ 29,342,507</u>	<u>\$ 9,392,652</u>

3. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2005, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
General obligation bonds	\$ 2,780,000	\$ -	\$ 740,000	\$ 2,040,000	\$ 205,000
Loans payable	29,736,841	1,985,666	2,380,000	29,342,507	2,415,000
Total long-term liabilities	<u>\$ 32,516,841</u>	<u>\$ 1,985,666</u>	<u>\$ 3,120,000</u>	<u>\$ 31,382,507</u>	<u>\$ 2,620,000</u>

F. Restricted Assets

The balances of restricted asset accounts for debt repayment and improvements are as follows:

Bond and interest cash and cash equivalents	\$ 1,530,457
Construction cash and cash equivalents	2,052,899
Bond and interest receivable	36,745
Taxes receivable (net of allowances)	3,077,412
Intergovernmental receivable	<u>18,715</u>
Total restricted assets	<u>\$ 6,716,228</u>

SANITARY DISTRICT
CITY OF HAMMOND
NOTES TO FINANCIAL STATEMENTS
(Continued)

G. Restatements

For the year ended December 31, 2005, certain changes have been made to the financial statements to more appropriately reflect financial activity of the District. Prior period adjustments represent an increase in accumulated depreciation and corresponding decrease in net assets due to correction of errors made in calculating prior years' annual depreciation expense.

Balance as Reported December 31, 2004	Prior Period Adjustments	Balance as Restated January 1, 2005
\$ 86,518,578	\$ (1,459,681)	\$ 85,058,897

III. Other Information

A. Risk Management

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; job related illnesses or injuries to employees; medical benefits to employees, retirees, and dependents (excluding postemployment benefits); and natural disasters.

The risks of torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters are covered by commercial insurance from independent third parties. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years. There were no significant reductions in insurance by major category of risk.

Medical Benefits and Job Related Illnesses or Injuries to Employees and Liability Insurance

The City has chosen to establish a risk financing fund for risks associated with medical, vision, dental, worker's compensation and liability claims. The District has chosen to participate in this fund for medical, vision and dental claims. The risk financing fund is accounted for in the City's Self-Insurance Fund (an internal service fund) where assets are set aside for claim settlements. An excess policy through commercial insurance covers individual claims in excess of \$150,000 per year. Settled claims resulting from this risk did not exceed commercial insurance coverage for the past three years. A premium is charged to each fund that accounts for payroll. The total charge allocated to each of the funds is calculated using trends in actual claims experience. Provisions are also made for unexpected and unusual claims.

Claim expenditures and liabilities of the fund are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported (IBNRs). Claim liabilities are calculated considering the effects of inflation, recent claim settlement trends, including frequency and amounts of pay outs, and other economic and social factors.

SANITARY DISTRICT
CITY OF HAMMOND
NOTES TO FINANCIAL STATEMENTS
(Continued)

Changes in the balance of the District's medical claim liabilities during the past two years are as follows:

	2005	2004
Unpaid claims, beginning of fiscal year	\$ 2,499,183	\$ 1,850,930
Incurred claims and changes in estimates	13,842,926	14,163,475
Claim payments	16,186,094	13,515,222
Unpaid claims, end of fiscal year	\$ 156,015	\$ 2,499,183

Unemployment Compensation

The District has chosen to establish a risk financing fund for risks associated with unemployment compensation claims. The risk financing fund is accounted for in the Unemployment Compensation Account where assets are set aside for claim settlements. Provisions are also made for unexpected and unusual claims.

Claim expenditures and liabilities of the account are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Claim liabilities are calculated considering the effects of inflation, recent claim settlement trends, including frequency and amounts of pay outs, and other economic and social factors.

Changes in the balance of claim liabilities during the past two years are as follows:

	2005	2004
Unpaid claims, beginning of fiscal year	\$ -	\$ -
Incurred claims and changes in estimates	-	14,491
Claim payments	-	14,491
Unpaid claims, end of fiscal year	\$ -	\$ -

B. Rate Structure

The current rate structure was approved by the Common Council on January 23, 2006.

C. Cash with Fiscal Agent

The Hammond and Munster Water Utilities serve as billing and collection agents for the District user charge system. The Hammond Water Utility deposits daily collections directly to the District's bank accounts. Thus, the amount reported as Cash with Fiscal Agent represents collections by the Munster Water Utility not yet remitted to the District.

SANITARY DISTRICT
CITY OF HAMMOND
NOTES TO FINANCIAL STATEMENTS
(Continued)

D. Subsequent Events

Property tax rates and levies for 2004 taxes payable in 2005 were not established by February 15, 2005, as required by state statute due to the delay in the completion of the reassessment of Lake County. The 2005 property tax rates and levies were not established until October 2004; thus, the property taxes were not billed or collected timely. The final settlement of the 2004 taxes payable in 2005, were just being distributed to the various governmental entities in March 2006. The 2005 pay 2006 tax rates and levies have yet to be established.

To offset the delay in tax collections, the District authorized the issuance of tax anticipation notes through the Indiana Bond Bank to mature on December 31, 2006. In January 2006, the District received \$3,811,506 of note proceeds.

On January 23, 2006, the City Council approved Ordinance 8731 modifying user fees for the treatment and disposal of sewage. Ordinance 8731 also created a Stormwater Customer Charge.

On February 15, 2005, the District approved Resolution 12-2005 declaring the District's intent to apply to the Great Lakes National Program Office (GLNPO) to participate in the cost sharing for the Optimized River Route of the CSO Basin Project contingent upon the receipt of \$4,501,445 of federal funds, or 65% of the cost, to design and install a pipeline in the north bank of the Grand Calumet River. The District agreed to participate by contributing \$2,423,855, or the 35% local match, by procuring a local bond issue. As of June 22, 2006, this project had not begun.

On February 15, 2005, the District approved Resolution 17-2005 to authorize and issue one or more special taxing district bonds payable from a special tax levied upon all of the taxable property in the Sanitary District in an aggregate principal amount not to exceed \$24,000,000 to procure funds to be applied to the costs of designing, planning, engineering, and constructing various public improvement projects. On March 15, 2005, the District held a public hearing and adopted the confirming Resolution 21-2005. The bonds shall bear interest at a rate or rates not exceeding 8% per annum and is to be paid semiannually on the 15th day of January and July. As of June 22, 2006, no bonds have been sold.

E. Transfers Out

The District transferred \$501,867 to the City as payment in lieu of taxes.

F. Postemployment Benefits

In addition to the pension benefits described below, the District provides postemployment medical insurance benefits, as authorized by Indiana Code 5-10-8, to all employees who retire from the District on or after attaining age 65 with at least 15 years of service. Currently, 18 retirees meet these eligibility requirements. The District provides \$1,000 per month per retiree and the retiree remits the balance of the premium to the City Controller. Expenditures for those postemployment benefits are recognized on a pay-as-you-go basis. During the year ended December 31, 2005, expenditures of \$219,000 were recognized for postemployment benefits.

SANITARY DISTRICT
CITY OF HAMMOND
NOTES TO FINANCIAL STATEMENTS
(Continued)

G. Consent Decree

In April of 1999, the District entered into a Consent Decree with the United States Environmental Protection Agency (EPA) to implement improvements to address the effects of sediment contamination in the West Branch of the Grand Calumet River.

For the Combined Sewer Overflow (CSO) Operations, the District agreed to install a metering and telemetry system for all pump stations, of which two-thirds were to be completed by June 1, 2003, and all pump stations to be completed by October 31, 2005. These deadlines were met.

For CSO Control, the District was to initiate construction by May 1, 2004, for new reservoir and pump station improvements, sewer separations, sewer interceptors, and sewer interceptor improvements in order to eliminate the use of the Columbia, Sohl and Johson Avenues CSOs. The projects are to be completed by May 1, 2009, and achieve operational status for all new or modified components and cease all discharges from Columbia, Sohl, and Johnson Avenues CSOs. The failure to comply with any completion date specified and remain in noncompliance for more than 90 days, the District shall not thereafter make any new hook-up, connection, or extension to its sewage system until the District certified to EPA and IDEM that it has completed the required task.

For any noncompliance of the Consent Decree requirements noted above, the stipulated penalty would be applicable based on the period of noncompliance. From the 1st to the 30th day of continuous violation, \$500 per day per violation; from the 31st to the 60th day of continuous violation, \$750 per day per violation; and after 60 days of continuous violation, \$1,000 per day per violation.

The District is required to report semiannually to the EPA and Indiana Department of Environmental Management (IDEM) on the status of the District's compliance with all requirements of the Decree. Reports were sent on June 16 and December 6, 2005.

H. Pension Plan

Public Employees' Retirement Fund

Plan Description

The City, including the District, contributes to the Indiana Public Employees' Retirement Fund (PERF), a defined benefit pension plan. PERF is an agent multiple-employer public employee retirement system, which provides retirement benefits to plan members and beneficiaries. All full-time employees are eligible to participate in the defined benefit plan. State statutes (IC 5-10.2 and 5-10.3) govern, through the PERF Board, most requirements of the system and give the District authority to contribute to the plan. The PERF retirement benefit consists of the pension provided by employer contributions plus an annuity provided by the member's annuity savings account. The annuity savings account consists of member's contributions, set by state statute at 3% of compensation, plus the interest credited to the member's account. The employer may elect to make the contributions on behalf of the member.

PERF administers the plan and issues a publicly available financial report that includes financial statements and required supplementary information for the plan as a whole and for its participants. The report may be obtained by contacting:

SANITARY DISTRICT
CITY OF HAMMOND
NOTES TO FINANCIAL STATEMENTS
(Continued)

Public Employees' Retirement Fund
Harrison Building, Room 800
143 West Market Street
Indianapolis, IN 46204
Ph. (317) 233-4162

Funding Policy and Annual Pension Cost

The contribution requirements of plan members for PERF are established by the Board of Trustees of PERF. The City's, including the District's, annual pension cost and related information, as provided by the actuary, is presented in this note.

Information to segregate the assets/liabilities and the actuarial study figures between the City and the District is not available. Therefore, the liability for Net Pension Obligation (NPO) is considered an obligation of the City as a whole and is not presented as an asset/liability of the District.

Actuarial Information for the Above Plan

	PERF
Annual required contribution	\$ 904,017
Interest on net pension obligation	(56,638)
Adjustment to annual required contribution	64,543
Annual pension cost	911,922
Contributions made	920,486
Decrease in net pension obligation	(8,564)
Net pension obligation, beginning of year	(781,215)
Net pension obligation, end of year	\$ (789,779)
Contribution rates:	
District	4.75%
Plan members	3%
Actuarial valuation date	07-01-05
Actuarial cost method	Entry age
Amortization method	Level percentage of projected payroll, closed
Amortization period	40 years
Amortization period (from date)	07-01-97
Asset valuation method	4 year smoothed market

SANITARY DISTRICT
CITY OF HAMMOND
NOTES TO FINANCIAL STATEMENTS
(Continued)

Actuarial Assumptions	PERF
Investment rate of return	7.25%
Projected future salary increases:	
Total	5%
Attributed to inflation	4%
Attributed to merit/seniority	1%
Cost-of-living adjustments	2%

Three Year Trend Information

	Year Ending	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
PERF	06-30-03	\$ 866,712	90%	\$ (649,056)
	06-30-04	734,971	118%	(781,215)
	06-30-05	911,922	125%	(789,779)

SANITARY DISTRICT
 REQUIRED SUPPLEMENTARY INFORMATION
 SCHEDULE OF FUNDING PROGRESS

Public Employees' Retirement Fund

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Excess of Assets Over (Unfunded) AAL (a-b)	Funded Ratio (a/b)	Covered Payroll (c)	Excess (Unfunded) AAL as a Percentage of Covered Payroll ((a-b)/c)
07-01-03	\$ 18,586,612	\$ 17,901,034	\$ 685,578	104%	\$ 17,270,930	4%
07-01-04	18,797,977	19,498,861	(700,884)	96%	18,447,579	(4%)
07-01-05	19,522,708	22,345,580	(2,822,872)	87%	19,211,969	(15%)

HAMMOND SANITARY DISTRICT
AUDIT RESULT AND COMMENT

PENALTIES NOT ASSESSED

The District is not applying a 10% penalty to customer accounts that have not paid within 30 days of the due date in accordance with state statute.

Indiana Code 36-9-25-11 states in part: "(f) If a fee established is not paid within thirty (30) days after it is due, the amount, together with a penalty of ten percent (10%) and a reasonable attorney's fee, may be recovered by the board from the delinquent user or owner of the property served in a civil action in the name of the municipality. (g) Fees assessed against real property under this section also constitute a lien against the property assessed. The lien attaches at the time of filing of the notice of lien in the county recorder's office. The lien is superior to all other liens except tax liens, and shall be enforced and foreclosed in the same manner as is provided for liens under IC 36-9-23-33 and IC 36-9-23-3 . . ."

SANITARY DISTRICT
CITY OF HAMMOND
EXIT CONFERENCE

The contents of this report were discussed on June 22, 2006, with Michael T. Unger, PhD., District Manager; Stanley Dostatni, President of the Board of Sanitary Commissioners; Barbara Cardwell, City Controller; and Joseph Allegretti, District Attorney.