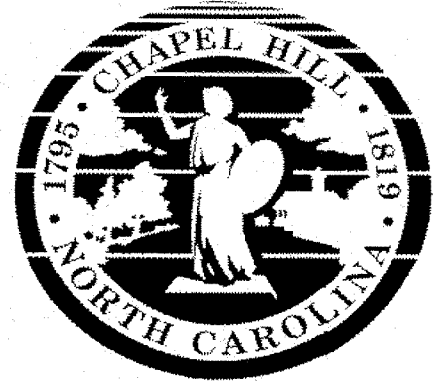


**Comprehensive  
Annual  
Financial  
Report**



**Town of  
Chapel Hill, North Carolina**

**Year Ended June 30, 2004**

**Town of Chapel Hill, North Carolina  
Comprehensive Annual Financial Report  
For the fiscal year ended June 30, 2004**

Prepared by:

Town of Chapel Hill Finance Department

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## TOWN OF CHAPEL HILL

September 8, 2004

To the Honorable Mayor, Town Council and  
Citizens of the Town of Chapel Hill  
Town of Chapel Hill, North Carolina

Ladies and Gentlemen:

State law requires that all general-purpose local governments publish a complete set of financial statements presented in conformity with generally accepted accounting principles (GAAP) and audited in accordance with generally accepted auditing standards by a firm of licensed certified public accountants. Pursuant to that requirement, we are pleased to submit to you the Comprehensive Annual Financial Report of the Town of Chapel Hill, North Carolina for the fiscal year ended June 30, 2004.

This report consists of management's representations concerning the finances of the Town of Chapel Hill. Consequently, management assumes full responsibility for the completeness and reliability of all the information presented in this report. To provide a reasonable basis for making these representations, management of the Town of Chapel Hill has established a comprehensive internal control framework that is designed both to protect the Town's assets from loss, theft, or misuses and to compile sufficient reliable information for the preparation of the Town of Chapel Hill's financial statements in conformity with GAAP. Because the cost of internal controls should not outweigh their benefits, the Town of Chapel Hill's comprehensive framework of internal controls has been designed to provide reasonable rather than absolute assurance that the financial statements will be free from material misstatement. To the best of our knowledge, this financial report is complete and reliable in all material respects.

The Town of Chapel Hill's financial statements have been audited by McGladrey & Pullen, LLP, a firm of independent licensed certified public accountants. The goal of the independent audit was to provide reasonable assurance that the financial statements of the Town of Chapel Hill for the fiscal year ended June 30, 2004, are free of material misstatement. The independent



audit involved examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; assessing the accounting principles used and significant estimates made by management; and evaluating the overall financial statement presentation. The independent auditor concluded, based upon the audit, that there was a reasonable basis for rendering an unqualified opinion that the Town of Chapel Hill's financial statements for the fiscal year ended June 30, 2004, are fairly presented in conformity with GAAP. The independent auditor's report is presented as the first component of the financial section of this report.

Generally Accepted Accounting Principles require that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with it.

### **Profile of the Town of Chapel Hill**

The Town is located principally in Orange County and slightly in Durham County in the north central portion of North Carolina on the Piedmont Plateau, approximately equidistant between Washington, D.C. and Atlanta, Georgia. The area's topography is characterized by rolling hills. The Town, which was chartered in 1819, presently covers an area of 21.1 square miles, serves an official State population of 51,485, and is the home of the University of North Carolina at Chapel Hill.

The Town is empowered by statute to levy an annual ad valorem tax on the appraised value of all taxable real and tangible personal property within its boundaries. Orange and Durham Counties are the other units levying such taxes within the corporate limits of the Town. The Town is also empowered by statute to extend its corporate limits by annexation.

The Town operates under a council-manager form of government. Policy-making and legislative authority are vested in the governing Town Council consisting of a mayor and eight other members. The Town Council appoints the members of various boards and commissions, the Town Manager, and Town Attorney. The Mayor presides over Council meetings and has full voting privileges.

The Mayor and all Council members are elected at large. Council members serve four-year terms. The Mayor and four Council members are elected every two years. All municipal elections are non-partisan.

The Town Manager is the chief administrative officer of the Town. He is the professional administrator who serves at the pleasure of the Town Council for an indefinite term.

This report includes all activities considered to be controlled by or dependent on the Town of Chapel Hill as well as its component unit. Those activities consist of the full range of municipal services contemplated by statute or the Town Charter. These services include public safety (fire, police and rescue), streets, sanitation, recreation, planning and zoning, inspections, general administration, parking and transportation. The Orange Water and Sewer Authority (OWASA) is the Town's only component unit. OWASA is a separate, legal entity for which the Town is financially accountable because the Town Council appoints a majority of the OWASA Board of Directors.

The annual budget serves as the foundation for the Town of Chapel Hill's financial planning and control. All departments of the Town are required to submit requests for appropriation to the Town Manager in January of each year. The Town Manager uses these requests as the starting point for developing a proposed budget. The Town Manager presents the proposed budget to the Council in April. The Council is required to hold public hearings on the proposed budget and to adopt a final budget by June 30. Formal budgetary accounting is employed for all funds, as a management control required by North Carolina General Statutes. Budgets are legally enacted by passage of an Annual Budget Ordinance and Project Budget Ordinances which may be formally amended as required. The Town Manager is authorized to transfer budget authorizations within departments, but changes of functions and total budgets of any fund require approval by the Town Council.

Budgetary control is maintained at the department level. Neither an operational expenditure nor an encumbrance is processed when the transaction would result in a department overrun. Open encumbrances are reported as reservations of fund balances at June 30, 2004.

The signature and authorization of the Town's Finance Director are required on all expenditure documents before checks are processed. Payroll checks are authorized by department heads and controlled by the budgeted position list maintained in the computerized payroll system.

The diverse nature of governmental operations and the necessity of assuring legal compliance preclude recording and summarizing all governmental financial transactions and balances in a single accounting entity. Therefore, from an accounting and financial management viewpoint, a governmental unit is a combination of several distinctly different fiscal and accounting entities, each having a separate set of accounts and functioning independently of each other. Each accounting entity is accounted for in a separate "fund". A fund is defined as a fiscal accounting

entity with a self-balancing set of accounts recording cash and other financial resources together with all related liabilities and residual equities or balances, and changes therein, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations.

### **Factors Affecting Financial Condition**

The information presented in the financial statements is perhaps best understood when it is considered from the broader perspective of the specific environment within which the Town of Chapel Hill operates.

**Local economy.** The Town of Chapel Hill is a part of Triangle region of North Carolina, which includes the Research Triangle Park, a major complex of research and research-oriented manufacturing facilities. The Town and Orange County and the Research Triangle Park area continue to experience growth and are considered to be among the most desirable areas of the country to live and work, according to several national surveys.

The economy of the Town is characterized by a high degree of institutional and public sector activity, plus office, commercial and service-oriented businesses. The University of North Carolina at Chapel Hill and the University of North Carolina Health Care System are the largest employers in the Town, providing approximately 22,000 jobs. These institutions contribute significantly to the low unemployment rate in the Town and Orange County. The Town's unemployment rate has been below State and national rates over the last five years. The Town's economy is expected to remain relatively strong in the foreseeable future because of the benefits derived from the low unemployment rate and a stable employment base.

**Long-term financial planning.** The Town is considering several new capital projects which could affect Town borrowings and future debt payments. The first of these projects is the new Town Operations Center which will be needed by the end of 2006 at a cost of approximately \$43 million. The Chapel Hill Public Works/Transit operations facilities have been located on the University's Horace Williams tract since 1977. The lease expires on December 31, 2006, and the lease will not be renewed after that date.

The Town has acquired a site on Millhouse Road, north of Eubanks Road, between I-40 and the railroad, for the new location of essential Town services. The planned operations center would house the Chapel Hill Transit System's operations, maintenance and administration functions, and the Public Works Department's solid waste, landscaping, field operations, fleet management, buildings maintenance and administration functions and a maintenance facility for

the Town's Public Housing program. It is anticipated that the design and construction of an operations center will be the largest single capital project in the Town's history.

The financing plan for the Town Operations Center includes the following: Capital Improvements Fund funding for annual payments on the Town Operations Center site purchase; anticipated partial funding from the Federal Transit Administration for the construction of the transportation facility portion of the project; anticipated partial funding from the federal Department of Housing and Urban Development; and debt financing for the construction of the remainder of the Public Works operational facility. The Town would need to finance approximately \$25 million not covered by federal grants. The Town anticipates the need for additional short-term financing of no more than \$12 million to cover cash needs in anticipation of federal and State grants.

On April 14, 2003 the Town Council unanimously adopted the Library Building Program as a part of the Library Master Plan. The Plan calls for the expansion of the present library building from 27,000 square feet to 75,500 square feet, the addition of user seating to accommodate 279 users instead of the current 120, and an increase in books and other materials. In addition to the Library Building Program, the Council recommended that the citizens of Chapel Hill consider bond financing for several other proposals.

In November 2003, voters of the Town of Chapel Hill approved a bond referendum for the following projects:

Project	Amount	Purpose
Library Building Improvements	\$ 16,260,000	Expansion of the Town library
Sidewalk and Streets	5,600,000	Construct 50% of sidewalk priorities Upgrade pedestrian amenities Make improvements for bicycle and pedestrian safety Make downtown streetscape improvements
Parks and Recreation Facilities	5,000,000	Construct 50% of greenway plans
Open Spaces and Areas	2,000,000	Purchase open space
Public Buildings	500,000	Establish an energy bank
Total	<u>\$ 29,360,000</u>	

The Council has approved the sale of the first \$4 million portion of these bonds for fall of 2004. The \$4 million will include \$500,000 for library facilities planning, \$300,000 for parks and recreation facilities, \$500,000 for energy efficiency building improvements and \$1.5 million for

sidewalks, pedestrian and cyclist amenities and downtown streetscape improvements. Additional sales are proposed as follows:

Year of Issuance	2006	2008	2009	Total
Amount	\$7.75 Million	\$8.805 Million	\$8.805 Million	\$25.36 Million

The potential effect of these projects on future property tax rates will be affected by the prevailing interest rates at the time of the various issuances, the receipt of federal funding related to the Town Operations Center, the timing of the implementation of the proposed projects and the availability of other sources or cost savings to fund the projects.

**Cash and Revenue Management.** Cash temporarily idle during the year was invested in a time deposit account and the State Treasurer’s investment pool. The average yield on investments was approximately 1.27% during fiscal year 2003-04. The Town earned interest revenue of \$192,595 on governmental funds for the year ended June 30, 2004.

The Town’s investment policy emphasizes safety and liquidity while maintaining a competitive yield on its portfolio. Accordingly, the majority of deposits were either insured by federal depository insurance or fully collateralized. Over 95 percent of the investments held by the Town at June 30, 2004 are classified in the category of lowest credit risk as defined by the Governmental Accounting Standards Board. This percentage did not fall below 75 percent at any time during the year.

**Risk Management.** The Town protects itself from potential loss through participation in the Interlocal Risk Financing Fund of North Carolina for general liability, automobile liability, public officials liability, law enforcement liability and property losses. The Town also participates in the Interlocal Risk Management Pool of North Carolina for workers' compensation. The Town's potential loss for liability coverages is limited to the deductible amount of \$2,500 per claim for all coverages, except public officials, which is limited to the deductible amount of \$5,000 per claim. The potential loss for workers' compensation is limited to the deductible amount of \$5,000 per claim.

### **Awards and Acknowledgements**

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the Town of

Chapel Hill for its Comprehensive Annual Financial Report for the fiscal year ended June 30, 2003.

The Certificate of Achievement is a prestigious national award recognizing conformance with the highest standards for preparation of State and local government financial reports. In order to be awarded a Certificate of Achievement, a governmental unit must publish an easily readable and efficiently organized comprehensive annual financial report, whose contents conform to program standards. Such reports must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe our current report continues to conform to the Certificate of Achievement Program requirements, and we are submitting it to GFOA to determine its eligibility for another Certificate.

In addition, the Town also received the GFOA's Distinguished Budget Presentation Award for its annual budget document for 2003-04. In order to qualify for the Distinguished Budget Presentation Award, the Town's budget document was judged to be proficient in all required categories, including as a policy document, a financial plan, an operations guide, and a communications device.

The presentation of this report could not have been accomplished without the efficient and dedicated services of the entire staff of the Finance Department and the various employees from other departments. We would like to express our appreciation to all members of the Department, other employees, and to the independent certified public accountants, McGladrey & Pullen, LLP, who assisted and contributed to its preparation.

We would also like to thank the Mayor and members of the Town Council for their interest and support in planning and conducting the financial operations of the Town in a responsible and progressive manner.

Respectfully submitted,

A handwritten signature in black ink that reads "W. Calvin Horton". The signature is written in a cursive style with a large initial "W" and a prominent "H".

W. Calvin Horton  
Town Manager

A handwritten signature in black ink that reads "Kay Johnson". The signature is written in a cursive style with a large initial "K" and a prominent "J".

Kay Johnson  
Finance Director

# Certificate of Achievement for Excellence in Financial Reporting

Presented to

Town of Chapel Hill,  
North Carolina

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
June 30, 2003

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



*Nancy L. Ziehl*

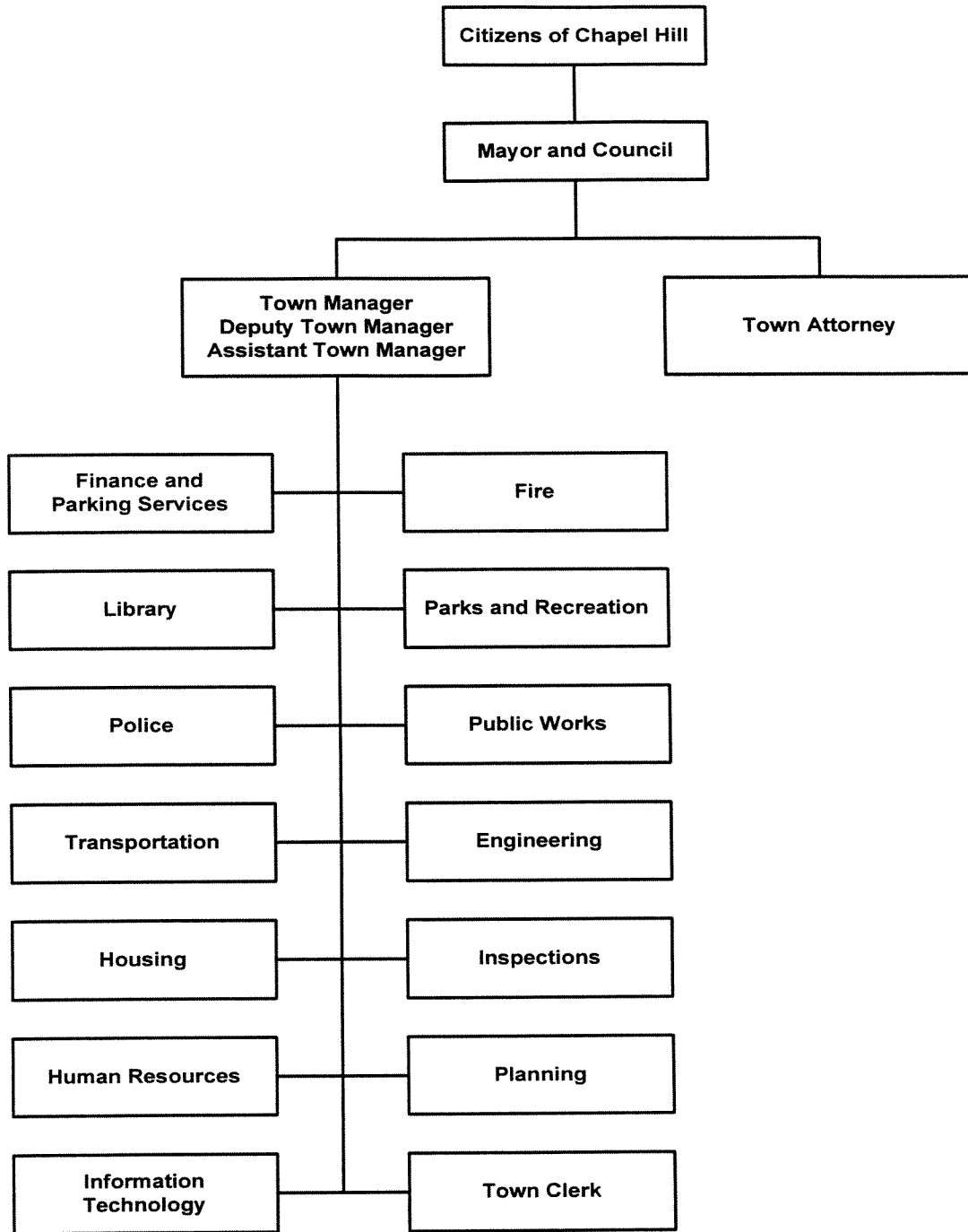
President

*Jeffrey R. Emer*

Executive Director



# TOWN OF CHAPEL HILL ORGANIZATIONAL CHART



**TOWN OF CHAPEL HILL, NORTH CAROLINA  
THE TOWN GOVERNING BODY AND OFFICIALS  
JUNE 30, 2004  
MEMBERS OF THE GOVERNING BODY**

**Mayor**  
Kevin Foy

**Mayor pro tem**  
Edith Wiggins

**Council Members**

Sally Greene

Ed Harrison

Cam Hill

Mark Kleinschmidt

Bill Strom

Dorothy Verkerk

Jim Ward

**Officials**

W. Calvin Horton

Town Manager

Florentine M. Miller

Deputy Town Manager

Bruce A. Heflin II

Assistant Town Manager

Kathleen A. Johnson

Finance Director

Ralph D. Karpinos

Town Attorney

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# McGladrey & Pullen

Certified Public Accountants

## Independent Auditor's Report

To the Honorable Mayor and  
the Members of the Town Council  
Town of Chapel Hill, North Carolina

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the Town's component unit, each major fund, and the aggregate remaining fund information of the Town of Chapel Hill, North Carolina (the "Town"), as of and for the year ended June 30, 2004, which collectively comprise the Town's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Town's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

In our opinion, based on our audit, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the Town's component unit, each major fund, and the aggregate remaining fund information of the Town of Chapel Hill, North Carolina, as of June 30, 2004, and the respective changes in financial position and cash flows, where applicable, thereof and for the respective budgetary comparison for the general fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note O to the financial statements, the June 30, 2003 financial position of the governmental activities of the Town has been restated to recognize previously unrecorded land underlying general government infrastructure fixed assets.

In accordance with *Government Auditing Standards*, we have also issued a report dated September 7, 2004 on our consideration of the Town's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis and the required supplementary information on pages 3 through 13 and 67 through 68 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Town of Chapel Hill, North Carolina's basic financial statements. The accompanying supplementary information, such as the introductory section, combining and individual nonmajor fund financial statements, statistical tables, as well as the accompanying schedule of expenditures of federal and State awards as required by the U. S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and the State Single Audit Implementation Act, are presented for purposes of additional analysis and are not a required part of the basic financial statements. The supplementary information and the accompanying schedule of expenditures of federal and State awards has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory section and the statistical tables have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

*McGladrey & Pullen, LLP*

Greensboro, North Carolina  
September 7, 2004

## Management's Discussion and Analysis

As management of the Town of Chapel Hill, we offer readers of the Town's financial statements this narrative overview and analysis of the financial activities for the fiscal year ended June 30, 2004. We encourage readers to read the information presented here in conjunction with additional information that we have furnished in the Town's financial statements, which follows this narrative.

### Financial Highlights

- The net assets of the Town of Chapel Hill exceeded its liabilities at the close of the fiscal year by \$83,381,375.
- The government's total net assets increased by \$4,747,408, due to increases in the governmental activities' net assets.
- As of the close of the current fiscal year, the Town of Chapel Hill's governmental funds reported combined ending fund balances of \$16,592,073, a decrease of \$2,286,402 in comparison with the prior year. Approximately 46.6% of this total amount, or \$7,725,834 is available for spending at the government's discretion (*unreserved fund balance*). Of the available balance, the Town has designated \$1,630,818 for the 2004-05 budget.
- At the end of the current fiscal year, unreserved fund balance for the General Fund was \$7,133,550, or 19.2% of total general fund expenditures for the fiscal year. \$1,499,000 of this amount was appropriated to balance the 2004-05 budget.
- The Town of Chapel Hill's total debt decreased by \$642,141 (1.9%) during the current fiscal year. The key factors in this decrease were the payoff of General Obligation debt in the amount of \$1,670,000 partially offset by an increase to installment notes payable for the purchase of vehicles and computers.
- The Town of Chapel Hill maintained its Aaa bond rating for the 6th consecutive year from Moody's and it's Aa+ rating from Standard and Poor's.

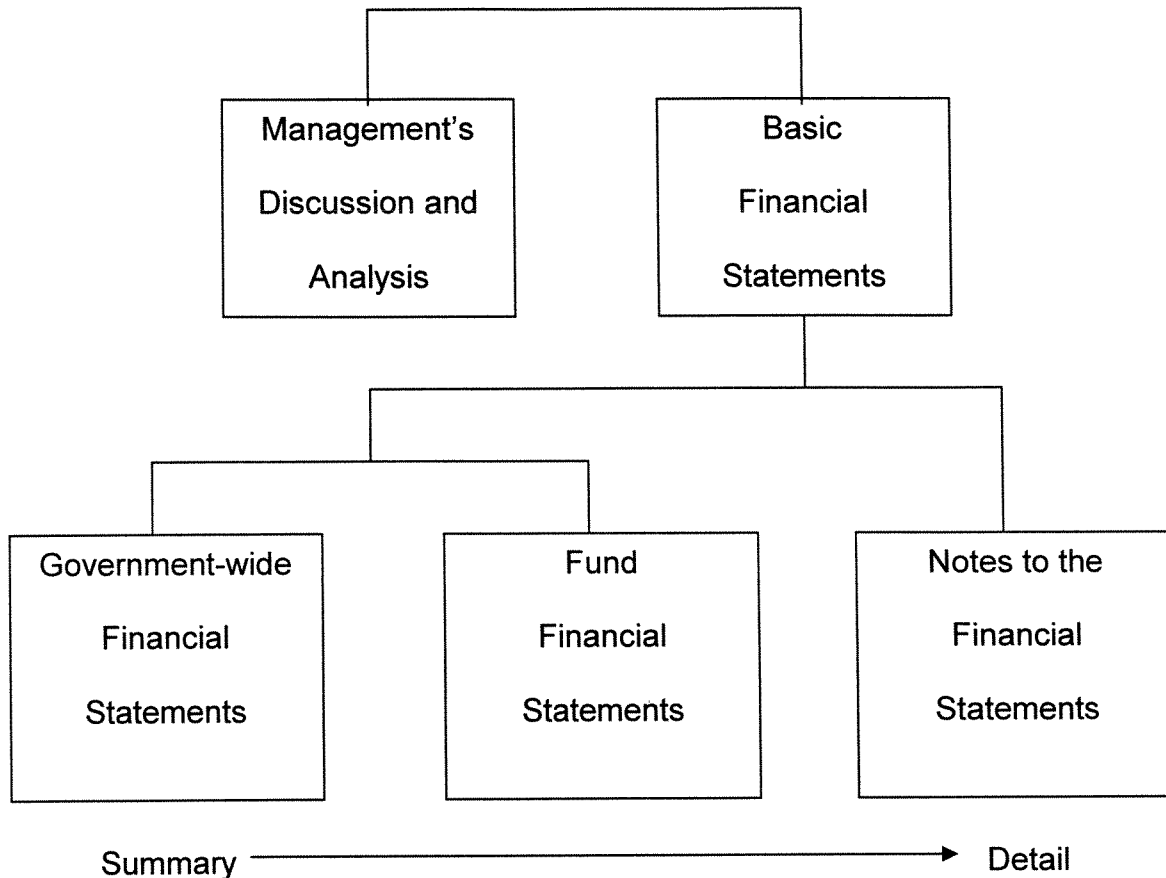
### Overview of the Financial Statements

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

The final section of the Town of Chapel Hill's financial statements is the federally mandated "Single Audit". The Single Audit Section is prepared to comply with the Single Audit Act of 1996 and the State Single Audit Implementation Act. Reports on internal control and compliance along with a schedule of financial assistance, are presented to reflect federal, State and local participation in various projects and programs, as adopted by the Town Council.

## Required Components of Annual Financial Report

Figure 1



### Government-wide Financial Statements

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

The two government-wide statements report the Town's net assets and how they have changed. Net assets are the difference between the Town's total assets and total liabilities. Measuring net assets is one way to gauge the Town's financial condition.

The government-wide statements are divided into three categories: 1) governmental activities; 2) business-type activities; and 3) component units. Governmental activities include most of the Town's basic services such as public safety, parks and recreation, and general administration. Property taxes and State and federal grant funds finance most of these activities. Business-type activities are those that the Town manages like a for-profit business. These include the parking fund, where profits from parking cover the cost of parking services, and the transportation fund,

which is managed like a for-profit business even though the Town continues to provide fare-free service for most of the transportation services.

The final category is the component unit. Although legally separate from the Town, the Town shows Orange Water and Sewer Authority as a component unit on its financial statements, because the Town exercises control over OWASA's Board by appointing a majority of its members.

The government-wide financial statements are in Exhibits 1 and 2 of this report.

## **Fund Financial Statements**

The fund financial statements (see Figure 1) provide a more detailed look at the Town's most significant activities. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Town of Chapel Hill, like all other governmental entities in North Carolina, uses fund accounting to ensure and reflect compliance (or non-compliance) with finance-related legal requirements, such as the General Statutes and the Town's budget ordinance.

All of the funds of the Town of Chapel Hill can be divided into two categories: governmental funds and proprietary funds. There are three parts to the Fund Financial Statements: 1) the governmental funds statements, 2) the budgetary comparison statements, and 3) the proprietary funds statements. The Town's Fund Financial Statements are on Exhibits 3 through 10.

**Governmental Funds** – Governmental funds are used to account for those functions reported as governmental activities in the government-wide financial statements. Most of the Town's basic services are accounted for in governmental funds. These funds focus on how assets can readily be converted into cash flow in and out, and what monies are left at year-end that will be available for spending in the next year. Governmental funds are reported using an accounting method called *modified accrual accounting* which provides a short-term spending focus. As a result, the governmental fund financial statements give the reader a detailed short-term view that helps the reader determine if there is an increase or decrease in financial resources available to finance the Town's programs. The relationship between government activities (reported in the Statement of Net Assets and the Statement of Activities) and governmental funds is described in a reconciliation that is a part of the fund financial statements.

The Town adopts an annual budget for its General Fund, as required by the General Statutes. The budget is a legally adopted document that incorporates input from the citizens of the Town, the management of the Town, and the Town Council decisions about which services to provide and how to pay for them. It also authorizes the Town to obtain funds from identified sources to finance these current period activities. The budgetary statement for the General Fund demonstrates how well the Town complied with the budget ordinance and whether or not the Town succeeded in providing the services as planned when the budget was adopted. The budgetary comparison statement uses the budgetary basis of accounting and is presented using the same format, language, and classifications as the legal budget document. The statement shows four columns: 1) the original budget as adopted by the Council, 2) the final budget as amended by the Council, 3) the actual resources, charges to appropriations, and ending balances in the General Fund, and 4) the difference or variance between the final budget and the actual resources and charges. To account for the difference between the budgetary basis of accounting and the modified accrual basis, a reconciliation showing the differences in the reported activities is shown on pages 22 and 25.



**Proprietary Funds** – The Town of Chapel Hill has two different kinds of proprietary funds. *Enterprise Funds* are used to report the same functions presented as business-type activities in the government-wide financial statements. The Town of Chapel Hill uses enterprise funds to account for both transportation and parking operations. These funds are the same as those functions shown in the business-type activities in the Statement of Net Assets and the Statement of Activities. *Internal Service Funds* are an accounting device used to accumulate and allocate costs internally among the functions of the Town of Chapel Hill. The Town uses internal service funds to account for three activities – the central garage, the purchase of vehicles, and the purchases of computer equipment and software. Because these operations predominantly benefit governmental rather than business-type activities, the internal service funds have been included within the governmental activities in the government-wide financial statements.

**Notes to the Financial Statements** – The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements are on pages 43 through 66 of this report.

**Supplemental Information** – In addition to the basic financial statements and accompanying notes, this report includes certain required supplementary information concerning the Town of Chapel Hill's progress in funding its obligation to provide separation allowance for law enforcement officers. Budgetary information required by the General Statutes can be found in this part of the statements. Required supplementary information can be found beginning on page 67 of this report.

### **Government-Wide Financial Analysis**

The Town uses the financial statement reporting model mandated by the Governmental Accounting Standards Board (GASB). GASB Statement 34 dictates the changes in the Town's financial reports beginning with the financial reports for fiscal year 2002-03.

## Town of Chapel Hill's Net Assets

**Figure 2**

	Governmental	Business-Type	Total
	Activities	Activities	
	2004	2004	2004
Current and other assets	\$ 22,587,974	3,878,281	26,466,255
Capital assets	74,286,429	20,747,385	95,033,814
Total assets	<u>96,874,403</u>	<u>24,625,666</u>	<u>121,500,069</u>
Long-term liabilities outstanding	23,605,805	6,442,397	30,048,202
Other liabilities	7,490,426	580,066	8,070,492
Total liabilities	<u>31,096,231</u>	<u>7,022,463</u>	<u>38,118,694</u>
Net assets:			
Invested in capital assets, net of related debt	48,939,875	14,367,385	63,307,260
Restricted	10,888,825	-	10,888,825
Unrestricted	5,949,472	3,235,818	9,185,290
Total net assets	<u>\$ 65,778,172</u>	<u>\$ 17,603,203</u>	<u>\$ 83,381,375</u>

As noted earlier, net assets may serve over time as one useful indicator of a government's financial condition. The assets of the Town of Chapel Hill exceeded liabilities by \$83,381,375 as of June 30, 2004. The Town's net assets increased by \$4,747,408 for the fiscal year ended June 30, 2004. However, the largest portion (75.9%) of net assets reflects the Town's investment in capital assets (e.g. land, buildings, machinery, and equipment), less any related debt still outstanding that was issued to acquire those items. The Town of Chapel Hill uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the Town of Chapel Hill's investment in its capital assets is reported net of the outstanding related debt, the resources needed to repay that debt must be provided by other sources, since the capital assets cannot be used to liquidate these liabilities. An additional portion of the Town of Chapel Hill's net assets (13.1%) represents resources that are subject to external restrictions on how they may be used. The remaining balance of \$9,185,290 is unrestricted.

Several particular aspects of the Town's financial operations positively influenced the total unrestricted governmental net assets:

- Receipt of unbudgeted revenues for the current year property taxes and Utility Franchise Tax in fiscal year 2004 of approximately \$550,000 and \$355,000 million, respectively.
- Continued diligence in the collection of property taxes by maintaining a tax collection percentage of 99.96.
- Increased licensing and permits fees for construction, especially in the Meadowmont development.
- Low cost of debt due to the Town's high bond rating and the current bond market.

**Town of Chapel Hill's Changes in Net Assets**  
**Figure 3**

	Governmental Activities 2004	Business-Type Activities 2004	Total 2004
<b>Revenues:</b>			
<b>Program revenues:</b>			
Charges for services	\$ 4,333,546	\$ 2,419,340	\$ 6,752,886
Operating grants and contributions	6,182,753	8,482,726	14,665,479
Capital grants and contributions		599,175	599,175
<b>General revenues:</b>			
Taxes	30,430,218	2,190,261	32,620,479
Grants and contributions not restricted to specific programs	2,683,589		2,683,589
Other	2,703,086	117,901	2,820,987
<b>Total revenues</b>	<b>46,333,192</b>	<b>13,809,403</b>	<b>60,142,595</b>
<b>Expenses:</b>			
General government	3,641,608		3,641,608
Environment and development	16,793,496		16,793,496
Public safety	15,280,202		15,280,202
Leisure activities	4,617,299		4,617,299
Nondepartmental	962,489		962,489
Interest expense	880,610		880,610
Transportation		11,469,835	11,469,835
Parking Facilities		1,749,648	1,749,648
<b>Total expenses</b>	<b>42,175,704</b>	<b>13,219,483</b>	<b>55,395,187</b>
Increase in net assets before transfers	4,157,488	589,920	4,747,408
Transfers	347,376	(347,376)	-
Increase in net assets	4,504,864	242,544	4,747,408
Net assets, July 1, 2003, as previously reported	53,529,120	17,360,659	70,889,779
Restatement (See Note O)	7,744,188	-	7,744,188
Net assets, July 1, 2003, as restated	61,273,308	17,603,203	78,633,967
Net assets, June 30, 2004	\$ 65,778,172	\$ 17,603,203	\$ 83,381,375

**Governmental activities.** Governmental activities show an increase in net assets of \$4,504,864. The increase is primarily due to the purchases land and construction. Projects include the Town Operations Center at a cost of about \$733,000; land for Parks and Recreation projects at a costs of approximately \$1.7 million, including just over \$1 million for Dry Creek Trail, about \$470,000 for Morgan Creek Greenways with additional amounts for smaller land

purchases. The Town borrowed just over \$1 million for a number of capital repairs including roofs and tennis courts. Because the projects were largely completed before the borrowing was put into place, net assets increased. In addition, Utility Franchise Fees exceeded budget by \$355,275 and the Town has about \$96,000 in unspent Community Development program income.

**Business-type activities:** Business-type activities increased the Town of Chapel Hill's net assets by \$242,544. The increase in net assets come from the Transportation Fund where charges for services exceeded budget by about \$133,000 and personnel expenses were below budget by about \$162,000 because of vacant positions. The Parking Facilities Fund experienced a decrease in net assets of about \$63,000 primarily because of the loss of a major business parking space rental tenant at one of the Town lots. Otherwise, parking revenues were at or above budget.

### **Financial Analysis of the Town's Funds**

As noted earlier, the Town of Chapel Hill uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

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

The general fund is the chief operating fund of the Town of Chapel Hill. At the end of the current fiscal year, unreserved fund balance of the General Fund was \$7,133,550 of which \$5,634,550 is undesignated, while total fund balance reached \$11,772,637. As a measure of the general fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved, undesignated fund balance represents 15.2% of total General Fund expenditures, while total fund balance represents 31.8% of that same amount.

At June 30, 2004, the governmental funds of the Town of Chapel Hill reported a combined fund balance of \$16,592,073, a 12.1% decrease over last year. Included in this change in fund balance is a decrease in fund balance in the Capital Projects Ordinance Fund.

**General Fund Budgetary Highlights:** During the fiscal year, the Town revised the budget on several occasions. Generally, budget amendments fall into one of three categories: 1) amendments made to adjust the estimates that are used to prepare the original budget ordinance once exact information is available; 2) amendments made to recognize new funding amounts from external sources, such as federal and State grants; and 3) increases in appropriations that become necessary to maintain services.

Conservative budgeting principles result in actual revenues exceeding budget estimates. This year the actual revenues were approximately \$1,146,000 more than the revenue budget. This difference is because of conservative budgeting with property taxes exceeding budget by about \$520,000 and utility franchise fees exceeding budget by about \$355,000. Expenditures were approximately \$1,800,000 less than budgeted. A portion of the underexpenditure represents the effect of departments spending under their total budgeted limit. A portion of the excess of

budget over actual expenditures represents purchase orders open at year end that, with the approval of the Town Council, are carried forward to the new year. The Town plans for actual revenues to exceed actual expenditures by at least the \$800,000 each year to become a part of appropriated fund balance in the following year.

**Proprietary Funds.** The Town of Chapel Hill's proprietary funds provide the same type of information found in the government-wide statements but in more detail. Unrestricted net assets of the Transportation Fund at the end of the fiscal year amounted to \$2,343,819, and those for the Parking Facilities Fund amounted to \$891,999. The total change in net assets for both funds was \$305,452 and (\$62,908), respectively. Other factors concerning the finances of these two funds are addressed in the discussion of the Town of Chapel Hill's business-type activities.

### **Capital Asset and Debt Administration**

**Capital assets.** The Town of Chapel Hill's investment in capital assets for its governmental and business-type activities as of June 30, 2004, totals \$95,033,814 (net of accumulated depreciation). These assets include buildings, roads and bridges, land, machinery and equipment, park facilities, and vehicles.

Major capital asset transactions during the year include the following additions:

- \$1,910,571 for land for open space, greenways and parks;
- \$1,175,894 for the completion of the Hargraves Community Center and pool; and
- \$ 946,379 for replacements of a portion of the Town's rolling stock.

Additional construction in progress of \$2,337,371 in governmental-type activities include:

- \$582,013 for design work on the Town Operations Center;
- \$299,878 for land purchase for Tanyard Branch Trail; and
- \$218,685 for Inter Faith Council Shelter.

No major demolitions were recorded this year.

**Town of Chapel Hill Capital Assets  
(net of depreciation)**

**Figure 4**

	Governmental Activities June 30, 2004	Business-type Activities June 30, 2004	Total June 30, 2004
Land	\$ 23,862,553	\$ 4,789,425	\$ 28,651,978
Land improvements	4,432,705	2,071,458	6,504,163
Infrastructure	15,787,646	-	15,787,646
Buildings and building improvements	18,500,818	3,878,179	22,378,997
Equipment and vehicles	4,390,820	10,008,323	14,399,143
Construction in progress	7,311,887	-	7,311,887
<b>Total</b>	<b>\$ 74,286,429</b>	<b>\$ 20,747,385</b>	<b>\$ 95,033,814</b>

Additional information on the Town's capital assets can be found on pages 53-54 of the Basic Financial Statements.

**Long-term Debt.** As of June 30, 2004, the Town of Chapel Hill had total outstanding bonded debt, backed by the full faith and credit of the Town of \$18,400,000.

**Town of Chapel Hill  
Outstanding Debt**

**Figure 5**

	Governmental Activities June 30, 2004	Business-type Activities June 30, 2004	Total June 30, 2004
General obligation bonds	\$ 18,400,000	\$ -	\$ 18,400,000
Installment notes payable	6,526,774	-	6,526,774
Separation allowance	419,780	-	419,780
Compensated absences	1,532,215	299,286	1,831,501
Certificates of participation	-	6,380,000	6,380,000
<b>Total</b>	<b>\$ 26,878,769</b>	<b>\$ 6,679,286</b>	<b>\$ 33,558,055</b>

The Town of Chapel Hill's total debt decreased by \$642,141 (1.9%) during the past fiscal year. The debt includes \$6,526,774 in installment purchase financing primarily for rolling stock and land for the Town Operations Center.

As mentioned in the financial highlights section of this document, the Town of Chapel Hill maintained its Aaa bond rating from Moody's Investor Service and AA+ rating from Standard and Poor's Corporation for the 6<sup>th</sup> consecutive year. This bond rating is a clear indication of the Town's sound financial condition. The Town of Chapel Hill is among a small number of municipalities its size in the country that maintains such a high financial rating. This achievement is a primary factor in keeping interest costs low on the Town's outstanding debt.

North Carolina general statutes limit the amount of general obligation debt that a unit of government can issue to 8 percent of the total assessed value of taxable property located within that government's boundaries. The legal debt margin for Town of Chapel Hill is \$326 million, well above the Town's outstanding debt for general obligation bonds of approximately \$18 million.

Additional information regarding the Town of Chapel Hill's long-term debt can be found beginning on page 56 of this report.

### **Economic Factors and Next Year's Budgets and Rates**

The following key economic indicators reflect the growth and prosperity of the Town.

- Low unemployment. The Town of Chapel Hill unemployment rate of 3.0% is well below the State average of 6.6%.
- Stable property tax base. The Town of Chapel Hill continues to collect property taxes at a rate in excess of 99%.
- Housing values. Average housing values within the Town continue to exceed those of surrounding jurisdictions. (For calendar year 2003, the average Chapel Hill home sold was valued at \$320,918; the average Durham County home sold was valued at \$173,844, the average Wake County home was valued at \$212,382; and the average Orange County home was valued at \$280,592.)

### **Budget Highlights for the Fiscal Year Ending June 30, 2005**

**Governmental Activities:** Property taxes, benefiting from economic growth, are expected to lead the increase in budgeted revenues in the General Fund with an increase of \$1,500,000 or 7%, comparing original budget 2003-04 to original budget 2004-05. In comparing actual receipts of \$21.6 million in 2003-04 to the 2004-05 budget of \$22.6 million, the increase is 4.5%. The Town will use these increases in revenues to finance programs currently in place.

Budgeted expenditures (excluding transfers) in the General Fund are expected to rise 7% to \$39,057,500. The largest increments are in employee compensation, including funding compensation and benefits adjustments.

**Business – type Activities:** The Town continued the policy of providing fare-free service for most transportation services. As a result of the increases for employee compensation and benefit adjustments, as well as additional staff for the EZ rider program, the budget for the

transportation department has increased by \$705,552 or 6.6%. Parking Facilities Fund revenues and expenditures are budgeted to remain approximately the same next year as this year, with an increase of about \$14,000 to fund compensation and benefits adjustments off-set by an increase in revenues from parking.

### **Requests for Information**

This report is designed to provide an overview of the Town's finances for those with an interest in this area. Questions concerning any of the information found in this report or requests for additional information should be directed to the Director of Finance, Town of Chapel Hill, 306 N. Columbia Street, Chapel Hill, NC 27516.



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