

**STATE BOARD OF ACCOUNTS**  
**302 West Washington Street**  
**Room E418**  
**INDIANAPOLIS, INDIANA 46204-2769**

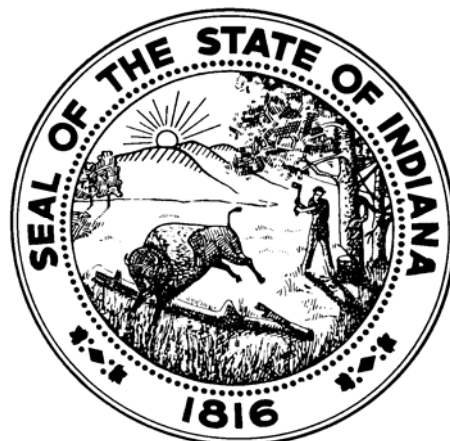
ANNUAL FINANCIAL REPORT

2006

SANITARY DISTRICT

CITY OF HAMMOND

LAKE COUNTY, INDIANA



**FILED**  
09/20/2007



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OFFICIALS

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



**STATE OF INDIANA**  
AN EQUAL OPPORTUNITY EMPLOYER

STATE BOARD OF ACCOUNTS  
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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, 2006. 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, 2006, 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 for the Sanitary District, as of December 31, 2006, and the respective changes in financial position and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Utility has not presented Management's Discussion and Analysis that the Government Accounting Standards Board has determined is necessary to supplement, although not required to part of, the basic financial statements.

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 accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management, regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

STATE BOARD OF ACCOUNTS

May 3, 2007

SANITARY DISTRICT  
CITY OF HAMMOND  
STATEMENT OF NET ASSETS  
December 31, 2006

<u>Assets</u>	<u>Wastewater Utility</u>	<u>Storm Water Utility</u>
Current assets:		
Cash and cash equivalents	\$ 685,514	\$ 204,878
Cash with fiscal agent	130,169	1,798
Accounts receivable (net of allowance)	824,186	23,455
Taxes receivable (net of allowance)	363,394	-
Intergovernmental receivables	130,362	-
Inventories	697,796	-
Prepaid items	<u>259,090</u>	<u>-</u>
Total current assets	<u>3,090,511</u>	<u>230,131</u>
Noncurrent assets:		
Restricted assets:		
Bond and interest cash and investments	2,456,471	-
Construction cash and investments	1,858,547	-
Taxes receivable (net of allowance)	474,866	-
Intergovernmental receivable	<u>1,026,197</u>	<u>-</u>
Total restricted assets	<u>5,816,081</u>	<u>-</u>
Deferred charges	<u>464,678</u>	<u>-</u>
Capital assets:		
Land, improvements to land and construction in progress	4,792,263	-
Other capital assets (net of accumulated depreciation)	<u>109,654,274</u>	<u>-</u>
Total capital assets	<u>114,446,537</u>	<u>-</u>
Total noncurrent assets	<u>120,727,296</u>	<u>-</u>
Total assets	<u>123,817,807</u>	<u>230,131</u>
<u>Liabilities</u>		
Current liabilities:		
Accounts payable	374,255	-
Accrued payroll and withholdings payable	207,307	-
Intergovernmental payable	190,000	-
Compensated absences payable	71,108	-
Current liabilities payable from restricted assets:		
Contracts payable	133,054	-
General obligation bond payable	220,000	-
Loans payable	2,460,000	-
Accrued interest payable	<u>554,807</u>	<u>-</u>
Total current liabilities	<u>4,210,531</u>	<u>-</u>
Noncurrent liabilities:		
General obligation bonds payable	1,615,000	-
Loans payable	<u>27,294,480</u>	<u>-</u>
Total noncurrent liabilities	<u>28,909,480</u>	<u>-</u>
Total liabilities	<u>33,120,011</u>	<u>-</u>
<u>Net Assets</u>		
Invested in capital assets, net of related debt	83,203,047	-
Restricted for debt service	2,572,724	-
Restricted for capital improvements	2,555,496	-
Unrestricted	<u>2,366,529</u>	<u>230,131</u>
Total net assets	<u>\$ 90,697,796</u>	<u>\$ 230,131</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, 2006

	Wastewater Utility	Storm Water Utility
Operating revenues:		
Residential sales	\$ 3,324,355	\$ -
Commercial and industrial sales	5,697,942	-
Municipal sales	2,161,746	-
Flat rate	-	231,572
Local tax distributions for sewer maintenance	1,829,723	-
Other charges for services	393,008	-
Other	860,811	-
	<u>14,267,585</u>	<u>231,572</u>
Total operating revenues		
Operating expenses:		
Sewer maintenance operations:		
Salaries and wages	772,785	-
Employee pensions and benefits	352,470	-
Materials and supplies	64,001	-
Repairs and maintenance	77,410	-
Contractual services	1,292,324	-
Fuel purchased	47,423	-
Utilities	50,054	-
Insurance	89,936	-
Miscellaneous	49,564	-
Pretreatment:		
Salaries and wages	88,835	-
Employee pensions and benefits	48,888	-
Materials and supplies	11,750	-
Contractual services	45,672	-
Fuel purchased	3,489	-
Insurance	6,541	-
Miscellaneous	350	-
Plant maintenance and operations:		
Salaries and wages	945,844	-
Employee pensions and benefits	484,733	-
Chemicals	140,464	-
Materials and supplies	3,284	-
Repairs and maintenance	1,627,879	-
Contractual services	1,875	-
Utilities	1,906,873	-
Sludge removal	288,413	-
Insurance	16,588	-
Miscellaneous	213,960	-
Collection system:		
Salaries and wages	565,761	-
Employee pensions and benefits	288,785	-
Materials and supplies	1,311	-
Repairs and maintenance	1,008,646	-
Contractual services	669,965	-
Insurance	84,880	-
Miscellaneous	3,905	-
Administration and general:		
Salaries and wages	903,201	-
Employee pensions and benefits	519,711	-
Materials and supplies	78,703	-
Repairs and maintenance	125,162	-
Contractual services	461,159	-
Utilities	101,536	-
Insurance	40,059	-
Miscellaneous	179,949	-
Storm Water:		
Contractual services	-	1,441
Depreciation	4,051,836	-
	<u>17,715,974</u>	<u>1,441</u>
Total operating expenses		
Operating loss	<u>(3,448,389)</u>	<u>230,131</u>
Nonoperating revenues (expenses):		
Local tax distributions restricted for debt service	2,354,499	-
Interest expense	(1,307,123)	-
Amortization of debt issuance costs	(35,401)	-
	<u>1,011,975</u>	<u>-</u>
Total nonoperating revenues (expenses)		
Income before contributions and transfers	(2,436,414)	230,131
Transfers to City	<u>(517,080)</u>	<u>-</u>
Change in net assets	(2,953,494)	230,131
Total net assets - beginning	<u>93,651,290</u>	<u>-</u>
Total net assets - ending	<u>\$ 90,697,796</u>	<u>\$ 230,131</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, 2006

	Wastewater Utility	Storm Water Utility
Cash flows from operating activities:		
Receipts from customers and users	\$ 15,965,904	\$ 208,117
Payments to suppliers and contractors	(9,138,656)	(1,441)
Payments to employees	<u>(4,875,109)</u>	<u>-</u>
Net cash provided by operating activities	<u>1,952,139</u>	<u>206,676</u>
Cash flows from noncapital financing activities:		
Proceeds from tax anticipation notes	1,448,986	-
Transfer to City	(517,080)	-
Principal paid on tax anticipation notes	(1,448,986)	-
Interest paid on notes	<u>(147,057)</u>	<u>-</u>
Net cash used by noncapital financing activities	<u>(664,137)</u>	<u>-</u>
Cash flows from capital and related financing activities:		
Local tax distributions	3,949,563	-
Proceeds from capital debt	2,826,973	-
Proceeds from tax anticipation notes	2,362,520	-
Acquisition and construction of capital assets	(3,322,995)	-
Principal paid on capital debt	(2,620,000)	-
Principal paid on tax anticipation notes	(2,362,520)	-
Loan issuance costs paid from capital debt	(82,017)	-
Interest paid on capital debt	<u>(1,180,423)</u>	<u>-</u>
Net cash used by capital and related financing activities	<u>(428,899)</u>	<u>-</u>
Net increase in cash and cash equivalents	859,103	206,676
Cash and cash equivalents, January 1	<u>4,271,598</u>	<u>-</u>
Cash and cash equivalents, December 31	<u>\$ 5,130,701</u>	<u>\$ 206,676</u>
Reconciliation of operating income (loss) to net cash provided by operating activities:		
Operating income (loss)	\$ (3,448,389)	\$ 230,131
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:		
Depreciation expense	4,051,836	-
(Increase) decrease in assets:		
Accounts receivable	29,702	(23,455)
Taxes receivable	1,695,164	-
Intergovernmental receivable	(111,447)	-
Bond and interest receivable	36,745	-
Deferred debits	48,155	-
Inventories	(27,003)	-
Prepaid items	(191)	-
Increase (decrease) in liabilities:		
Accounts payable	69,019	-
Accrued payroll and withholdings payable	24,796	-
Intergovernmental payable	(487,356)	-
Compensated absences payable	<u>71,108</u>	<u>-</u>
Total adjustments	<u>5,400,528</u>	<u>(23,455)</u>
Net cash provided by operating activities	<u>\$ 1,952,139</u>	<u>\$ 206,676</u>
Noncash investing, capital and financing activities:		
Acquisition of capital assets through contracts payable (net)	\$ 88,102	\$ -
Disposal of obsolete asset	32,377	-
Transfer of construction in progress to capital assets	5,497,042	-

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 on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

D. Assets, Liabilities and Net Assets or Equity

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.

Investment income, including changes in the fair value of investments, is reported as revenue in the operating statement.

2. Property Taxes

Property taxes levied are collected by the County Treasurer and are distributed to the primary government in June and in December. State statutes (IC 6-1.1-17-16) require the Department of Local Government Finance to establish property tax rates and levies by February 15. These rates

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

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 accordance with rules and regulations adopted by the 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 taxes collected for debt repayment are classified as nonoperating.

3. Inventories and Prepaid Items

All inventories are valued at cost using the first in/first out (FIFO) method. Inventories of governmental funds 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 in both government-wide and fund financial statements.

Based upon an agreement between user cities/towns and the District, a set rate is paid. Annually, a study is performed to determine if the user cities/towns 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 the repayment of debt and District improvements, are classified as restricted assets on the statement of net assets balance sheet 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

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

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.

Major outlays for capital assets and improvements are capitalized as projects are constructed.

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 regular vacation day. One week of accumulated sick leave is paid to union employees through cash payments upon termination if the employee has accumulated 75 days. Nonunion employees eligible for retirement, or upon separation of employment with at least 10 years of full-time service, will be reimbursed 1 days pay for each 4 days of unused sick leave up to the accumulation of 75 days. Nonunion employees with at least 15 years of full-time service will be reimbursed 1 days pay for each 2 days of unused sick leave, up to the accumulation of 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.

Sick leave is accrued when incurred.

No liability is reported for vacation and 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 term of the related debt.

II. Detailed Notes on All Funds

A. Deposits and Investments

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. Indiana Code 5-13-8-1 allows a political subdivision of the State of Indiana to deposit public funds in a financial institution only if the financial institution is a depository eligible to receive state funds; and has a principal office or branch that qualifies to receive public funds of the political subdivision. The bank balances were insured by the Federal Deposit Insurance Corporation or the Public Deposit Insurance Fund, which covers all public funds held in approved depositories.

B. Capital Assets

Capital asset activity for the year ended December 31, 2006, was as follows:

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

	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, not being depreciated:				
Land	\$ 497,919	\$ -	\$ -	\$ 497,919
Construction in progress	<u>6,836,959</u>	<u>2,954,427</u>	<u>5,497,042</u>	<u>4,294,344</u>
 Total capital assets, not being depreciated	 <u>7,334,878</u>	 <u>2,954,427</u>	 <u>5,497,042</u>	 <u>4,792,263</u>
Capital assets, being depreciated:				
Land improvements	92,367,551	1,569,425	-	93,936,976
Buildings	41,239,281	23,291	-	41,262,572
Building improvements	6,597,528	293,351	-	6,890,879
Major equipment	41,810,745	3,268,435	32,377	45,046,803
Minor equipment	<u>1,473,292</u>	<u>579,894</u>	<u>-</u>	<u>2,053,186</u>
 Totals	 <u>183,488,397</u>	 <u>5,734,396</u>	 <u>32,377</u>	 <u>189,190,416</u>
Less accumulated depreciation for:				
Land improvements	33,415,227	1,855,835	-	35,271,062
Buildings	16,999,046	674,543	-	17,673,589
Building improvements	4,008,966	192,064	-	4,201,030
Major Equipment	19,821,464	1,108,326	32,377	20,897,413
Minor equipment	<u>1,271,980</u>	<u>221,068</u>	<u>-</u>	<u>1,493,048</u>
 Totals	 <u>75,516,683</u>	 <u>4,051,836</u>	 <u>32,377</u>	 <u>79,536,142</u>
 Total capital assets, being depreciated, net	 <u>107,971,714</u>	 <u>1,682,560</u>	 <u>-</u>	 <u>109,654,274</u>
 Total capital assets, net	 <u>\$ 115,306,592</u>	 <u>\$ 4,636,987</u>	 <u>\$ 5,497,042</u>	 <u>\$ 114,446,537</u>

C. Construction Commitments

Construction work in progress is composed of the following:

Project	Total Project Authorized	Expended to December 31, 2006	Committed
LCR CSO Viscloskey	\$ 5,000,000	\$ 2,555,652	\$ 2,444,348
CSO Storage Basin	425,000	420,830	4,170
SCADA (SRF IV Phase)	<u>1,517,862</u>	<u>1,317,862</u>	<u>200,000</u>
 Totals	 <u>\$ 6,942,862</u>	 <u>\$ 4,294,344</u>	 <u>\$ 2,648,518</u>

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

D. Operating Leases

The District has entered into various operating leases having initial or remaining noncancelable terms exceeding one year for copiers. Rental expenditures for these leases were \$23,436. The following is a schedule by years of future minimum rental payments as of December 31, 2006:

2007	\$	22,319
2008		22,363
2009		15,415
2010		8,467
2011		<u>8,467</u>
 Total	 \$	 <u>77,031</u>

E. Short-Term Liabilities

The District may use short-term notes and loans, including tax anticipation warrants, to finance operations cash flow, due to the delay in receipt of property tax collections.

Short-term debt activity for the year ended December 31, 2006, was as follows:

	<u>Beginning Balance</u>	<u>Issued/ Draws</u>	<u>Redeemed Repayments</u>	<u>Ending Balance</u>
Notes payable	\$ -	\$ 3,811,506	\$ 3,811,506	\$ -

F. 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 primary government. General obligation bonds currently outstanding at year end are as follows:

<u>Purpose</u>	<u>Interest Rates</u>	<u>Amount</u>
2003 Special Taxing District refunding bonds	5.72% to 6.12%	<u>\$ 1,835,000</u>

Annual debt service requirements to maturity for general obligation bonds are as follows:

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

Year Ended December 31	Principal	Interest
2007	\$ 220,000	\$ 105,405
2008	230,000	91,800
2009	245,000	77,265
2010	260,000	61,812
2011	275,000	45,441
2012-2016	<u>605,000</u>	<u>37,485</u>
Totals	<u>\$ 1,835,000</u>	<u>\$ 419,208</u>

2. Notes and Loans Payable

The District has entered into various loans with the State Revolving Loan Fund (SRF). Under the terms of the loans, revenue bonds issued by the District have been purchased by the Indiana Bond Bank. The proceeds are set aside to finance District improvements. Funds are loans to the District as costs are accrued, to the maximum allowed. The District has drawn down all of the 1993, 1997, 1998, and 2001A Loan Program Funds; however, the 2001B and 2006A Loan Program Funds for \$10,500,000 and \$2,100,000, respectively, are still being drawn down. Annual debt service requirements to maturity for the loans are as follows:

Year Ended December 31	Principal	Interest
2007	\$ 2,460,000	1,146,300
2008	2,540,000	1,203,489
2009	2,630,000	1,025,789
2010	2,670,000	924,021
2011	2,720,000	820,576
2012-2016	10,425,000	2,721,249
2017-2021	5,025,048	1,104,278
2022-2026	<u>1,284,432</u>	<u>90,627</u>
Totals	<u>\$ 29,754,480</u>	<u>\$ 9,036,329</u>

3. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2006, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
General obligation bonds payable	\$ 2,040,000	\$ -	\$ 205,000	\$ 1,835,000	\$ 220,000
Loans payable:	<u>29,342,507</u>	<u>2,826,973</u>	<u>2,415,000</u>	<u>29,754,480</u>	<u>2,460,000</u>
Total long-term liabilities	<u>\$ 31,382,507</u>	<u>\$ 2,826,973</u>	<u>\$ 2,620,000</u>	<u>\$ 31,589,480</u>	<u>\$ 2,680,000</u>

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

G. Restricted Assets

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

Bond and interest cash and cash equivalents	\$ 2,456,471
Construction cash and cash equivalents	1,858,547
Taxes receivable (net of allowances)	474,866
Intergovernmental receivable	<u>1,026,197</u>
Total restricted assets	<u>\$ 5,816,081</u>

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; job related illnesses or injuries to employees; 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

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 liability 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 in the past three years. A premium is charged to each fund that accounts for employee 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.

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

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

	2005	2006
Unpaid claims, beginning of fiscal year	\$ 2,499,183	\$ 3,780,710
Incurred claims and changes in estimates	14,196,487	15,298,305
Claim payments	12,914,960	16,699,968
Unpaid claims, end of fiscal year	\$ 3,780,710	\$ 2,379,047

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 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.

There were no changes in the balance of claim liabilities during the past two years, since there were no claims incurred or paid.

B. Subsequent Events

Property tax rates and levies for the 2006 pay 2007 were not established by February 15, 2007, as required by statute, due to the delay in the completion of trending of the assessment of Lake County. This will result in delays in billing, collection and distribution of tax revenues by the County, for the District, in 2007.

To offset the delay in tax collections, the District authorized the issuance of tax anticipation notes. On January 2, 2007, the District sold tax anticipation warrants of \$1,600,000 to the Indiana Bond Bank. The warrants will be repaid when the 2007 property tax distributions are received.

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 eight percent (8%) per annum and is to be paid semiannually on the 15<sup>th</sup> day of January and July. In 2006, \$2,100,000 of the bonds were been sold to the State Revolving Loan Fund. The District closed on bonds totaling \$4,635,000 on April 25, 2007, which were sold on the open market. Additionally, the District anticipates selling an additional bond issue for \$17,225,000 to the State Revolving Loan Fund by August 2007.

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

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.

D. Transfers to City

The District transferred \$517,080 to the City as payment in lieu of taxes.

E. 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 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 Johnson 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.

For any noncompliance of the Consent Decree requirements noted above, the stipulated penalty would be applicable based on the period of noncompliance. From the first to the 30<sup>th</sup> day of continuous violation, \$500 per day per violation; from the 31<sup>st</sup> to the 60<sup>th</sup> 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 semi-annually 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 15 and December 15, 2006.

A permit renewal application was submitted to IDEM on January 29, 1999. A new NPDES Permit was issued in 2006. Due to concerns regarding certain pollutant parameters, the permit has been petitioned by the District for administrative review. Also, the District has been advised by the EPA and IDEM of their intent to seek civil penalties as provided in the existing Consent Decree. This is in regards for certain NPDES Permit pollutant parameter violations alleged to have occurred over the last five years, which the District denies the existence and/or the extent of these violations.

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, 19 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, 2006, expenditures of \$228,000 were recognized for postemployment benefits

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

G. Rate Structure

The current rate structure, for the treatment and disposal of sewage, as well as a storm water customer charge, was approved by the Common Council on January 23, 2006.

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:

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, which includes the District, 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.

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

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

Actuarial Assumptions

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%)

SANITARY DISTRICT  
CITY OF HAMMOND  
AUDIT RESULTS AND COMMENTS

INTERNAL CONTROLS

A portion of an industrial customer's billing is based upon lab reports of testing and results. The results are then summarized by the pretreatment department, and then the summary is used by the billing staff. Since information is manually inputted at multiple stages, this process increases the potential for errors to be made and not be detected during the performance of job duties.

Sixty percent of the selected industrial customers tested for a billing period had errors on the summary reports, when the reports were compared to the supporting lab documents, which caused incorrect amounts to be billed. Forty percent had other errors in the amounts billed, where the amounts used to calculate the billing did not agree to the amounts as presented on the summary reports. This resulted in customers being under or over billed, which also affects the revenue of the Sanitary District.

Governmental units should have internal controls in effect which provide reasonable assurance regarding the reliability of financial information and records, effectiveness and efficiency of operations, proper execution of management's objectives, and compliance with laws and regulations. Among other things, segregation of duties, safeguarding controls over cash and all other assets and all forms of information processing are necessary for proper internal control. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 7)

CONTRACTS

The board attorney does not have a contract with the District. District Board Resolution 13-2004 addresses the retainer paid to the board attorney; it does not address other compensation and benefits received by the board attorney.

Payments made or received for contractual services should be supported by a written contract. Each governmental unit is responsible for complying with the provisions of its contracts. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 7)

SANITARY DISTRICT  
CITY OF HAMMOND  
AUDIT RESULTS AND COMMENTS  
(Continued)

PENALTIES, INTEREST AND OTHER CHARGES

Penalties and interest totaling \$1,050.25 were paid to the Indiana Department of Revenue on January 26, 2007, for the period November 2006. This was due to late remittance of payroll withholdings. Due to the last payroll of November falling prior to the 20th of the month, the bank used by the District would not permit the payment of the withholding to be scheduled at the time of the payroll. Staff did not follow up on scheduling the remittance, resulting in the late payment and penalty and interest.

Officials and employees have the duty to pay claims and remit taxes in a timely fashion. Failure to pay claims or remit taxes in a timely manner could be an indicator of serious financial problems which should be investigated by the governmental unit.

Additionally officials and employees have a responsibility to perform duties in a manner which would not result in any unreasonable fees being assessed against the governmental unit.

Any penalties, interest or other charges paid by the governmental unit may be the personal obligation of the responsible official or employee.

(Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 7)

PENALTIES NOT ASSESSED

As noted in the prior audit, the District is not applying a ten percent (10%) penalty to customer accounts that have not paid within thirty 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 May 3, 2007, with Stanley Dostatni, President of the Board of Sanitary Commissioners; Linda Sheets, Deputy City Controller; William E. Biller, Business Manager; and Michael T. Unger, Ph.D., District Manager. The official response has been made a part of this report and may be found on pages 22 through 26.

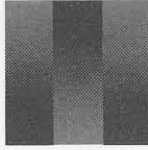
# SANITARY DISTRICT of HAMMOND

5143 COLUMBIA AVENUE  
HAMMOND, INDIANA 46327-1794  
TELEPHONE (219) 853-6412 - 13 - 14 - 88  
FAX (219) 853-6321

Board of Sanitary Commissioners

STANLEY J. DOSTATNI  
JOE L. ESCOBEDO  
STEVEN R. FOWLER  
LOUIS KARUBAS  
RUSSELL A. SNYDER

May 10, 2007



MICHAEL T. UNGER, Ph.D.  
District Manager  
WILLIAM E. BILLER, C.P.A.  
Business Manager  
JOSEPH P. ALLEGRETTI  
Legal Counsel

State Board of Accounts  
ATTN: Mr. Larry Tippin  
302 West Washington Street  
Room E 418  
Indianapolis, In 46204-2765

Re: Official Response – Hammond Sanitary District, Audit for 2006

Dear Mr. Tippin:

On Thursday May 3, 2007 representatives of the Hammond Sanitary District met with your auditors. The purpose of this meeting was to review the audit results and comments for the 2006 audit. Enclosed is the District's official response to the State Board of Accounts' Audit Results and Comments for the calendar year 2006. Please include this response with the State Board of Accounts' Audit Report.

Sincerely,

William E. Biller  
Business Manager

Enclosure

Pc: Board of Commissioners  
Joseph P. Allegretti  
Michael T. Unger, District Manager  
Cynthia David, Lake County Office SBA

HAMMOND SANITARY DISTRICT  
AUDIT RESULTS AND COMMENTS  
FOR PERIOD ENDING DECEMBER 31, 2006  
Page 1

1. INTERNAL CONTROLS:

A portion of an industrial customer's billing is based upon lab reports of testing and results. The results are then summarized by the pretreatment department, and then the summary is used by the billing staff. Since information is manually inputted at multiple stages, this process increases the potential for errors to be made and not be detected during the performance of job duties.

Sixty percent of the selected industrial customers tested for a billing period had errors on the summary reports, when the reports were compared to the supporting lab documents, which caused incorrect amounts to be billed. Forty percent had other errors in the amounts billed, where the amounts used to calculate the billing did not agree to the amounts as presented on the summary reports. This resulted in customers being under or over billed, which also affects the revenues of the Sanitary District.

Governmental units should have internal controls in effect which provide reasonable assurance regarding the reliability of financial information and records, effectiveness and efficiency of operations, proper execution of management's objectives, and compliance with laws and regulations. Among other things, segregation of duties, safeguarding controls over cash and all other assets and all forms of information processing are necessary for proper internal control. (Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 7).

**RESPONSE:**

The District will agree that the number of errors, as they relate to the billing process, has increased over the last nine to twelve months. One of the audit steps taken by the District at year end is a reconciliation of the billing data as it relates to data maintained by the pretreatment department. For calendar year 2006 this audit process resulted in six errors being found and revised billings being issued.

District will undertake a review of our billing system to see if we can simplify the process and eliminate the manual duplication of data entry. Also, the District will become more vigilant with our data input.

HAMMOND SANITARY DISTRICT  
AUDIT RESULTS AND COMMENTS  
FOR PERIOD ENDING DECEMBER 31, 2006  
Page 2

2. CONTRACTS

The board attorney does not have a contract with the District. District Board Resolution 13-2004 addresses the retainer paid to the board attorney; it does not address other compensation and benefits received by the board attorney.

Payments made or received for contractual services should be supported by a written contract. Each governmental unit is responsible for complying with the provisions of its contracts (Accounting and Uniform Compliance Guidelines Manual for Cites and Towns, Chapter 7).

RESPONSE:

The District and its attorney will under take steps to have a contract that is in compliance with the required guidelines by the next audit.

3. PENALTIES, INTEREST AND OTHER CHARGES:

Penalties and interest totaling \$1,050.25 were paid to the Indiana Department of Revenue on January 26, 2007 for the period November 2006. This was due to late remittance of payroll withholding. Due to the last payroll of November falling prior to the 20<sup>th</sup> of the month, the bank used by the District would not permit the payment of the withholding to be schedule at the time of the payroll. Staff did not follow up on scheduling the remittance, resulting in the late payment and penalty and interest.

Officials and employees have the duty to pay claims and remit taxes in a timely fashion. Failure to pay claims or remit taxes in a timely manner could be an indicator of serious financial problems which should be investigated by the governmental unit.

Additionally officials and employees have a responsibility to perform duties in a manner which would not result in any unreasonable fees being assessed against the governmental unit.

HAMMOND SANITARY DISTRICT  
AUDIT RESULTS AND COMMENTS  
FOR PERIOD ENDING DECEMBER 31, 2006

Page 3

Any penalties, interest or other charges paid by the governmental unit may be the personal obligation of the responsible official or employee.

(Accounting and Uniform Compliance Guidelines Manual for Cities and Towns, Chapter 7).

**RESPONSE:**

District agrees that it and its employees have the duty and responsibility to insure that all claims and taxes are paid in a timely manner. The District's staff accountant has been directed to schedule the remittance at the earliest date that the system will accept, rather than schedule said remittance for the 20<sup>th</sup> of following month. Business Manager also has started to note the remittance date for state withholding on his calendar, so that payment can be verified, prior to the reconciliation of bank accounts in the following month.

4. **PENALTIES NOT ASSESSED:**

As noted in the prior audit, the District is not applying a ten percent (10%) penalty to customer accounts that have not paid within thirty days of the due date in accordance with state statute.

IC 36-9-25-11 states in part ....”(f) If a fee established is not paid with 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...”

HAMMOND SANITARY DISTRICT  
AUDIT RESULTS AND COMMENTS  
FOR PERIOD ENDING DECEMBER 31, 2006

Page 4

RESPONSE:

The above statute does not authorize the District to apply a ten percent (10%) penalty to a customer's account not paid by the due date. The above statute only allows the District to collect a ten percent (10%) penalty (along with a reasonable attorney fee) if a civil action is brought against the delinquent user for unpaid user charges.

The action recommended by the State Board of Accounts may not be instituted by the District without appropriate legislative amendment.

The District does take civil action against real property that is delinquent for amounts greater than \$75 via the semi annual filing of liens with the county recorder and treasurer.