

CITY OF BISBEE, ARIZONA

**Financial Statements,
Supplementary Information
and
Single Audit Reports**

Year Ended June 30, 2003

CITY OF BISBEE, ARIZONA
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JUNE 30, 2003

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Independent Auditors' Report

To the City Council
City of Bisbee, Arizona

We have audited the accompanying general purpose financial statements of City of Bisbee, Arizona, as of and for the year ended June 30, 2003, as listed in the table of contents. These general purpose financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

The City does not maintain detailed records of its fixed assets accounted for in the General Fixed Assets Account Group or the Enterprise Funds. Accordingly, the combined balance sheet as of June 30, 2003 does not include the general fixed assets account group, which should be included in order to conform with U.S. generally accepted accounting principles, and we were unable to satisfy ourselves as to the stated amount reported as fixed assets in the Enterprise Funds on the combined balance sheet as of June 30, 2003. In addition, we were unable to satisfy ourselves as to the amount to record as depreciation expense in the Enterprise Funds.

In our opinion, except for the effects due to the omission of the general fixed assets account group and such adjustments, if any, as might have been determined to be necessary had we been able to satisfy ourselves as to the stated amount of the fixed assets and the amount to record as depreciation expense in the Enterprise Funds, the general purpose financial statements referred to above present fairly, in all material respects, the financial position of City of Bisbee, Arizona, as of June 30, 2003, and the results of its operations and the cash flows of its proprietary fund types for the year then ended in conformity with U.S. generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated December 5, 2003, on our consideration of City of Bisbee, Arizona'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.

To the City Council
City of Bisbee, Arizona

Our audit was performed for the purpose of forming an opinion on the general purpose financial statements taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-profit Organizations*, and is not a required part of the general purpose financial statements of City of Bisbee, Arizona. Such information has been subjected to the auditing procedures applied in the audit of the general purpose financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the general purpose financial statements taken as a whole.

Fester & Chapman A.C.

December 5, 2003

CITY OF BISBEE, ARIZONA
 COMBINED BALANCE SHEET - ALL FUND TYPES AND ACCOUNT GROUP
 JUNE 30, 2003

	Governmental Fund Types			Proprietary Fund Type	Account Group	Totals (Memorandum Only)
	General	Special Revenue	Capital Projects	Enterprise	General Long-Term Debt	
ASSETS AND OTHER DEBITS						
Assets:						
Cash in bank	\$ 154,146	\$ 226,966	\$ 50,031	\$ 403,303		\$ 834,446
Investments	805,069	1,830		371,056		1,177,955
Receivables (net of allowance for uncollectibles):						
Accounts	96,126			230,768		326,894
Due from other governments	208,348	86,846		579		295,773
Prepaid expenses	22,756					22,756
Construction in progress				3,528,991		3,528,991
Fixed assets (net of accumulated depreciation)				4,264,221		4,264,221
Other Debits:						
Amount to be provided for retirement of general long-term debt					\$ 716,380	716,380
Total assets and other debits	<u>\$ 1,286,445</u>	<u>\$ 315,642</u>	<u>\$ 50,031</u>	<u>\$ 8,798,918</u>	<u>\$ 716,380</u>	<u>\$ 11,167,416</u>
LIABILITIES, EQUITY AND OTHER CREDITS						
Liabilities:						
Accounts payable	\$ 138,401	\$ 70,283	\$ 2,754	\$ 825,603		\$ 1,037,041
Accrued payroll and related liabilities	125,465	5,801		18,054		149,320
Due to other governments	1,093	16,476				17,569
Note payable				2,609,464	\$ 21,025	2,630,489
Compensated absences payable				5,922	122,909	128,831
Claims and judgments payable		42,215				42,215
Capital leases payable					110,652	110,652
Lease purchase agreements payable					461,794	461,794
Total liabilities	<u>264,959</u>	<u>134,775</u>	<u>2,754</u>	<u>3,459,043</u>	<u>716,380</u>	<u>4,577,911</u>
Equity and other credits:						
Contributed capital				3,499,226		3,499,226
Retained earnings, unreserved				1,840,649		1,840,649
Fund balances -						
Unreserved, undesignated	<u>1,021,486</u>	<u>180,867</u>	<u>47,277</u>			<u>1,249,630</u>
Total equity and other credits	<u>1,021,486</u>	<u>180,867</u>	<u>47,277</u>	<u>5,339,875</u>		<u>6,589,505</u>
Total liabilities, equity and other credits	<u>\$ 1,286,445</u>	<u>\$ 315,642</u>	<u>\$ 50,031</u>	<u>\$ 8,798,918</u>	<u>\$ 716,380</u>	<u>\$ 11,167,416</u>

The accompanying notes are an integral part of these statements.

CITY OF BISBEE, ARIZONA
 COMBINED STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
 FUND BALANCES - ALL GOVERNMENTAL FUND TYPES
 YEAR ENDED JUNE 30, 2003

	<u>Governmental Fund Types</u>			Totals (Memorandum Only)
	<u>General</u>	<u>Special Revenue</u>	<u>Capital Projects</u>	
Revenues:				
Taxes	\$ 2,516,430			\$ 2,516,430
Intergovernmental	703,384	\$ 1,745,283		2,448,667
Fines and forfeitures	94,193			94,193
Licenses and permits	93,580			93,580
Charges for services	680,005			680,005
Rents and royalties	51,590			51,590
Contributions and donations		5,503	\$ 10,333	15,836
Interest income	17,902	920		18,822
Miscellaneous	<u>214,306</u>	<u>1,200</u>		<u>215,506</u>
Total revenues	<u>4,371,390</u>	<u>1,752,906</u>	<u>10,333</u>	<u>6,134,629</u>
Expenditures:				
Current:				
General government	1,445,954	952,902		2,398,856
Public safety	2,465,625	140,523		2,606,148
Highways and streets		469,847		469,847
Culture and recreation	347,340	102,202		449,542
Capital outlay			193,775	193,775
Debt service:				
Principal	14,093	17,222	77,882	109,197
Interest	<u>1,705</u>	<u>8,026</u>	<u>28,241</u>	<u>37,972</u>
Total expenditures	<u>4,274,717</u>	<u>1,690,722</u>	<u>299,898</u>	<u>6,265,337</u>
Excess of revenues over (under) expenditures	96,673	62,184	(289,565)	(130,708)
Other financing sources (uses)				
Operating transfers in	462,536	36,540	62,765	561,841
Operating transfers out	<u>(334,121)</u>	<u>(123,277)</u>		<u>(457,398)</u>
Total other financing sources (uses)	<u>128,415</u>	<u>(86,737)</u>	<u>62,765</u>	<u>104,443</u>
Excess of revenue and other sources over (under) expenditures and other uses	225,088	(24,553)	(226,800)	(26,265)
Fund balances, beginning of year, as restated (Note 11)	<u>796,398</u>	<u>205,420</u>	<u>274,077</u>	<u>1,275,895</u>
Fund balances, end of year	<u>\$ 1,021,486</u>	<u>\$ 180,867</u>	<u>\$ 47,277</u>	<u>\$ 1,249,630</u>

The accompanying notes are an integral part of these statements.

CITY OF BISBEE, ARIZONA
 COMBINED STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES
 IN FUND BALANCES - BUDGET AND ACTUAL
 GENERAL AND SPECIAL REVENUE FUNDS
 YEAR ENDED JUNE 30, 2003

	General Fund			Special Revenue Funds		
	Budget	Actual	Variance Favorable (Unfavorable)	Budget	Actual	Variance Favorable (Unfavorable)
Revenues:						
Taxes	\$ 2,381,297	\$ 2,516,430	\$ 135,133			
Intergovernmental	693,379	703,384	10,005	\$ 733,060	\$ 1,745,283	\$ 1,012,223
Fines and forfeitures	166,250	94,193	(72,057)			
Licenses and permits	107,500	93,580	(13,920)			
Charges for services	393,500	680,005	286,505			
Rents and royalties	48,000	51,590	3,590			
Contributions and donations				8,800	5,503	(3,297)
Interest income	10,050	17,902	7,852	2,000	920	(1,080)
Miscellaneous	383,152	214,306	(168,846)	50,000	1,200	(48,800)
Total revenues	<u>4,183,128</u>	<u>4,371,390</u>	<u>188,262</u>	<u>793,860</u>	<u>1,752,906</u>	<u>959,046</u>
Expenditures:						
Current:						
General government	1,591,809	1,445,954	145,855	134,360	952,902	(818,542)
Public safety	2,402,511	2,465,625	(63,114)	85,000	140,523	(55,523)
Highways and streets				503,963	469,847	34,116
Culture and recreation	359,591	347,340	12,251	8,800	102,202	(93,402)
Debt service:						
Lease payments	16,094	15,798	296		25,248	(25,248)
Total expenditures	<u>4,370,005</u>	<u>4,274,717</u>	<u>95,288</u>	<u>732,123</u>	<u>1,690,722</u>	<u>(958,599)</u>
Excess of revenues over (under) expenditures	(186,877)	96,673	283,550	61,737	62,184	447
Other financing sources (uses)						
Operating transfers in	462,536	462,536		54,390	36,540	(17,850)
Operating transfers out	(275,659)	(334,121)	(58,462)	(116,127)	(123,277)	(7,150)
Total other financing sources (uses)	<u>186,877</u>	<u>128,415</u>	<u>(58,462)</u>	<u>(61,737)</u>	<u>(86,737)</u>	<u>(25,000)</u>
Excess of revenues and other sources over expenditures and other uses		225,088	225,088		(24,553)	(24,553)
Fund balances, beginning of year	796,398	796,398		205,420	205,420	
Fund balances, end of year	<u>\$ 796,398</u>	<u>\$ 1,021,486</u>	<u>\$ 225,088</u>	<u>\$ 205,420</u>	<u>\$ 180,867</u>	<u>\$ (24,553)</u>

The accompanying notes are an integral part of these statements.

CITY OF BISBEE, ARIZONA
 COMBINED STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
 IN FUND BALANCE - BUDGET AND ACTUAL
 CAPITAL PROJECTS FUND
 YEAR ENDED JUNE 30, 2003

	Capital Projects Fund		
	Budget	Actual	Variance Favorable (Unfavorable)
Revenues:			
Contributions and donations		\$ 10,333	\$ 10,333
Miscellaneous	\$ 590,027		(590,027)
Total revenues	590,027	10,333	(579,694)
Expenditures:			
Capital outlay	590,027	193,775	396,252
Lease payments		106,123	(106,123)
Total expenditures	590,027	299,898	290,129
Excess of expenditures over revenues		(289,565)	(289,565)
Other financing sources			
Operating transfers in		62,765	62,765
Total other financing sources		62,765	62,765
Excess of expenditures over revenues and other sources		(226,800)	(226,800)
Fund balance, beginning of year, as restated (Note 11)	274,077	274,077	
Fund balance, end of year	\$ 274,077	\$ 47,277	\$ (226,800)

The accompanying notes are an integral part of these statements.

CITY OF BISBEE, ARIZONA
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN RETAINED EARNINGS
PROPRIETARY FUND TYPE - ENTERPRISE FUNDS
YEAR ENDED JUNE 30, 2003

Operating revenues	
Charges for sales and services	\$ 2,091,860
Rents	900
Miscellaneous	<u>6,900</u>
Total operating revenues	2,099,660
Operating expenses	
Costs of sales and services	<u>1,471,467</u>
Total operating expenses	<u>1,471,467</u>
Operating income	628,193
Non-operating expenses	
Interest expense	<u>(9,941)</u>
Total non-operating expenses	(9,941)
Operating transfers	
Operating transfers in	290,270
Operating transfers out	<u>(394,714)</u>
Total operating transfers	<u>(104,444)</u>
Net income	513,808
Retained earnings, beginning of year, as restated (Note 11)	<u>1,326,841</u>
Retained earnings, end of year	<u>\$ 1,840,649</u>

The accompanying notes are an integral part of these statements.

CITY OF BISBEE, ARIZONA
STATEMENT OF CASH FLOWS
PROPRIETARY FUND TYPE - ENTERPRISE FUNDS
YEAR ENDED JUNE 30, 2003

Cash flows from operating activities:	
Cash received from customers	\$ 2,086,927
Cash payments to suppliers for goods and services	(752,922)
Cash payments to employees for services	<u>(673,125)</u>
Net cash provided by operating activities	660,880
Cash flows from capital and related financing activities:	
Proceeds from loans - WIFA	2,609,464
Payments for capital acquisitions	(3,067,435)
Interest paid on loans - WIFA	<u>(16,528)</u>
Net cash used by capital and related financing activities	(474,499)
Cash flows from non-capital financing activities:	
Operating transfers in	290,270
Operating transfers out	<u>(394,714)</u>
Net cash used by noncapital financing activities	(104,444)
Cash flows from investing activities:	
Proceeds of interest	<u>6,586</u>
Net cash provided by investing activities	<u>6,586</u>
Net increase in cash and cash equivalents	88,523
Cash and cash equivalents, beginning of year, as restated (Note 11)	<u>685,836</u>
Cash and cash equivalents, end of year	<u>\$ 774,359</u>
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	\$ 628,193
Adjustments to reconcile operating income to net cash provided by operating activities:	
Increase in accounts receivable	(12,733)
Increase in accounts payable	52,880
Increase in accrued payroll	1,230
Decrease in compensated absences payable	<u>(8,690)</u>
Net cash provided by operating activities	<u>\$ 660,880</u>

The accompanying notes are an integral part of these statements.

CITY OF BISBEE, ARIZONA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the City of Bisbee, Arizona (the City) conform to U.S. generally accepted accounting principles applicable to governmental units as promulgated by the Governmental Accounting Standards Board (GASB), except for the omission of the general fixed assets account group on the combined balance sheet and recording of depreciation expense on the enterprise funds statement of revenues, expenses and changes in retained earnings. A summary of the City's more significant accounting policies follows.

The City was incorporated under the laws of the State of Arizona. The City operates under a council-manager form of government and provides the following services as authorized by general law: public safety, highways and streets, parks and recreation, planning and zoning, and general administrative services. As required by generally accepted accounting principles, these financial statements present the City of Bisbee, Arizona (the primary government) and its component units.

A. Reporting Entity

The City is a general purpose local government that is governed by a separately elected city council. These general purpose financial statements present all the fund types and the general long term debt account group of the City (a primary government) and its component units.

Component units are legally separate entities for which the City is considered to be financially accountable. Blended component units, although legally separate entities, are in substance part of the City's operations, and so data from these units are combined with data of the primary government. Discretely presented component units, on the other hand, are reported in a separate column in the combined financial statement to emphasize they are legally separate from the City. Each blended component unit discussed below has a June 30 year-end. The City has no discretely presented component units.

The City of Bisbee Municipal Property Corporation (BMPC) is governed by a three-member board appointed by the City Council. Although it is legally separate from the City, the BMPC is reported as if it were part of the primary government because its sole purpose is to finance and construct two of the City's public buildings. The BMPC's debt is reported as part of the general long-term debt account group. Separate financial statements for the BMPC are not prepared.

B. Fund Accounting

The City's accounts are maintained in accordance with the principles of fund accounting to ensure that limitations and restrictions on the City's available resources are observed. The principles of fund accounting require that resources be classified for accounting and reporting purposes into funds or account groups in accordance with the activities or objectives specified for those resources. Each fund is considered a separate accounting entity, and its operations are accounted for in a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues, and expenditures (or expenses).

CITY OF BISBEE, ARIZONA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

B. Fund Accounting - Continued

Account groups are reporting devices to account for certain assets and liabilities of the governmental funds not recorded directly in those funds.

Accounts are separately maintained for each fund and account group; however, in the accompanying financial statements, funds that have similar characteristics have been combined into generic fund types that are further classified into broad fund categories. A description of the City's fund categories, types, and account groups follows.

1. Governmental Funds account for the City's general government activities using the flow of current financial resources measurement focus and include the following fund types.

The *General Fund* is the City's primary operating fund. It accounts for all financial resources of the City, except those required to be accounted for in other funds.

The *Special Revenue Funds* account for specific revenue sources that are legally restricted to expenditures for specified purposes.

The *Capital Projects Fund* accounts for the acquisition or construction of major capital facilities.

2. Proprietary Funds account for the City's ongoing activities that are similar to those found in the private sector using the flow of economic resources measurement focus. The City applies all applicable FASB Statements and Interpretations, APB Opinions, and ARBs to its proprietary activities unless those pronouncements conflict with or contradict GASB pronouncements. The City's proprietary funds include the following fund type.

The *Enterprise Fund* accounts for operations that are financed and operated in a manner similar to private business enterprises, in which the intent of the City Council 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 for which the City Council 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.

3. Account Groups are used to establish control and accountability for certain City liabilities that are not recorded in the funds and include the following group.

The *General Long-Term Debt Account Group* accounts for all long-term obligations of the City, except those accounted for in the Proprietary Funds.

CITY OF BISBEE, ARIZONA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

C. Basis of Accounting

Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied, and determines when revenues and expenditures (or expenses) are recognized in the accounts and reports in the financial statements. The financial statements of the Governmental Funds are presented on the modified accrual basis of accounting. Revenues are recognized when they become measurable and available to finance expenditures of the current period. Expenditures are recognized when the related fund liability is incurred, except for principal and interest on general long-term debt that are recognized when due.

Those revenues susceptible to accrual prior to receipt are franchise taxes; special assessments; licenses and permits; intergovernmental aid, grants, and reimbursements; interest revenue; charges for services; and sales taxes collected and held by the State at year-end on the City's behalf. Fines and forfeits and miscellaneous revenues are not susceptible to accrual because generally they are not measurable until received in cash.

The City reports deferred revenue and expense on its combined balance sheet. Deferred revenues and expenses arise when a potential revenue and expense does not meet both the "measurable" and "available" criteria for recognition in the current period. Deferred revenues and expenses also arise when resources are received or expended by the City before it has a legal claim to them. In subsequent periods, when both revenue and expense recognition criteria are met, or when the City has a legal claim to the resources or expenses, the liability for deferred revenue and the asset for deferred charges are removed from the combined balance sheet and revenue and/or expense is recognized.

The financial statements of the proprietary fund are presented on the accrual basis of accounting. Revenues are recognized when they are earned, and expenses are recognized when they are incurred.

D. Budgeting and Budgetary Control

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

1. On or before the third Monday in July, the City Manager submits to the City Council a proposed operating budget for the fiscal year commencing July 1. The operating budget includes proposed expenditures and the means of financing them.
2. Public hearings are conducted at City Hall to obtain taxpayer comments.
3. Prior to September 1, the budget is legally enacted through passage of an ordinance.

CITY OF BISBEE, ARIZONA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

D. Budgeting and Budgetary Control - Continued

4. Any revisions that alter the total expenditures of any Fund or department must be approved by the City Council.
5. The budget is used as a management control device during the year for the general fund, special revenue funds and capital project fund.
6. Budgets for the general fund, special revenue funds, and capital project fund are adopted on a basis consistent with generally accepted accounting principles (GAAP).

The level of budgetary control is at the department level for all governmental fund types, as reported in the Official Budget Forms prepared pursuant to guidelines established by the State of Arizona, Office of the Auditor General, and included as an attachment to the resolution adopting the annual City budget. The City Council may transfer appropriations between funds and departments.

Encumbrances - Encumbrance accounting is used for budgetary and control purposes; however, encumbrances outstanding at year-end do not constitute expenditures or liabilities, and are reversed before financial statements are prepared.

E. Pronouncements of GASB and FASB

Government Accounting Standards Board (GASB) Statement No. 20 states that the Financial Accounting Standards Board (FASB) and its predecessor body pronouncements issued before November 30, 1989, continue to be applicable to enterprise funds unless they conflict with or contradict GASB guidance.

Enterprise funds may take either of the following approaches to FASB guidance issued subsequent to November 30, 1989.

1. An entity may elect to continue to follow FASB guidance that does not conflict with or contradict GASB guidance. If this election is made, it must be followed consistently. It would not be appropriate to follow some FASB pronouncements, issued subsequent to the cutoff date, but not others.
2. An entity may elect not to subject itself to FASB guidance issued subsequent to the cutoff date. In that case, even FASB amendments of guidance issued prior to the cutoff date would not be applicable to proprietary operations.

The City of Bisbee has elected to subject itself to FASB guidance issued subsequent to November 30, 1989.

CITY OF BISBEE, ARIZONA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

F. Total Columns on Combined Statements

Total columns on the combined statements are captioned "Memorandum Only" to indicate that they are presented only to facilitate financial analysis. Amounts in these columns do not present the financial position, results of operations, or changes in financial position of the City in conformity with generally accepted accounting principles. Such amounts are not comparable to a consolidation and interfund eliminations have not been made in the aggregation of these amounts.

G. Deposits and Investments

Arizona Revised Statutes authorize the City to invest public monies in the State Treasurer's investment pool; interest bearing savings accounts, certificates of deposit, and repurchase agreements in eligible depositories; bonds or other obligations of the United States government that are guaranteed as to principal and interest by the United States government; and bonds of the State of Arizona counties, cities, towns, school districts, and special districts as specified by statute. As required by statute, collateral is required for demand deposits, certificates of deposit, and repurchase agreements at 101 percent of all deposits not covered by Federal depository insurance.

The State Board of Deposit provides oversight for the State Treasurer's pools, and the Local Government Investment Pool Advisory Committee provides consultation and advice to the Treasurer. The fair value of a participant's position in the pool approximates the value of that participant's pool shares.

Nonparticipating interest-earning investment contracts are stated at cost. Money market investments and participating interest-earning investment contracts with a remaining maturity of one year or less at time of purchase are stated at amortized cost.

For purposes of its statement of cash flows, the City considers only those highly liquid investments with a maturity of three months or less when purchased, to be cash equivalents.

H. Allowance for Doubtful Accounts

The allowance for doubtful accounts in the proprietary fund is estimated at over 50% of the year-end accounts receivable balance and has a balance of \$248,824 at June 30, 2003.

I. Use of Estimates

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenditures (or expenses) during the reporting period. Actual results could differ from those estimates.

CITY OF BISBEE, ARIZONA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

J. Compensated Absences

Compensated absences consist of paid time off which can be used as vacation or sick leave. Fire Department employees may accumulate up to 312 hours of paid time off depending on year of service, and all other city employees may accumulate up to 208 hours of vacation depending on years of service, but any paid time off in excess of the maximum amount that is unused at year-end is forfeited. An employee may be allowed to carry forward paid time off to the first six months of the following year if staffing shortages prevented the employee from utilizing their paid time off. An employee taking leave for a serious illness of a family member under the Family Medical Leave Act may use the paid time off as part of the unpaid twelve week period allowed by law.

The amounts of compensated absences expected to be paid by available financial resources in the general fund, special revenue fund, and the capital projects fund are immaterial, and therefore no amounts are recorded as an expenditure and a current liability at June 30, 2003 in those funds. Amounts of compensated absences that are not expected to be liquidated with expendable available financial resources of the governmental funds are recorded in the general long-term debt account group. Vested compensated absences of the proprietary fund are recorded as expenses and liabilities of that fund as the benefits accrue to employees.

K. Intergovernmental Grants and Aid

Grants and assistance awards made on the basis of entitlement periods are recorded as intergovernmental receivables and revenues when entitlement occurs. Reimbursement grants are recorded as intergovernmental receivables and revenues when the related expenditures are incurred.

L. Property Tax Revenues

Property tax revenues are recognized as revenue in the year collected or if collected within 60 days thereafter.

CITY OF BISBEE, ARIZONA
 NOTES TO FINANCIAL STATEMENTS
 JUNE 30, 2003

NOTE 2 - DEPOSITS AND INVESTMENTS

Deposits: At June 30, 2003, the City had cash on hand of \$1,197. The carrying amount of the City's total cash in bank was \$833,249, and the bank balance was \$920,610. Of the bank balance, \$145,021 was covered by federal depository insurance and \$775,589 was covered by collateral held by the pledging financial institution's trust department in the City's name.

The City's deposits at June 30, 2003 were entirely covered by Federal depository insurance or by collateral held by the City's custodial bank in the City's name.

Investments are categorized into these three categories of credit risk:

- (1) Insured or registered in the City's name, or securities held by the City or its agent in the City's name.
- (2) Uninsured and unregistered, with securities held by the counter-party's trust department or agent in the City's name.
- (3) Uninsured and unregistered, with securities held by the counter-party, or by its trust department or agent, but not in the City's name.

At June 30, 2003, the City's investments were as follows:

	Carrying Amount	Fair Value
Investments not subject to categorization:		
State Treasurer's investment pool	\$ 1,177,955	\$ 1,177,955

NOTE 3 - DUE FROM OTHER GOVERNMENTS

Amounts due from other governments at June 30, 2003 include the following:

	General Fund	Special Revenue Funds	Enterprise Funds	Total
Arizona State Treasurer				
State sales tax	\$ 40,836			\$ 40,836
City sales tax	102,161			102,161
Local government investment pool	1,179	\$ 81	\$ 579	1,839
Arizona Department of Transportation	20,764	46,676		67,440
Arizona State Land Department				
Fire suppression	20,762			20,762
Arizona State Highway Department				
Urban Revenue Fund		40,089		40,089
Cochise County Treasurer	22,646			22,646
Total	\$ 208,348	\$ 86,846	\$ 579	\$ 295,773

CITY OF BISBEE, ARIZONA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003

NOTE 4 - GENERAL FIXED ASSETS

The management of the City of Bisbee has determined that sufficient records do not currently exist to support an amount that should be reported in the general fixed asset account group. Accordingly, no balance has been reported in the combined balance sheet for the general fixed asset account group.

NOTE 5 - ENTERPRISE FUND FIXED ASSETS

The City maintains three enterprise funds which account for the operation of the City's sewers, landfill/sanitation, and the Queen Mine, a historic tourist attraction. Property, plant and equipment for the enterprise funds are normally stated at historical cost and depreciated over the assets' estimated useful lives. However, the balance reported on the combined balance sheet for fixed assets for the enterprise funds was not audited for the same reason indicated in Note 4. This amount represents an estimate by management and no assurance is provided on this balance by the auditor's report. As a result, no depreciation expense was recorded in the enterprise fund for the year ended June 30, 2003.

NOTE 6 - LONG-TERM DEBT

The following is a summary of changes in long-term debt of the City for the year ended June 30, 2003:

	Governmental Funds				Enterprise Funds
	Note Payable	Capital Leases Payable	Lease Purchase Agreements Payable	Total	WIFA Loan
Debt payable at July 1, 2002	\$ 24,562	\$ 171,547	\$ 506,951	\$ 703,060	
Additional principal					\$ 2,609,464
Principal retired	3,537	60,895	45,157	109,589	
Debt payable at June 30, 2003	\$ 21,025	\$ 110,652	\$ 461,794	\$ 593,471	\$ 2,609,464

CITY OF BISBEE, ARIZONA
 NOTES TO FINANCIAL STATEMENTS
 JUNE 30, 2003

NOTE 6 - LONG-TERM DEBT - CONTINUED

Long-term debt payable at June 30, 2003 is comprised of the following:

Notes Payable

Loan agreement with the State of Arizona Department of Transportation, Aeronautics Division, to fund improvements to the City's airport; payable in yearly installments of \$5,131 including interest at 6.49%; matures March 2008. \$ 21,025

Loan agreement with the Water Infrastructure Financing Authority to fund rehabilitation of the City's wastewater infrastructure; payable in annual installments of interest only at 1.66%. Beginning in 2005, annual installments will be \$302,564 including interest at 3.472%; matures July 2022. 2,609,464
\$ 2,630,489

Capital Leases Payable

Capital lease agreement for Ford ambulance; payable in monthly installments of \$1,233 including interest at 6.03% ; matures July 2004. \$ 16,640

Capital lease agreement for Caterpillar road grader; payable in monthly installments of \$3,598 including interest at 9.14%; matures October 2005 94,012
\$ 110,652

Lease Purchase Agreements Payable

City of Bisbee Municipal Property Corporation lease purchase agreement for remodeling of the City's police station; payable in semi-annual installments of \$12,624 including interest at 5.71%; lease payments have been assigned to investors; matures January 2009. \$ 126,601

City of Bisbee Municipal Property Corporation lease purchase agreement for construction of a Fire Station; payable in semi-annual installments of \$23,987 including interest at 5.65%; lease payments have been assigned to investors; matures June 2112. 335,193
\$ 461,794

CITY OF BISBEE, ARIZONA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003

NOTE 6 - LONG-TERM DEBT - CONTINUED

Annual cash requirements to amortize all the outstanding debt at June 30, 2003, including interest payments are as follows:

Year Ending June 30,	Note Payable	Governmental Funds			Total	Enterprise Funds
		Capital Leases Payable	Lease Purchase Agreements Payable			Loan
2004	\$ 5,131	\$ 57,969	\$ 73,220	\$ 136,320	\$ 60,087	
2005	5,131	45,643	73,221	123,995	230,044	
2006	5,131	14,392	73,222	92,745	302,564	
2007	5,131		74,222	79,353	302,564	
2008	4,715		73,222	77,937	302,564	
Thereafter			217,141	217,141	1,714,205	
	25,239	118,004	584,248	727,491	2,912,028	
Interest	4,214	7,352	122,454	134,020	302,564	
Principal	<u>\$ 21,025</u>	<u>\$ 110,652</u>	<u>\$ 461,794</u>	<u>\$ 593,471</u>	<u>\$ 2,609,464</u>	

In July 2002, the City of Bisbee entered into a loan agreement with the Water Infrastructure Financing Authority (WIFA) to help fund improvements to the City's wastewater infrastructure system. The City will borrow a total of \$4,000,000 as needed to fund the ongoing costs of the construction project. The loan repayment schedule will extend 20 years, until July 2022. Under the terms of the loan, the City is required to make interest payments only in the amount of \$60,087 in 2004. The first principal payment of \$163,684 with interest of \$66,360 is due in 2005 for a total of \$230,044. The interest rate in effect for 2004 and 2005 will be 1.659%. Subsequent annual payments will be \$302,564 and the interest rate will be 3.472%. The amount drawn down on the loan at June 30, 2003 was \$2,609,464 and that amount has been recorded as a liability of the Enterprise Funds.

NOTE 7 - RISK MANAGEMENT

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City is a member of the Arizona Municipal Risk Retention Pool (AMRRP), a public entity risk pool currently operating as a common risk management and insurance program for Arizona municipalities. The City pays an annual premium to AMRRP for its general insurance coverage. The Agreement for Formation of the AMRRP provides that AMRRP will be self-sustaining through member premiums and will reinsure through commercial companies for excess claims for each insured event.

CITY OF BISBEE, ARIZONA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003

NOTE 7 - RISK MANAGEMENT - CONTINUED

The City is also a member of the Arizona Municipal Workers Compensation Pool (AMWCP), a public entity risk pool. The pool provides member cities with workers' compensation coverage, as required by law, and risk management services. The City is responsible for paying premiums based on an experience rating formula that allocates pool expenditures and liabilities among the members.

NOTE 8 - COMPENSATED ABSENCES

A summary of the change in the liability for compensated absences recorded in the general long-term debt account group for the year ended June 30, 2003 follows:

Balance at July 1, 2002	\$ 126,274
Net decrease in liability	<u>(3,365)</u>
Balance at June 30, 2003	<u>\$ 122,909</u>

NOTE 9 - COMMITMENTS AND CONTINGENCIES

Litigation - Each year the City receives notices of claims for damages occurring generally from negligence, bodily injury, breach of contract, and other legal matters. The filing of such claims commences a statutory period for initiating a lawsuit against the City arising therefrom. The City has comprehensive general liability insurance with the Arizona Municipal Risk Retention Pool and separate liability insurance concerning its Queen Mine Tour. In the opinion of the City Attorney, all known claims against the City are fully insurable. The City's attorney has indicated that there is one legal action that will likely result in damages being paid to the litigant of \$42,215. Accordingly, a liability has been recorded in the amount of \$42,215.

Lease Purchase Agreements - The City leases a fire station from the BMPC (see Note 1) under a lease purchase agreement that transfers ownership to the City at the conclusion of the lease on June 1, 2012. Also, the City leases the City's police station from the BMPC under a lease purchase agreement that transfers ownership of the police station to the City at the conclusion of the lease on January 1, 2009. Both of these leases stipulate that the City has the option to purchase the properties held by the BMPC before the terms of the leases are concluded, by paying the Prepayment Price (the total of all unpaid principal amounts).

The BMPC obtained the funds for the construction of the fire station and remodel of the police station from investors. In return, the BMPC has assigned the lease payments from the City for the fire station and police station directly to the investors. As a result, lease payments from the City are paid to the investors through the underwriter who acts as a fiduciary agent.

CITY OF BISBEE, ARIZONA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003

NOTE 9 - COMMITMENTS AND CONTINGENCIES - CONTINUED

Also, to secure the lease payments to the investors, the City has pledged excise, transaction, privilege, franchise and income taxes which the City now collects and may collect in the future or which are allocated or apportioned to the City by the State. This includes any amounts received from any political subdivision or governmental unit or agency of the State, except those amounts which by law must be expended for other purposes.

NOTE 10 - RETIREMENT PLANS

Plan Descriptions - The City contributes to the two plans described below. Benefits are established by state statute and generally provide retirement, death, long-term disability, survivor, and health insurance premium benefits.

The Arizona State Retirement System (ASRS) administers a cost-sharing multiple-employer defined benefit pension plan that covers general employees of the City. The ASRS is governed by the Arizona State Retirement System Board according to the provisions of A.R.S. Title 38, Chapter 5, Article 2.

The Public Safety Personnel Retirement System (PSPRS) is an agent multiple-employer defined benefit pension plan that covers public safety personnel who are regularly assigned hazardous duty as employees of the State of Arizona or one of its political subdivisions. The PSPRS, acting as a common investment and administrative agent, is governed by a five-member board, known as the Fund Manager, and 189 local boards according to the provisions of A.R.S. Title 38, Chapter 5, Article 4.

Each plan issues a publicly available financial report that includes its financial statements and required supplementary information. A report may be obtained by writing or calling the applicable plan.

ASRS
3300 N. Central Ave.
P.O. Box 33910
Phoenix, AZ 85067-3910

PSPRS
1020 E. Missouri Ave.
Phoenix, AZ 85014

(602) 240-2200 or (800) 621-3778 (602) 255-5575

Funding Policy - The Arizona State Legislature established and may amend active plan members' and the City's contribution rates.

Cost-sharing plans - For the year ended June 30, 2003, active ASRS members and the City were each required by statute to contribute at the actuarially determined rate of 2.49 percent (2.0 percent retirement and 0.49 percent long-term disability) of the members' annual covered payroll. The City's contributions to ASRS for the years ended June 30, 2003, 2002, and 2001 were \$48,997, \$44,475, and \$46,545, respectively, which were equal to the required contributions for the year.

CITY OF BISBEE, ARIZONA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003

NOTE 10 - RETIREMENT PLANS - CONTINUED

Agent plans - For the year ended June 30, 2003, active PSPRS members were required by statute to contribute 7.65 percent of the members' annual covered payroll. The City is required to contribute the remaining amounts necessary to fund the PSPRS, as determined by the actuarial basis specified by the statute. The current rate is 23.27% of annual covered payroll for police and 22.00% of annual covered payroll for firefighters.

Annual Pension Cost - The City's pension cost for the agent plans for the year ended June 30, 2003, the date of the most recent actuarial valuation, and related information follows.

	<u>Bisbee Police PSPRS</u>	<u>Bisbee Fire Fighters PSPRS</u>
Contribution rates:		
City	23.27%	22.00%
Plan members	7.65%	7.65%
Annual pension cost	\$62,662	\$63,281
Contributions made	\$62,662	\$63,281
Actuarial valuation date	6/30/03	6/30/03
Actuarial cost method	individual entry age	individual entry age
Actuarial assumptions:		
Investment rate of return	9%	9%
Projected salary increases		
includes inflation at 5.5%	6.5%-9.5%	6.5%-9.5%
Cost-of-living adjustments	none	none
Amortization method	level percent open	level percent open
Remaining amortization		
period from 7/1/02	20 years	20 years
Asset valuation method	smoothed market value	smoothed market value

Trend Information - Annual pension cost information for the current and two preceding years follows for each of the agent plans.

Bisbee Police			
Year Ended June 30,	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
2003	\$ 62,662	100.0 %	\$ 0
2002	81,690	100.0 %	0
2001	97,121	100.0 %	0

CITY OF BISBEE, ARIZONA
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003

NOTE 10 - RETIREMENT PLANS - CONTINUED

Bisbee Fire Fighters					
Year Ended June 30,	Annual Pension Cost (APC)	Percentage of APC Contributed		Net Pension Obligation	
2003	\$ 63,281	100.0	%	\$ 0	
2002	83,924	100.0	%	0	
2001	87,910	100.0	%	0	

Analysis of Funding Progress - The following was obtained from the three most recent actuarial valuations of the agent plans.

Bisbee Police						
Actuarial Valuation Date June 30,	Actuarial Value of Plan Assets (a)	Actuarial Accrued Liability (b)	Funding (Liability) Excess (a-b)	Funded Ratio (a/b)	Annual Covered Payroll (c)	Unfunded Liability as Percentage of Covered Payroll ((a-b)/c)
2003	\$2,534,766	\$3,834,521	\$(1,299,755)	66.1 %	\$ 527,477	246.4 %
2002	2,679,937	3,474,121	(794,184)	77.1 %	553,414	143.5 %
2001	2,743,544	2,901,605	(158,061)	94.6 %	641,859	24.6 %

Bisbee Fire Fighters						
Actuarial Valuation Date June 30,	Actuarial Value of Plan Assets (a)	Actuarial Accrued Liability (b)	Funding (Liability) Excess (a-b)	Funded Ratio (a/b)	Annual Covered Payroll (c)	Unfunded Liability as Percentage of Covered Payroll ((a-b)/c)
2003	\$3,860,157	\$5,354,722	\$(1,494,565)	72.1 %	\$ 694,715	215.1 %
2002	3,992,589	4,665,678	(673,089)	85.6 %	770,972	87.3 %
2001	4,164,816	4,204,615	(39,799)	99.1 %	754,800	5.3 %

CITY OF BISBEE, ARIZONA
 NOTES TO FINANCIAL STATEMENTS
 JUNE 30, 2003

NOTE 11 - RESTATEMENT

Retained earnings at July 1, 2002, as previously reported, was adjusted to capitalize prior year fixed assets in the wastewater improvement project in the Enterprise funds and to account for a change in the classification of the wastewater improvement project from the Capital Projects fund to the Enterprise funds.

Retained earnings at July 1, 2002, as previously reported	\$ 903,463
Adjustment to capitalize prior year fixed assets in the wastewater improvement project in the Enterprise funds	245,504
Adjustment to classify the wastewater improvement project to the Enterprise Funds	<u>177,874</u>
Beginning retained earnings, as restated	<u>\$ 1,326,841</u>

Fund balance at July 1, 2002, as previously reported, was adjusted to account for a change in the classification of the wastewater improvement project from the Capital Projects fund to the Enterprise funds.

Fund balance at July 1, 2002, as previously reported	\$ 451,951
Adjustment to classify the wastewater improvement project to the Enterprise Funds	<u>(177,874)</u>
Beginning fund balance, as restated	<u>\$ 274,077</u>

Cash and cash equivalents balance at July 1, 2002, as previously reported, was adjusted to account for a change in the classification of the wastewater improvement project from the Capital Projects fund to the Enterprise funds.

Cash and cash equivalents balance at July 1, 2002, as previously reported	\$ 507,962
Adjustment to classify the wastewater improvement project to the Enterprise funds	<u>177,874</u>
Beginning cash and cash equivalents, as restated	<u>\$ 685,836</u>

SUPPLEMENTARY INFORMATION

CITY OF BISBEE, ARIZONA
 SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
 YEAR ENDED JUNE 30, 2003

<u>Federal Grantor/ Pass-Through Grantor Program Title</u>	<u>CFDA Number</u>	<u>Pass-Through Grantor's Number</u>	<u>Expenditures</u>
U.S. Department of Housing and Urban Development			
Passed through:			
Arizona Department of Commerce Community Development Block Grant/ State's Program	14.228	099-00	\$ 69,454
U.S. Department of Interior			
Passed through:			
Arizona Historic Preservation Office Historic Preservation Fund Grants in Aid	15.904	640215	16,621
Passed through:			
Arizona State Land Department Wildland Urban Interface Community and Rural Fire Assistance	15.228	F-RFA-2030	9,900
Passed through:			
Arizona Department of Transportation Outdoor Recreation, Acquisition, Development and Planning	15.916	CH-BIS-SL447-02D	<u>6,800</u>
Total U.S. Department of Interior			<u>33,321</u>
Office of National Drug Control Policy			
Passed through:			
Cochise County Sheriff's Office High Intensity Drug Trafficking Areas	15.unknown	HIDTA 2003 BISBEE	55,218
U.S. Department of Transportation			
Federal Transit Formula Grant	20.507	KR01-1183TRN	141,522
Passed through:			
Governor's Office of Highway Safety State and Community Highway Safety	20.600	GHA 2003 PS 001	<u>3,275</u>
Total U.S. Department of Transportation			<u>144,797</u>
National Foundation on the Arts and the Humanities			
Promotion of the Humanities Public Programs	45.164	GL 21739 02	500
State Library Program	45.310	221-2-1-02	<u>3,542</u>
Total National Foundation on the Arts and the Humanities			<u>4,042</u>

CITY OF BISBEE, ARIZONA
 SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
 YEAR ENDED JUNE 30, 2003

Federal Grantor/ Pass-Through Grantor Program Title	CFDA Number	Pass-Through Grantor's Number	<u>Expenditures</u>
Federal Emergency Management Association			
Passed through:			
State of Arizona Division of Emergency Management Hazard Mitigation Program	83.548	FEMA-1314-DR-AZ	778,158
Passed through:			
Arizona Grants Management Branch Assistance to Firefighters Grant	83.554	HMGP-977-35, 36, 37	<u>45,960</u>
Total Federal Emergency Management Association			<u>824,118</u>
Total expenditures of federal awards			<u>\$ 1,130,950</u>

CITY OF BISBEE, ARIZONA
NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
YEAR ENDED JUNE 30, 2003

NOTE 1 - BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the City of Bisbee, Arizona and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

NOTE 2 - CATALOG OF FEDERAL DOMESTIC ASSISTANCE (CFDA) NUMBERS

The program titles and CFDA numbers were obtained from the federal or pass-through grantor or the 2003 Catalog of Federal Domestic Assistance Update.

NOTE 3 - SUBRECIPIENTS

The City did not award any federal funds to subrecipients.

SINGLE AUDIT REPORTS

Independent Auditors' Report on Compliance and on Internal Control over
Financial Reporting Based on an Audit of Financial Statements
Performed in Accordance with *Government Auditing Standards*

To the City Council
City of Bisbee, Arizona

We have audited the general purpose financial statements of City of Bisbee, Arizona (the City), as of and for the year ended June 30, 2003, and have issued our report thereon dated December 5, 2003, which was qualified because of the omission of the general fixed assets account group, and because we do not express an opinion on the amounts reported as fixed assets in the Enterprise Funds on the combined balance sheets or on the amount to record as depreciation expense in the Enterprise Funds on the statement of revenues, expenses and changes in retained earnings. Except as discussed in the preceding sentence, we conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether City of Bisbee, Arizona's general purpose financial statements are free of material misstatements, 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 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*. However, we noted certain immaterial instances of noncompliance, which we have reported to the management of City of Bisbee, Arizona, in a separate letter dated December 5, 2003.

Internal Control over Financial Reporting

In planning and performing our audit, we considered the City's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the general purpose financial statements and not to provide assurance on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control over financial reporting that, in our judgment, could adversely affect the City's ability to record, process, summarize, and report financial data consistent with the assertions of management in the general purpose financial statements. The reportable condition is described in the accompanying schedule as item 03-01.

To the City Council
City of Bisbee, Arizona

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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 general purpose 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 internal control over financial reporting would not necessarily disclose all such internal control matters that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we consider item 03-01 to be a material weakness. We also noted other matters involving internal control over financial reporting that we have reported to the management of the City in a separate letter dated December 5, 2003.

This report is intended solely for the information and use of management, others within the organization, City Council, 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. However, this report is a matter of public record and its distribution is not limited.

A handwritten signature in black ink that reads "Lester E. Chapman P.C." The signature is written in a cursive style with a large initial 'L' and 'C'.

December 5, 2003

Independent Auditors' Report on Compliance with Requirements
Applicable to Each Major Program and on Internal Control
Over Compliance in Accordance with OMB Circular A-133

To the City Council
City of Bisbee, Arizona

Compliance

We have audited the compliance of City of Bisbee, Arizona (the City) with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major programs for the year ended June 30, 2003. The City's major federal program is 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's management. Our responsibility is to express an opinion on the City's compliance based on our audit.

We conducted our audit of compliance in accordance with U.S. generally accepted auditing standards; 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's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the City's compliance with those requirements.

In our opinion, the City complied, in all material respects, with the requirements referred to above that are applicable to its major federal programs for the year ended June 30, 2003.

Internal Control Over Compliance

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

To the City Council
City of Bisbee, Arizona

Page Two

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be a material weakness. A material weakness is a condition in which the design or operation of one or more 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 management, others within the organization, City Council, 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. However, this report is a matter of public record and its distribution is not limited.

Lester E. Chapman P. C.

December 5, 2003

CITY OF BISBEE, ARIZONA
 SCHEDULE OF FINDINGS AND QUESTIONED COSTS
 YEAR ENDED JUNE 30, 2003

A. Summary of Audit Results

Financial Statements

Type of auditors' report issued:	Qualified	
	YES	NO
Material weakness identified in internal control over financial reporting?	<u> X </u>	<u> </u>
Reportable condition identified not considered to be material weakness?	<u> </u>	<u> X </u>
Noncompliance material to the financial statements noted?	<u> </u>	<u> X </u>

Federal Awards

Material weakness identified in internal control over major programs?	<u> </u>	<u> X </u>
Reportable condition identified not considered to be material weakness?	<u> </u>	<u> X </u>

Type of auditors' report issued on compliance for major programs: **Unqualified**

Any audit findings disclosed that are required to be reported in accordance with Circular A-133 (section .510[a])?	<u> </u>	<u> X </u>
--	---------------	--------------

Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
83.548	Hazard Mitigation Grant

Dollar threshold used to distinguish between Type A and Type B programs: **\$ 300,000**

Auditee qualified as low-risk auditee?	<u> </u>	<u> X </u>
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Other Matters

Auditee's summary schedule of prior audit findings required to be reported in accordance with Circular A-133 (section .315[b])?	<u> X </u>	<u> </u>
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CITY OF BISBEE, ARIZONA
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
CONTINUED
YEAR ENDED JUNE 30, 2003

B. Findings - Financial Statement Audit

Record Keeping: Material Weakness 03-01

STATEMENT OF CONDITION AND CRITERIA: The City has not taken a physical inventory of fixed assets in several years, resulting in inadequate accounting records and the failure to safeguard and properly account for fixed assets. As a result of this, our audit report states that an amount for the general fixed asset account group will not be shown on the combined balance sheet and that this is a departure from generally accepted accounting principles. Also, we do not express an opinion on the amount reported as fixed assets in the Enterprise Funds on the combined balance sheet or on the amount to report as depreciation expense in the Enterprise Funds on the statement of revenues, expenses, and changes in retained earnings.

RECOMMENDATION: To help ensure that fixed assets are properly recorded and physically accounted for and to comply with the Uniform Administrative Requirements for Grants and Cooperative Agreements with State and Local Governments (Common Rule, Subpart C, .32), the City should take a physical inventory of fixed assets at least every two years for federal assets and every three years for nonfederal assets, and reconcile such inventories to the fixed assets listings and general ledger.

C. Findings and Questioned Costs - Major Federal Award Programs Audit

None



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SCHEDULE OF PRIOR AUDIT FINDINGS
YEAR ENDED JUNE 30, 2003

Federal Award Findings and Questioned Costs

**Federal Emergency Management Association
CFDA No. 83.548 Hazard Mitigation Grant**

Noncompliance: 02-02

STATEMENT OF CONDITION: The City did not maintain evidence of at least two sealed bids for federal expenditures in excess of \$5,000.

RECOMMENDATION: In order to comply with the federal procurement requirements and Arizona Revised Statutes, we recommend that the City maintain required documentation of compliance with all applicable bidding requirements.

CURRENT STATUS: Corrected.

CORRECTIVE ACTION PLAN



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CORRECTIVE ACTION PLAN

YEAR ENDED JUNE 30, 2003

Financial Statement Findings

03-01

The City does not maintain accurate fixed asset records.

The City has substantially completed an inventory of fixed assets and land and is in the process of valuation for financial statement purposes.

Assets will be accurately reflected in the 2004 report.