

Washington State Auditor's Office
Financial Statements Audit Report

City of Oak Harbor
Island County

Audit Period
January 1, 2009 through December 31, 2009

Report No. 1004826

Issue Date
December 27, 2010



WASHINGTON
BRIAN SONNTAG
STATE AUDITOR



**Washington State Auditor
Brian Sonntag**

December 27, 2010

Mayor and City Council
City of Oak Harbor
Oak Harbor, Washington

Report on Financial Statements

Please find attached our report on the City of Oak Harbor's financial statements.

We are issuing this report in order to provide information on the City's financial condition.

Sincerely,

BRIAN SONNTAG, CGFM
STATE AUDITOR

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Island County
January 1, 2009 through December 31, 2009**

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Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters in Accordance with *Government Auditing Standards*

City of Oak Harbor
Island County
January 1, 2009 through December 31, 2009

Mayor and City Council
City of Oak Harbor
Oak Harbor, Washington

We have audited the financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Oak Harbor, Island County, Washington, as of and for the year ended December 31, 2009, which collectively comprise the City's basic financial statements, and have issued our report thereon dated November 19, 2010

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to the financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit, we considered the City's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the City's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of the City's compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended for the information and use of management and the Mayor and City Council. However, this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

A handwritten signature in black ink, appearing to read "Brian Sonntag". The signature is fluid and cursive, with a large initial "B" and "S".

BRIAN SONNTAG, CGFM
STATE AUDITOR

November 19, 2010

Independent Auditor's Report on Financial Statements

**City of Oak Harbor
Island County
January 1, 2009 through December 31, 2009**

Mayor and City Council
City of Oak Harbor
Oak Harbor, Washington

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Oak Harbor, Island County, Washington, as of and for the year ended December 31, 2009, which collectively comprise the City's basic financial statements as listed on page 5. These financial statements are the responsibility of the City'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 opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Oak Harbor, as of December 31, 2009, and the respective changes in financial position and, where applicable, cash flows thereof, and the budgetary comparison for the General Fund, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and 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 on pages 6 through 14 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted

principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

A handwritten signature in black ink, appearing to read "Brian Sonntag". The signature is fluid and cursive, with the first name "Brian" and last name "Sonntag" clearly distinguishable.

BRIAN SONNTAG, CGFM
STATE AUDITOR

November 19, 2010

Financial Section

**City of Oak Harbor
Island County
January 1, 2009 through December 31, 2009**

REQUIRED SUPPLEMENTAL INFORMATION

Management's Discussion and Analysis – 2009

BASIC FINANCIAL STATEMENTS

Statement of Net Assets – 2009
Statement of Activities – 2009
Balance Sheet – Governmental Funds – 2009
Reconciliation of the Balance Sheet of the Governmental Funds to the Statement of Net Assets – 2009
Statement of Revenues, Expenditures and Changes in Fund Balance – Governmental Funds – 2009
Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balance of the Governmental Funds to the Statement of Activities – 2009
Statement of Revenues, Expenditures and Changes in Fund Balances – Budget to Actual – General Fund – 2009
Statement of Net Assets – Proprietary Funds – 2009
Statement of Revenues, Expenses and Changes in Fund Net Assets – Proprietary Funds – 2009
Statement of Cash Flows – Proprietary Funds – 2009
Notes to Financial Statements – 2009

Management Discussion and Analysis

As management of the City of Oak Harbor, we offer readers of the city's financial statements this narrative overview and analysis of the financial activities of the City of Oak Harbor for the fiscal year ended December 31, 2009. This information is provided in an effort to assist the reader in focusing on significant financial events, to provide an overview of the City's financial activity, to identify changes in the City's financial position, to identify deviations from the City's adopted budget, and to identify individual fund issues and concerns. We encourage readers to consider the information presented here in conjunction with additional information presented in the form of financial statements, footnotes, and other data.

Financial Highlights

- The City's overall financial condition improved in 2009, as compared to 2008.
- Total City's net assets on a consolidated basis equal \$115,549,959, representing the net difference between assets and liabilities. This balance is comprised of \$66,333,549 invested in net capital assets, net of related debt, \$16,600,130 in restricted net assets for capital projects, \$953,353 in restricted assets for debt service, and \$31,662,927 in unrestricted net assets.
- As shown on the Statement of Net Assets, fiscal year December 31, 2009 ended with an Unrestricted Net Asset Balance of \$11,674,219 in Governmental Activities. These monies are intended to provide a cushion against significant downturns in revenues and to maintain sufficient working capital and cash flow to meet daily financial needs. Other reserves have been designated by management to address annual budget amendments, vehicle and equipment replacements, major building repairs, and future facility improvements.
- Total Change in Net Assets, as found on the Statement of Activities, from Governmental activities and Business-type activities is \$1,641,425 and \$3,938,389, respectively.

Overview of the Financial Statements

This discussion and analysis are intended to serve as an introduction to the City of Oak Harbor's basic financial statements. The City of Oak Harbor's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves. The City of Oak Harbor has adopted the provisions of Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements – Management's Discussion and Analysis – for State and Local Governments* as of January 1, 2002.

Government-wide Financial Statements

The government-wide financial statements are designed to provide readers with a broad overview of the City of Oak Harbor's finances, in a manner similar to a private-sector business.

The *Statement of Net Assets* presents information on all the City's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City is improving or deteriorating.

The *Statement of Activities* presents information showing how the City's net assets changed during the most recent fiscal year. All changes in the net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in the statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of the government-wide financial statements distinguish functions of the City of Oak Harbor that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the City of Oak Harbor include general government, judicial, public safety, highways and streets, economic development, senior services, and

culture and recreation. The business-type activities of the City include water, sewer, solid waste, and storm water utilities, and a municipal marina as well.

Fund Financial Statements

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 City of Oak Harbor, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

Governmental funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statement, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of the governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The City of Oak Harbor maintains 19 individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the general fund, as the general fund is considered to be a major fund. Data from the remaining governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these non-major governmental funds is provided in the form of combining statements in the city's full report, which is available upon request.

The City of Oak Harbor adopts a biennial appropriated budget for its general fund. A budgetary comparison statement has been provided for the general fund to demonstrate compliance with this budget.

Proprietary funds. The City of Oak Harbor maintains two types of proprietary funds. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The City uses enterprise funds to account for its Water, Sewer, Solid Waste, and Storm Drainage Utilities and Municipal Marina. Internal service funds are an accounting device used to accumulate and allocate costs internally among the City's various functions. The City uses internal service funds to account for its fleet of vehicles, central stores, labor pool, technology assets, and for facilities maintenance.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statements provide separate information for the Water, Sewer, Solid Waste, Storm Drainage Utilities and the Municipal Marina as all are considered, or have been designated to be major funds of the City. The internal service funds are combined into a single, aggregated presentation in the proprietary fund financial statements. Individual fund data is provided in the form of combining statements in the city's full report, which is available upon request.

Fiduciary funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary are consolidate into the government-wide financial statements because the resources of those funds are available to support the City of Oak Harbor's programs. The City does not utilize Fiduciary funds at this time.

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.

Other information. In addition to the basic financial statements and accompanying notes, required supplementary information presents a budgetary comparison schedule for the General Fund to demonstrate compliance with the budget.

Government-wide Financial Analysis

Net Assets

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the City of Oak Harbor, assets exceeded liabilities by \$115,549,959. The largest portion of the City's net assets (57.4%) reflects its investment in capital assets (land, buildings, machinery, and equipment), less related debt used to acquire those assets that is still outstanding. The City uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the City's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

Assets	Net Assets					
	Governmental Activities		Business-type Activities		Totals	
	2009	2008	2009	2008	2009	2008
Current	\$20,511,238	\$22,400,379	\$32,694,517	\$27,840,186	\$53,205,755	\$50,240,565
Capital assets	23,570,936	29,192,168	46,656,605	38,827,552	70,227,541	68,019,720
Total assets	44,082,174	51,592,547	79,351,122	66,667,738	123,433,296	118,260,285
Liabilities						
Long-term	1,698,415	1,841,667	4,269,874	4,068,947	5,968,289	5,910,614
Other	982,164	919,796	932,884	1,459,730	1,915,048	2,379,526
Total liabilities	2,680,579	2,761,463	5,202,758	5,528,677	7,883,337	8,290,140
Net Assets						
Invested in capital assets net of related debt	23,570,936	28,562,958	42,762,613	35,333,195	66,333,549	63,896,153
Restricted	6,156,440	5,530,789	11,397,043	10,846,803	17,553,483	16,377,592
Unrestricted	11,674,219	14,737,337	19,988,708	14,959,063	31,662,927	29,696,400
Total net assets	41,401,595	48,831,084	74,148,364	61,139,061	115,549,959	109,970,145

A portion of the City's net assets (15.2%) represent resources that are subject to external restrictions on how they may be used. The remaining balance of unrestricted net assets (27.4%) may be used to meet the city's ongoing obligations to citizens and creditors.

At the end of the current fiscal year, the City is able to report positive balances in all three categories of net assets, both for the government as a whole, as well as for its separate governmental and business-type activities. The same situation was true of the prior year.

Changes in Net Assets

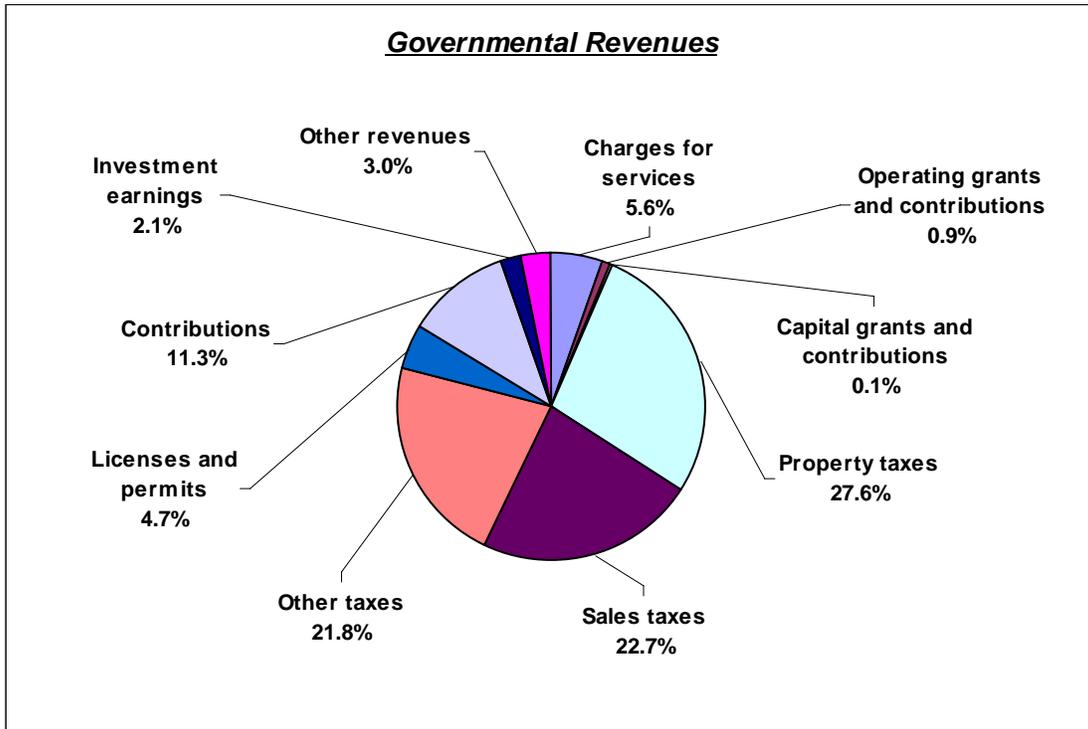
The changes in net assets table illustrates the increases or decreases in net assets of the City resulting from its operating activities. The table shows the revenues, expenses, and related changes in net assets in tabular form for the governmental activities separate from the business-type activities for 2009 and 2008.

	Changes in Net Assets					
	Governmental		Business-type		Totals	
	2009	2008	2009	2008	2009	2008
Revenues						
Program revenues						
Charges for services	\$806,610	\$1,317,035	\$14,378,114	\$13,977,073	\$15,184,724	\$15,294,108
Operating grants and contributions	127,696	84,265	30,565	38,528	158,261	122,793
Capital grants and contributions	20,240	254,418	1,236,923	889,807	1,257,163	1,144,225
General revenues						
Property taxes	3,983,435	3,680,344	-	-	3,983,435	3,680,344
Sales and use taxes	3,276,747	3,187,625	-	-	3,276,747	3,187,625
Other taxes	3,139,412	3,050,311	-	-	3,139,412	3,050,311
Other revenues	3,061,958	4,544,567	523,330	3,247,595	3,585,288	7,792,162
Total revenues	14,416,098	16,118,565	16,168,932	18,153,003	30,585,030	34,271,568
Expenses						
Governmental						
General government	2,526,182	3,710,141	-	-	2,526,182	3,710,141
Judicial	418,655	975,738	-	-	418,655	975,738
Public safety	6,643,759	6,941,977	-	-	6,643,759	6,941,977
Physical environment	179,089	955,121	-	-	179,089	955,121
Transportation	1,136,291	598,680	-	-	1,136,291	598,680
Health and human services	445,042	70,634	-	-	445,042	70,634
Economic environment	921,456	1,218,288	-	-	921,456	1,218,288
Culture and recreation	1,422,123	1,376,400	-	-	1,422,123	1,376,400
Interest on long-term debt	32,198	41,916	-	-	32,198	41,916
Other expenses	-	5,835	-	-	-	5,835
Business-type						
Water	-	-	3,426,584	3,286,649	3,426,584	3,286,649
Sewer	-	-	3,073,823	2,908,297	3,073,823	2,908,297
Solid waste	-	-	2,752,195	3,277,528	2,752,195	3,277,528
Storm drain	-	-	1,030,034	1,041,566	1,030,034	1,041,566
Marina	-	-	997,785	1,394,009	997,785	1,394,009
Total expenses	13,724,795	15,894,730	11,280,421	11,908,049	25,005,216	27,802,779
Change in net assets before transfers	691,303	223,835	4,888,511	6,244,954	5,579,814	6,468,789
Transfers	950,122	1,493,686	(950,122)	(1,417,353)	-	76,333
Change in net assets	1,641,425	1,717,521	3,938,389	4,827,601	5,579,814	6,545,122
Net assets - beginning	39,760,170	47,113,563	70,209,975	56,311,460	109,970,145	103,425,023
Net assets - ending	41,401,595	48,831,084	74,148,364	\$61,139,061	\$115,549,959	\$109,970,145

Revenues by Source

Governmental activities contributed \$1,641,425 of the total change in net assets of \$5,579,814. The increase in net assets in 2009 was slightly lower than the increase in net assets for 2008 by \$76,096. The key element of this decrease is as follows:

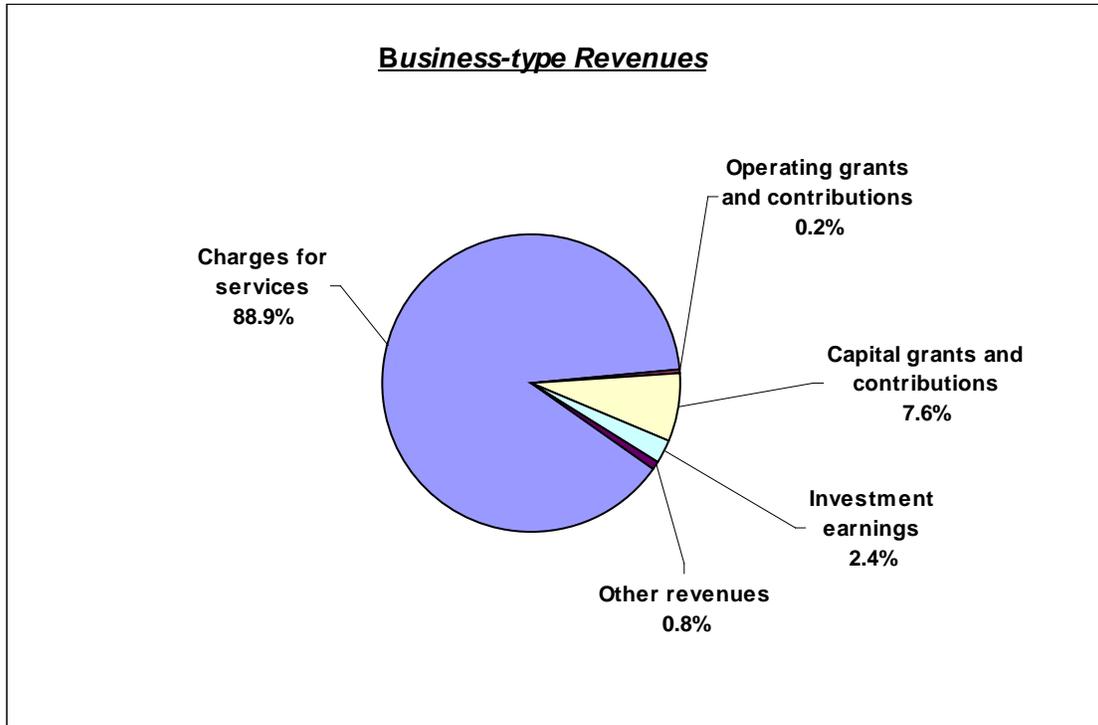
During 2009, the City changed its method of allocating internal service fund revenues and expenditures between Governmental Activities and Business-activities. The effect of this change is that less internal service fund revenue is allocated to Governmental Activities than in the previous year.



The above chart includes debt service, but excludes net transfers.

Business-type activities increased the City of Oak Harbor's net assets by \$3,938,389 or 70.6% of the total change of net assets of \$5,579,814. Business-type activities accounts for 64.2% of the City's net assets. Key reasons for this increase include:

- Deferment of a number of utility system improvements until 2010. These projects are for utility upgrades to be complete on the Oak Harbor Street Improvement project, and for the utility replacement project to occur on Pioneer Way.
- A financially secure rate structure
- The continued accumulation of system development fees, service revenue, and other funding sources for capital projects scheduled for future years.



The above chart excludes net transfers.

Financial Analysis of the City's Funds

As noted earlier, the City of Oak Harbor uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds

The focus of the City's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the City's financing requirements. In particular, unreserved fund balance may serve as a useful measure of the city's net resources available for spending at the end of a fiscal year.

As of the end of 2009, the City's governmental funds reported combined ending fund balances of \$18,019,920. Nearly all of this constitutes unreserved fund balance, which is available for spending at the city's discretion. While none of these funds are restricted by legislation or ordinance, portions of the unreserved fund balance are used to pay debt service and for other specific uses.

The general fund is the chief operating fund of the City. At the end of 2009, unreserved fund balance of the general fund was \$6,927,309. 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. The general fund unreserved fund balance represents 100.0% of total General Fund net assets.

The fund balance of the City of Oak Harbor's general fund increased by \$666,997 during 2009. Key factors include:

- An increase in utility taxes as a result of increased market participation, and the implementation of a .25% utility tax increase in the water, wastewater, and garbage funds for the purpose of funding the City's art acquisition program.
- The under expenditure of several city programs due to personnel vacancies.
- Efficiencies in labor costs via the reduction of overtime expenditures.
- Careful monitoring of expenditures and budgetary compliance.

Proprietary Funds

The City of Oak Harbor's enterprise funds are all presented as major funds for purposes of this report. As a result, all statements related to the enterprise funds are presented at the entity-wide level. The City does have Internal Service funds which are reported in the fund statements.

General Fund Budgetary Highlights

For 2009, the adopted general fund budget for expenditures, net of ending fund balance, was \$12,901,893, the final budget was \$12,606,647, and the actual expenditures were \$12,427,734. Amendments to the City budget are made for the following purposes:

- Reallocating fund resources between various line items within the General Fund
- To record the award of a \$27,000 Homeland Security Grant for the fire department.
- To adjust the budget for the move of the Engineering Department from City Hall to the Public Works Facility, and to transfer the appropriation authority for the department to Fund #510 Facility Fund.
- To carryover unexpended appropriations expiring on December 31, 2008 to the actual beginning fund balances as of January 1, 2009.
- Actual expenditures for personnel were less than budgeted due to a number of vacancies in employee positions during the year.

Actual revenues were \$689,247 higher than the final budget, or 105.6%. Actual expenditures are \$178,913 lower than final budget amounts, net of budgeted ending fund balance, or 98.6%. See below for the primary contributing factors:

- Sales taxes exceeded projections by \$170,782.
- Utility taxes exceeded projections by \$81,780.
- Cable franchise fees exceeded projections by \$118,858.
- Building permits exceeded projections by 82,204.
- Zoning and subdivision fees exceeded projections by \$62,751.
- Actual budgetary expenditures were less than projections due to conservative cost monitoring, and by the vacancy of various staff positions within the General Fund.

Capital Assets and Debt Administration

Capital Assets

The City of Oak Harbor's investment in non-current and capital assets for its governmental and business type activities as of December 31, 2009, amounts to \$70,227,541 (net of accumulated depreciation). This investment in capital assets includes land, buildings and system, improvements, machinery and equipment, and park facilities. The City has completed its inventory and analysis of its roads, highways, and bridges as capital assets of the city.

Capital assets, net of accumulated depreciation, in governmental activities decreased from \$29,192,168 2008 to \$23,570,936 primarily due to the reallocation of internal service fund capital assets from Governmental Activities to Business-type activities. This reallocation was based on a revised calculation implemented in 2009 to allocate internal service fund net assets on a different basis than the previous years. Capital assets in business-type activities increased from \$38,827,552 in 2008 to \$46,656,605. This increase is primarily due to upgrades to the City's utility infrastructure, relocation costs incurred moving the City's water line along State Route 20, donated capital infrastructure received from developers, and the same reallocation of capital assets from Governmental Activities to Business-type Activities as referred to previously.

Non-current Liabilities

At the end of 2009, the City of Oak Harbor had total non-current liabilities consisting of outstanding bonded debt, PWTF loans, and other long-term liabilities as reflected on the Statement of Net Assets, of \$5,968,289.

Economic Factors and the Next Year's Budgets and Rates

The city continues to recover from the effects of the slow economy and changes in state laws as it develops its budgets and financial plans for the future.

Slow Economy

The local economy has experienced some of the deceleration that other communities have felt since the events of September 11, 2001. On a national level, the effects of this event, combined with the economic impacts of the banking insolvencies, real estate devaluations, and declines in equity markets on a national level, the costs of energy, and the negative effects of the sub-prime market continue to be apparent. From a local perspective, sales taxes represent a significant revenue component and a barometer of the local economy. Sales tax receipts in 2009 were approximately 2.8% higher than the previous year. While this positive increase is encouraging, most of the difference is due to the large construction project in process to remodel the Oak Harbor High School. This one-time project will be substantially completed during 2009. Accordingly, it is anticipated that sales tax receipts in 2010 will be less than 2009.

The City continues to experience a moderate demand for single family housing. There remain several undeveloped parcels within the City limits that are scheduled for development over the next 24 to 36 months. The eventual development will result in increased property tax receipts, however the sales tax receipts as a result of construction will begin to decrease as the inventory of available parcels of property becomes smaller. As always, the outcome will be determined on the general economy and improved consumer confidence.

Changes in State Law

Washington has seen a wave of initiatives and anti-tax measures over the past several years. The most significant changes are the elimination of the motor vehicle excise tax, the elimination of a motor vehicle license fee and the imposition of a one-percent limit to increases in the property tax.

In 1999, the City of Oak Harbor received in excess of \$800,000 per year from the State Motor Vehicle Excise tax, representing approximately 9% of the General Fund. This tax was eliminated in 2000 by the State Legislature which enacted the change after an initiative was approved by the voters; even though

the initiative was reversed by the courts as unconstitutional. For a brief time, the state provided “back fill” money to help offset the losses to cities and counties. This amounted to about \$140,000 annually in Oak Harbor. However, the state discontinued the backfill to Oak Harbor in 2004.

In 2001 the voters approved an initiative which reduced the permitted increase in property taxes from six percent to one percent each year. The property tax laws are quite complicated and there is a provision whereby the City of Oak Harbor has “banked” past capacity. However, the various legislative bodies, including the Oak Harbor City Council are very mindful of the voter’s interests in keeping taxes and fees at a minimum.

During 2008, the State of Washington implemented the Streamlined Sales tax (SST) program of distributing sales tax receipts to local cities. Sales taxes on remote sales now are distributed to the receiving location rather than the location where the remote sale was originated. It is anticipated that the During 2009, the City received a higher allocation of sales tax receipts from this change as the mix of light manufacturing and order receiving entities is smaller in size than many communities. This increase in allocation is expected to continue in the future.

Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Finance Director, City of Oak Harbor, 865 SE Barrington Drive, Oak Harbor, WA 98277.

**City of Oak Harbor
Statement of Net Assets
December 31, 2009**

	Primary Government		
	Governmental Activities	Business-type Activities	Total
Assets			
Cash & cash equivalents	\$ 18,206,508	\$ 23,934,032	\$ 42,140,540
Receivables (net)	594,811	1,802,998	2,397,809
Internal balances	54,110	(54,110)	-
Due from other governments	911,179	10,301	921,480
Inventories	-	33,475	33,475
Prepays	-	10,674	10,674
Bond issue cost net of accumulated amortization	-	53,864	53,864
Restricted assets:			
Cash & cash equivalents	744,630	6,903,283	7,647,913
Capital assets not being depreciated:			
Land	8,476,703	1,333,347	9,810,050
Construction in progress	1,268,443	1,477,924	2,746,367
Intangible assets	13,000	-	13,000
Capital assets net of accumulated depreciation:			
Buildings and system	4,474,679	4,899,464	9,374,143
Improvements other than buildings	266,788	34,410,440	34,677,228
Machinery and equipment	1,114,643	4,535,430	5,650,073
Infrastructure	7,956,680	-	7,956,680
Total assets	\$ 44,082,174	\$ 79,351,122	\$ 123,433,296
Liabilities			
Accounts payable	\$ 414,382	\$ 698,468	\$ 1,112,850
Accrued interest payable	-	48,197	48,197
Other current liabilities	195,260	160,615	355,875
Deferred revenue	372,522	25,604	398,126
Noncurrent liabilities:			
Due within one year:			
Compensated absences	432,338	122,289	554,627
Other long-term liabilities	-	55,905	55,905
Bonds payable, net	287,912	480,000	767,912
Due in more than one year:			
Compensated absences	648,508	183,436	831,944
Other long-term liabilities	254,672	868,685	1,123,357
Bonds payable, net	74,985	2,559,559	2,634,544
Total liabilities	2,680,579	5,202,758	7,883,337
Net Assets			
Invested in capital assets net of related debt	23,570,936	42,762,613	66,333,549
Restricted for:			-
Capital projects	6,156,440	10,443,690	16,600,130
Debt service	-	953,353	953,353
Unrestricted	11,674,219	19,988,708	31,662,927
Total net assets	\$ 41,401,595	\$ 74,148,364	\$ 115,549,959

The accompanying notes are an integral part of this statement.

**City of Oak Harbor
Statement of Activities
For the Year Ended December 31, 2009**

Function/Program	Program Revenues			Net (Expense) Revenue and Changes in Net Assets		
	Expenses	Operating		Governmental Activities	Primary Government	
		Charges for Services	Grants and Contributions		Capital Grants and Contributions	Business-type Activities
Primary government						
Governmental activities:						
General government	\$ 2,526,182	\$ 96,700	\$ -	\$ (2,429,482)	\$ -	(2,429,482)
Judicial	418,655	-	-	(418,655)	-	(418,655)
Public safety	6,643,759	56,570	91,470	(6,495,719)	-	(6,495,719)
Physical environment	179,089	15	-	(179,074)	-	(179,074)
Transportation	1,136,291	67,062	-	(1,034,052)	-	(1,034,052)
Health and human services	445,042	189,363	1,726	(253,953)	-	(253,953)
Economic environment	921,456	184,751	34,500	(702,205)	-	(702,205)
Culture and recreation	1,422,123	212,149	-	(1,224,911)	-	(1,224,911)
Interest on long-term debt	32,198	-	-	(32,198)	-	(32,198)
Total governmental activities	13,724,795	806,610	127,696	(12,770,249)	-	(12,770,249)
Business-type activities:						
Water	3,426,584	4,451,161	-	-	1,406,245	1,406,245
Sewer	3,073,823	4,320,182	3,108	-	1,840,560	1,840,560
Solid waste	2,752,195	3,125,516	-	-	373,321	373,321
Storm drain	1,030,034	1,265,842	25,004	-	483,784	483,784
Marina	997,785	1,215,413	2,453	-	261,271	261,271
Total business-type activities	11,280,421	14,378,114	30,565	1,236,923	4,365,181	4,365,181
Total primary government	\$ 25,005,216	\$ 15,184,724	\$ 158,261	(12,770,249)	4,365,181	(8,405,068)
General revenues:						
Property taxes				3,983,435	-	3,983,435
Sales and use taxes				3,276,747	-	3,276,747
Business, occupancy and other taxes				3,139,412	-	3,139,412
Licenses and permits				684,730	-	684,730
Grants and other contributions						
not restricted to specific programs				1,629,626	-	1,629,626
Unrestricted investment earnings				308,450	391,616	700,066
Miscellaneous				421,883	139,378	561,261
Gain (loss) on sale of assets				17,269	(7,664)	9,605
Transfers				950,122	(950,122)	-
Total general revenues and transfers				14,411,674	(426,792)	13,984,882
Change in net assets				1,641,425	3,938,389	5,579,814
Net assets - beginning				39,760,170	70,209,975	109,970,145
Net assets - ending				\$ 41,401,595	\$ 74,148,364	\$ 115,549,959

The accompanying notes are an integral part of this statement.

**City of Oak Harbor
Balance Sheet
Governmental Funds
December 31, 2009**

	General Fund	Other Governmental Funds	Total Governmental Funds
Assets			
Cash & cash equivalents	\$ 7,322,564	\$ 10,883,944	\$ 18,206,508
Accounts receivables (net)	438,600	156,211	594,811
Due from other funds	43,540	41	43,581
Due from other governments	536	-	536
Restricted cash	50,800	400,928	451,728
Total assets	\$ 7,856,040	\$ 11,441,124	\$ 19,297,164
Liabilities and Fund Balances			
Liabilities			
Accounts payable	\$ 183,683	\$ 87,244	\$ 270,927
Deposits	125,935	69,325	195,260
Due to other funds	41	6,156	6,197
Deferred revenue	216,633	155,889	372,522
Compensated absences	402,439	29,899	432,338
Total liabilities	928,731	348,513	1,277,244
Fund balances			
Unreserved, reported in:			
General fund	6,927,309	-	6,927,309
Special revenue funds	-	4,936,171	4,936,171
Capital project funds	-	6,156,440	6,156,440
Total fund balance	6,927,309	11,092,611	18,019,920
Total liabilities and fund balances	\$ 7,856,040	\$ 11,441,124	\$ 19,297,164

The accompanying notes are an integral part of this statement.

**City of Oak Harbor
Reconciliation of the Balance Sheet
of the Governmental Funds
to the Statement of Net Assets
December 31, 2009**

Total fund balances—governmental funds \$ 18,019,920

Amounts reported for governmental activities in the statement of net assets are different because:

Capital assets used in governmental activities are not financial resources and are not reported in funds:

Historical cost of assets not being depreciated	\$ 9,758,146	
Historical cost of assets being depreciated	36,495,209	
Accumulated depreciation	<u>(23,006,389)</u>	23,246,966

Long-term assets not available to pay for current period expenditures and therefore deferred. 910,643

Internal service funds are used by management to charge the costs of fleet management, shop facilities and information systems to individual funds. The assets and liabilities of the internal service funds are included in the governmental activities in the statement of net assets. 603,079

Some liabilities are not due and payable in the current period and therefore are not reported in the funds, including:

Accounts payable	\$ (112,936)	
Compensated absences	(648,508)	
Bonds and interest payable	(362,897)	
Other post-employment benefit liabilities	<u>(254,672)</u>	(1,379,013)

Net assets of governmental activities \$ 41,401,595

The accompanying notes are an integral part of this statement.

City of Oak Harbor
Statement of Revenues, Expenditures, and Changes in Fund Balances
Governmental Funds
For the Year Ended December 31, 2009

	General Fund	Other Governmental Funds	Total Governmental Funds
Revenues			
Taxes	\$ 9,686,168	\$ 658,624	\$ 10,344,792
Licenses and permits	679,612	5,118	684,730
Intergovernmental	400,536	1,369,437	1,769,973
Charges for services	507,462	299,148	806,610
Fines and forfeits	172,274	-	172,274
Interest revenue	131,807	176,643	308,450
Miscellaneous	128,020	121,747	249,767
Total revenues	11,705,879	2,630,717	14,336,596
Expenditures			
Current:			
General government	2,507,436	-	2,507,436
Judicial	438,934	-	438,934
Public safety	6,357,253	-	6,357,253
Physical environment	192,538	-	192,538
Transportation	9,377	922,226	931,603
Health and human services	5,493	434,449	439,942
Economic environment	920,057	-	920,057
Culture and recreation	1,130,987	168,427	1,299,414
Debt Service:			
Principal	-	266,313	266,313
Interest	-	32,198	32,198
Capital outlay	126,642	668,114	794,756
Total expenditures	11,688,717	2,491,727	14,180,444
Excess (deficiency) of revenues over (under) expenditures	17,162	138,990	156,152
Other Financing Sources (Uses)			
Transfers in	1,374,057	619,004	1,993,061
Transfers out	(739,017)	(303,922)	(1,042,939)
Sale of capital assets	14,029	3,240	17,269
Other sources	766	216	982
Total other financing sources (uses)	649,835	318,538	968,373
Net change in fund balances	666,997	457,528	1,124,525
Fund balances - beginning	6,260,312	10,635,083	16,895,395
Fund balances - ending	\$ 6,927,309	\$ 11,092,611	\$ 18,019,920

The accompanying notes are an integral part of this statement.

City of Oak Harbor
Reconciliation of the Statement of Revenues
Expenditures, and Changes in Fund Balances of the Governmental Funds
to the Statement of Activities
For the Year Ended December 31, 2009

Net change in fund balances—governmental funds \$ 1,124,525

Amounts reported for governmental activities in the statement of activities are different because:

Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as outlays exceeded depreciation in the current period:

Capital outlay	\$ 794,756	
Depreciation	<u>(888,302)</u>	(93,546)

Donated capital increases net assets in the statement of activities, but does not appear in the governmental funds because it is not a financial resource. 348,048

Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds. 61,251

Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets and does not effect the statement of activities. 266,313

Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds, including:

Change in accounts payable	\$ 58,508	
Change in compensated absences	(59,709)	
Other post-employment benefit expense	<u>(131,383)</u>	(132,584)

Internal service funds are used by management to charge the costs of fleet management, shop facilities and information systems to individual funds. The net revenues and expenses of the internal service funds are reported with governmental activities in the statement of activities. 67,418

Change in net assets of governmental activities \$ 1,641,425

The accompanying notes are an integral part of this statement.

City of Oak Harbor
Statement of Revenues, Expenditures, and Changes in Fund Balances — Budget and Actual
General Fund
For the Year Ended December 31, 2009

	Budgeted Amounts		Actual Amounts	Total Variance with Final Budget
	Original	Final		
Revenues				
Taxes	\$ 9,456,516	\$ 9,456,516	\$ 9,686,168	\$ 229,652
Licenses and permits	475,550	475,550	679,612	204,062
Intergovernmental	423,000	450,000	400,536	(49,464)
Charges for services	453,600	453,600	507,462	53,862
Fines and forfeits	168,000	168,000	172,274	4,274
Interest revenue	156,000	156,000	131,807	(24,193)
Miscellaneous	66,000	66,000	128,020	62,020
Total revenues	11,198,666	11,225,666	11,705,879	480,213
Expenditures				
Current:				
General government	2,405,236	2,504,496	2,507,436	(2,940)
Judicial	419,250	419,250	438,934	(19,684)
Public safety	6,562,634	6,598,114	6,357,253	240,861
Physical environment	983,773	244,654	192,538	52,116
Transportation	-	-	9,377	(9,377)
Health and human services	6,000	6,000	5,493	507
Economic environment	780,305	997,437	920,057	77,380
Culture and recreation	1,114,340	1,114,340	1,130,987	(16,647)
Capital outlay	140,360	162,360	126,642	35,718
Total expenditures	12,411,898	12,046,651	11,688,717	357,934
Excess (deficiency) of revenues over (under) expenditures	(1,213,232)	(820,985)	17,162	838,147
Other Financing Sources (Uses)				
Transfers in	1,782,060	1,179,818	1,374,057	194,239
Transfers out	(489,995)	(559,996)	(739,017)	(179,021)
Sale of capital assets	-	-	14,029	14,029
Other sources	-	-	766	766
Total other financing sources (uses)	1,292,065	619,822	649,835	30,013
Net change in fund balances	78,833	(201,163)	666,997	868,160
Fund balances - beginning	2,686,515	5,204,064	6,260,312	1,056,248
Fund balances - ending	\$ 2,765,348	\$ 5,002,901	\$ 6,927,309	\$ 1,924,408

The accompanying notes are an integral part of this statement.

City of Oak Harbor
Statement of Net Assets
Proprietary Funds
December 31, 2009

	Business-Type Activities						Total	Governmental Activities
	Water and Water Reserve Fund	Sewer and Sewer Reserve Fund	Solid Waste and Solid Waste Reserve Fund	Storm Drain and Storm Drain Reserve Fund	Marina and Marina Reserve Fund	Internal Service Funds		
Assets								
Current assets:								
Cash & cash equivalents	\$ 8,955,273	\$ 10,424,583	\$ 2,494,887	\$ 737,843	\$ 1,215,504	\$ 23,828,090	\$ 105,942	
Accounts receivables (net)	531,891	585,409	438,211	208,254	39,233	1,802,998	-	
Due from other governments	-	-	-	1,606	8,695	10,301	-	
Inventories	-	-	-	-	24,552	24,552	8,923	
Prepays	-	4,613	-	-	6,061	10,674	-	
Bond issue cost net of accumulated amortization	-	53,864	-	-	-	53,864	-	
Total current assets	9,487,164	11,068,469	2,933,098	947,703	1,294,045	25,730,479	114,865	
Noncurrent assets:								
Restricted cash	452,652	593,123	70,857	48,000	67,403	1,232,035	5,964,150	
Capital assets net of accumulated depreciation:								
Land	99,589	4,200	201,810	-	1,027,748	1,333,347	-	
Construction in progress	121,673	912,641	-	1,924	377,836	1,414,074	63,850	
Buildings and system	243,892	625,134	-	-	489,942	1,358,968	3,540,496	
Improvements other than buildings	14,397,774	17,666,895	114,395	1,372,448	816,594	34,368,106	309,122	
Machinery and equipment	853,563	1,536,301	35,101	16,013	12,146	2,453,124	2,139,488	
Total noncurrent assets	16,169,143	21,338,294	422,163	1,438,385	2,791,669	42,159,654	12,017,106	
Total assets	\$ 25,656,307	\$ 32,406,763	\$ 3,355,261	\$ 2,386,088	\$ 4,085,714	\$ 67,890,133	\$ 12,131,971	

The accompanying notes are an integral part of this statement.

City of Oak Harbor
Statement of Net Assets
Proprietary Funds
December 31, 2009
(Continued)

	Business-Type Activities							Governmental Activities
	Water and Water Reserve Fund	Sewer and Sewer Reserve Fund	Solid Waste and Solid Waste Reserve Fund	Storm Drain and Storm Drain Reserve Fund	Marina and Marina Reserve Fund	Total	Internal Service Funds	
Liabilities								
Current liabilities:								
Accounts payable	\$ 365,867	\$ 96,869	\$ 104,857	\$ 12,296	\$ 69,927	\$ 649,816	\$ 79,171	
Deposits	10,494	134	700	48,000	94,121	153,449	-	
Retainage	-	-	-	-	7,166	7,166	-	
Due to other funds	9,868	13,972	5,736	1,636	2,901	34,113	3,271	
Interest payable	2,136	46,061	-	-	-	48,197	-	
Deferred revenue	14,872	10,732	-	-	-	25,604	-	
Compensated absences	24,386	6,976	13,845	16,451	3,239	64,897	57,392	
Due to other governments	55,905	-	-	-	-	55,905	-	
Bonds payable, net	-	480,000	-	-	-	480,000	-	
Total current liabilities	483,528	654,744	125,138	78,383	177,354	1,519,147	139,834	
Noncurrent liabilities:								
Compensated absences	36,580	10,465	20,768	24,677	4,858	97,348	86,088	
Due to other governments	798,528	-	-	-	-	798,528	-	
Bonds payable, net	-	2,559,559	-	-	-	2,559,559	-	
Landfill closure	-	-	70,157	-	-	70,157	-	
Total noncurrent liabilities	835,108	2,570,024	90,925	24,677	4,858	3,525,592	86,088	
Total liabilities	1,318,636	3,224,768	216,063	103,060	182,212	5,044,739	225,922	
Net Assets								
Invested in capital assets								
net of related debt	14,862,058	17,705,612	351,306	1,390,385	2,724,266	37,033,627	6,052,956	
Restricted for:								
Capital projects	5,304,546	4,638,609	115,514	385,021	-	10,443,690	-	
Debt service	360,230	593,123	-	-	-	953,353	-	
Unrestricted	3,810,837	6,244,651	2,672,378	507,622	1,179,236	14,414,724	5,853,093	
Total net assets	\$ 24,337,671	\$ 29,181,995	\$ 3,139,198	\$ 2,283,028	\$ 3,903,502	\$ 62,845,394	\$ 11,906,049	

Amounts reported for business-type activities in the statement of net assets are different because:
Adjustments to reflect consolidation of internal service fund activities related to enterprise funds.
Net assets of business type activities

11,302,970
\$ 74,148,364

The accompanying notes are an integral part of this statement.

City of Oak Harbor
Statement of Revenues, Expenses, and Changes in Fund Net Assets
Proprietary Funds
For the Year Ended December 31, 2009

	Business-Type Activities						Governmental Activities
	Water and Water Reserve Fund	Sewer and Sewer Reserve Fund	Solid Waste Reserve Fund	Storm Drain Reserve Fund	Marina and Marina Reserve Fund	Total	
Operating Revenues							
Charges for services	\$ 4,227,518	\$ 4,212,216	\$ 3,124,909	\$ 1,262,263	\$ 368,510	\$ 13,195,416	\$ 1,647,928
System development revenue	218,753	106,759	-	-	-	325,512	-
Other operating revenues	4,476	754	-	3,334	846,895	855,459	1,912,830
Total operating revenues	4,450,747	4,319,729	3,124,909	1,265,597	1,215,405	14,376,387	3,560,758
Operating Expenses							
Cost of sales and service	1,705,344	803,091	491,959	407,379	545,521	3,953,294	1,871,832
Contractual services	50,718	58,922	27,702	151,710	14,231	303,283	205,521
Utilities	18,093	188,758	1,067,058	2,323	83,304	1,359,536	66,451
Taxes	471,483	341,881	346,514	94,741	-	1,254,619	-
Repairs and maintenance	77,131	85,554	357,590	58,985	34,679	613,939	124,529
Other operating expenses	418,861	516,784	394,187	211,443	85,541	1,626,816	520,961
Insurance claims and expenses	33,684	49,927	23,384	8,521	25,100	140,616	25,707
Depreciation	664,917	891,797	70,366	105,638	209,750	1,942,468	601,056
Total operating expenses	3,440,231	2,936,714	2,778,760	1,040,740	998,126	11,194,571	3,416,057
Operating income (loss)	1,010,516	1,383,015	346,149	224,857	217,279	3,181,816	144,701
Nonoperating Revenues (Expenses)							
Interest revenue	95,338	179,017	55,718	16,306	21,211	367,590	24,026
External subsidiaries	-	481,416	-	25,004	43,643	550,063	-
Other nonoperating revenues	50,389	-	6,377	50,364	12,586	119,716	19,662
Gain (loss) on sale of fixed assets	-	-	-	-	-	-	(7,664)
Interest expense	(4,464)	(156,942)	-	-	-	(161,406)	-
Total nonoperating revenues (expenses)	141,263	503,491	62,095	91,674	77,440	875,963	36,024
Net income (loss) before contributions and transfers	1,151,779	1,886,506	408,244	316,531	294,719	4,057,779	180,725
Capital contributions	381,668	112,785	-	222,972	-	717,425	-
Transfers in	24,000	-	-	25,000	25,000	74,000	386,946
Transfers out	(408,050)	(342,238)	(229,672)	(238,150)	(115,927)	(1,334,037)	(77,031)
Change in net assets	1,149,397	1,657,053	178,572	326,353	203,792	3,515,167	490,640
Net assets - beginning	23,188,274	27,524,942	2,960,626	1,956,675	3,699,710	59,330,227	11,415,409
Net assets - ending	\$ 24,337,671	\$ 29,181,995	\$ 3,139,198	\$ 2,283,028	\$ 3,903,502	\$ 62,845,394	\$ 11,906,049

Amounts reported for business-type activities in the statement of activities are different because:
Change in net assets \$ 3,515,167
Adjustments to reflect consolidation of internal service fund activities related to enterprise funds. 423,222
Change in net assets of business-type activities \$ 3,938,389

The accompanying notes are an integral part of this statement.

City of Oak Harbor
Statement of Cash Flows
Proprietary Funds
For the Year Ended December 31, 2009

	Business-Type Activities										Governmental Activities	
	Water and Water		Sewer and Sewer		Solid Waste Reserve Fund		Storm Drain and Storm Drain		Marina and Marina			Total
	Reserve Fund	Reserve Fund	Reserve Fund	Reserve Fund	Reserve Fund	Reserve Fund	Reserve Fund	Reserve Fund	Reserve Fund	Internal Service Funds		
Cash Flows From												
Operating Activities												
Receipts from customers and users	\$ 4,474,969	\$ 4,333,447	\$ 3,111,524	\$ 1,243,223	\$ 1,205,642	\$ 14,368,805	\$	\$	\$	\$	\$	\$ 1,727
Receipts from interfund services provided	-	-	-	-	-	-	-	-	-	-	-	3,559,031
Payments to suppliers	(1,888,709)	(1,026,096)	(1,689,047)	(461,320)	(510,302)	(5,575,474)	-	-	-	-	-	(1,248,854)
Payments to employees	(442,476)	(497,257)	(326,282)	(285,719)	(241,577)	(1,793,311)	-	-	-	-	-	(935,994)
Payments for interfund services used	(403,291)	(512,052)	(721,333)	(239,367)	(15,299)	(1,891,342)	-	-	-	-	-	(565,828)
Net cash provided by operating activities	1,740,493	2,298,042	374,862	256,817	438,464	5,108,678	-	-	-	-	-	810,082
Cash Flows From Noncapital Financing Activities												
Transfers from other funds	24,000	-	-	25,000	25,000	74,000	-	-	-	-	-	386,946
Transfers to other funds	(408,050)	(342,238)	(229,672)	(238,150)	(115,927)	(1,334,037)	-	-	-	-	-	(77,031)
Receipts from miscellaneous revenues	50,389	3,109	6,376	75,368	15,039	150,281	-	-	-	-	-	19,662
Net cash provided (used) by noncapital financing activities	(333,661)	(339,129)	(223,296)	(137,782)	(75,888)	(1,109,756)	-	-	-	-	-	329,577
Cash Flows From Capital and Related Financing Activities												
Principal paid on capital debt	(84,552)	(454,798)	-	-	-	(539,350)	-	-	-	-	-	-
Interest paid on capital debt	(4,695)	(161,839)	-	-	-	(166,534)	-	-	-	-	-	-
Purchases of capital assets	(1,789,871)	(1,178,459)	-	(1,924)	(354,855)	(3,325,109)	-	-	-	-	-	(454,308)
Proceeds from sales of capital assets	-	-	-	-	-	-	-	-	-	-	-	(7,664)
Capital grants and contributions	-	478,307	-	-	41,190	519,497	-	-	-	-	-	-
Net cash used by capital and related financing activities	(1,879,118)	(1,316,789)	-	(1,924)	(313,665)	(3,511,496)	-	-	-	-	-	(461,972)

The accompanying notes are an integral part of this statement.

City of Oak Harbor
Statement of Cash Flows
Proprietary Funds
For the Year Ended December 31, 2009
(Continued)

	Business-Type Activities				Total	Governmental Activities
	Water and Water Reserve Fund	Sewer and Sewer Reserve Fund	Solid Waste Solid Waste Reserve Fund	Storm Drain and Storm Drain Reserve Fund		
Cash Flows From						
Investing Activities						
Interest and dividends received	95,338	179,017	55,718	16,306	21,211	24,026
Net cash provided by investing activities	95,338	179,017	55,718	16,306	21,211	24,026
Net increase (decrease) in cash and cash equivalents	(376,948)	821,141	207,284	133,417	70,122	701,713
Cash and cash equivalents - beginning of year	9,784,873	10,196,565	2,358,460	652,426	1,212,785	5,368,379
Cash and cash equivalents - end of year	\$ 9,407,925	\$ 11,017,706	\$ 2,565,744	\$ 785,843	\$ 1,282,907	\$ 6,070,092
Reconciliation of Operating Income to Net Cash Provided (Used) by Operating Activities:						
Operating income	\$ 1,010,516	\$ 1,383,015	\$ 346,149	\$ 224,857	\$ 217,279	\$ 144,701
Adjustments to reconcile operating income to net cash provided by operating activities:						
Depreciation expense	664,917	891,797	70,366	105,638	209,750	601,056
(Increase) decrease in accounts receivable	15,041	7,892	(13,385)	(20,768)	(10,158)	(21,378)
(Increase) decrease in due from other governments	-	-	-	(1,606)	(1,693)	(3,299)
(Increase) decrease in inventories	-	-	-	-	1,978	1,978
(Increase) decrease in prepaids	-	(322)	-	-	(460)	(782)
Increase (decrease) in accounts payable	48,340	17,007	(32,104)	(12,947)	17,663	33,959
Increase (decrease) in deposits	6,448	134	-	-	2,088	8,670
Increase (decrease) in retainage	(11,316)	(8,802)	-	-	7,166	(12,952)
Increase (decrease) in due to other funds	371	326	1,630	(19,122)	(4,678)	(21,473)
Increase (decrease) in deferred revenue	2,733	5,692	-	-	-	8,425
Increase (decrease) in compensated absences payable	3,443	1,303	2,206	(19,235)	(471)	35,642
Net cash provided by operating activities	\$ 1,740,493	\$ 2,298,042	\$ 374,862	\$ 256,817	\$ 438,464	\$ 810,082
Noncash Activities:						
Contributions of capital Assets from developer construction	\$ 381,668	\$ 112,785	\$ -	\$ 222,972	\$ -	\$ 717,425

The accompanying notes are an integral part of this statement.

Notes to the Financial Statements

Note 1 – Summary of Significant Accounting Policies

The financial statements of the City of Oak Harbor have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governmental units. GAAP statements include all relevant Governmental Accounting Standards Board (GASB) pronouncements. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The financial statements have incorporated all applicable GASB pronouncements as well as Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on accounting procedures issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

A. Reporting Entity

The City of Oak Harbor was incorporated on May 14, 1915 and operates under the laws of the state of Washington applicable to an optional code city with a Mayor-Council form of government. The governing body consists of eight elected officials, the mayor and seven council members. The mayor and council members are each elected to serve a four-year term. The City Manager administers policies and coordinates the activities of the City. The heads of the various departments, formed to provide various services, are under the direct supervision of the City Manager.

The City's Annual Financial Report includes all funds and organizations that are controlled by or dependent on the City. Control by the City was determined on the basis of budget adoption, taxing authority, and resource allocation criteria. Dependence on the City was determined by the City's obligation to redeem the organization's debts, to finance the organization's deficits, and the extent to which subsidies from the City constitute a major portion of the organization's total resources. Applying these criteria, as outlined in Governmental Accounting Standards Board (GASB) Statement 1, the combined financial statements do not include the financial position or results of operation for:

The Oak Harbor Library -

Although the City has a contract with the Sno-Isle Library System that obligates the City to provide a portion of the insurance and intergovernmental charges for services, the Sno-Isle Library is a separate municipal corporation and is not a component unit of the City.

North Whidbey Park District -

The North Whidbey Park and Recreation District is a separate corporation with an independently elected Board of Directors.

B. Government-wide and Fund Financial Statements

Basic financial statements are presented at both the government-wide and fund financial level. Both levels of statements categorize primary activities as either governmental or business-type.

Government-wide financial statements display information about the reporting government as a whole. These statements focus on the sustainability of the City as an entity and the change in aggregate financial position resulting from the activities of the fiscal period. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. These aggregated statements consist of the Statement of Net Assets and the Statement of Activities.

The Statement of Activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services or privileges provided by a given function or

segment, and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

Fund financial statements display information at the individual fund level. Each fund is considered to be a separate accounting entity. Funds are classified and summarized as governmental, proprietary, and fiduciary even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements. Non-major funds are consolidated into a single column within each fund type in the financial section of the basic financial statements and are detailed in the supplemental information.

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule include charges between the City's business-type activities/enterprise funds, as well as some special revenue funds, and the General Fund. The City allocates charges as reimbursement for services provided by the General Fund in support of those functions based on levels of service provided. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

Basis of Presentation

Financial transactions of the City are recorded in individual funds. Each fund is accounted for by providing a separate set of self-balancing accounts that comprises its assets, liabilities, reserves, fund equity, revenues and expenses/expenditures. The various funds are reported by generic classification within the financial statements.

The GASB 34 model sets forth minimum criteria (percentage of the assets, liabilities, revenues or expenditures/expenses of either fund category or the governmental and enterprise combined) for the determination of major funds. The City reports the General Fund and all Proprietary funds as major funds. Non-major funds are combined in a column in the fund financial statements.

General Fund

This is the City's primary operating fund. It accounts for all the financial operations of the City except those that are required to be accounted for in another fund. Principal sources of revenue are property taxes, licenses and permits, state and county shared revenues and charges for administrative services from other funds. Primary expenditures are for general government, police and fire protection and culture and recreation.

Additionally, the City reports non-major funds within the governmental fund type. These funds account for revenues derived from specific taxes, grants, or other sources that are designated to finance particular activities of the City.

- Special Revenue funds are used to account for the proceeds of specific revenue sources that are legally restricted to expenditures for specified purposes.
- Debt Service funds account for the accumulation of resources to pay principal, interest and related costs on (certain) general long-term (bonded) debt.
- Capital Projects funds account for financial resources used for the acquisition or construction of major capital facilities (other than those financed by Business or Proprietary Funds).

The City's Special Revenue funds include the following entities:

The *Street fund #101* receives State-shared unrestricted gasoline tax revenues and Capron funds. Capron funds are State-shared revenues comprised of gasoline taxes and motor vehicle license fees. Island and San Juan Counties and municipalities within these counties are the only recipients of Capron funds. Revenues are used for maintenance of the City streets.

The *Arterial Street fund #104* receives State-shared restricted gasoline tax revenues and State grants for capital improvements to the City's arterial street system.

The *Transportation Capital Improvement fund #105* collects revenues on development activity and grants to be used for expenditures on improvements to public streets and roads.

The *Paths & Trails fund #106* accounts for ½ of 1% of the Motor Vehicle Fuel Tax. These taxes are dedicated for the construction of pedestrian/bicycle paths and trails within the City.

The *Cumulative Street Reserve fund #110* reserves matching funds for grant requirements and as a contingency reserve for unanticipated expenditures.

The *Arts Acquisition and Maintenance fund #115* collects ¼% of the 6¼% utility tax to foster the creative arts in the City.

The *Civic Improvement (2%) fund #116* receives hotel/motel tax revenues for expenditure on the promotion of tourism. The City receives both the basic 2% and the additional 2% lodging taxes.

The *Park Improvement - Neighborhood Parks fund #125* receives revenue from developers for constructing and maintaining new and established neighborhood parks.

The *Park Improvement - Community Parks fund #126* receives revenue from developers for constructing and maintaining new and established larger scale community parks.

The *Senior Center fund #129* receives participant fees, grant revenues, and contributions from The City's General Fund and Island County for expenditures associated with providing services and activities for the senior citizens in Oak Harbor and Island County.

The City's Debt Service funds include the following accounting entities:

1996 \$2,680,000 Unlimited Tax General Obligation Refunding Bond - Public Safety and Fire Station fund #201 accounts for the advance refunding of the callable portion of the City's 1987 \$1,065,000 G.O. Bond and advance refunding of the City's 1991 \$2,672,000 G.O. Bond.

2008 \$192,000 LOCAL Bond - Fire Equipment fund #230 accounts for the debt service payment on the financing for two new fire engines.

The City's Capital Projects funds include the following entities:

The *Cumulative Reserve 1st ¼% Real Estate Excise Tax fund #311* collects the first ¼% excise tax on the sales price from the exchange of all real estate. These funds are deposited into this fund and must be used for capital-type projects necessary to implement Growth Management Act-related improvements.

The *Cumulative Reserve 2nd ¼% Real Estate Excise Tax fund #312* collects the second ¼% excise tax on the sales price on the exchange of all real estate. These funds are deposited into this fund and must be used for capital projects identified in the City's Capital Facilities Plan.

The *Construction – Municipal Pier Project fund #320* is one of the City's Capital Projects funds. This fund accounts for the construction activity related to the Municipal Pier Project.

The *Waterfront Redevelopment fund #325* receives funding from various grant, lodging tax, and subsidy sources to be used in the redevelopment of Windjammer Park project.

The *Scenic Heights LID fund #361* is another of the City's Capital Projects Funds. This fund accounts for the financial activity related to the Scenic Heights LID project.

The *2004 Sewer Bond Construction fund #362* is for the purpose of accumulating bond proceeds and other funding sources to remove sludge from and repair damage to the City's Seaplane Base sewer lagoon. In addition, this fund will be used to account for various sewer fund related capital construction projects.

The *Bayshore LID fund #2007-1 #363* accounts for the financial activity related to Bayshore LID project.

Proprietary Funds

The City electively reports all of its five enterprise funds as major funds for specific community focus. These funds are used to account for the acquisition, operation, and maintenance of water, sewer, solid waste, storm drain, and marina facilities.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the City's five enterprise funds are collected primarily through user charges. Operating expenses for enterprise funds and internal service funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

- *Enterprise funds* operate in a manner similar to private business enterprises where the intent is to provide goods or services to the general public and be reimbursed primarily through user charges. An enterprise fund may also be established when the governing body decides that periodic determination of net income is needed.
- *Internal Service funds* account for operations that provide goods or services to other departments or funds of the city on a cost-reimbursement basis.

The City reports the following enterprise funds:

The *Water fund #401 and Water Cumulative Reserve fund #411* accounts for the operations and capital planning of the City-owned water utility. The water department maintains three storage tanks, approximately 99 miles of water mains, three booster pumps and associated appurtenances. The distribution system serves the City of Oak Harbor and supplies water to the U.S. Naval Air Station at Whidbey Island.

The *Sewer fund #402 and Sewer Cumulative Reserve fund #412* accounts for the operations and capital planning of the City-owned sanitary sewer utility. The City's sewer treatment plant and sewer treatment lagoons provide secondary treatment. The sewer department maintains approximately 69 miles of sanitary sewer mains, 10 remote lift stations and associated appurtenances. The collection and treatment system serves the City of Oak Harbor and a portion of the U.S. Naval Air Station at Whidbey Island.

The *Solid Waste fund #403 and Solid Waste Cumulative Reserve fund #413* accounts for the operations of the City-owned solid waste utility. The solid waste utility provides full service solid waste, recycling and yard waste. This utility serves the City of Oak Harbor.

The *Storm Drain fund #404 and Storm Drain Cumulative Reserve fund #414* accounts for the operations and capital planning of the City-owned storm drain utility. The storm drain utility consists of 10 City-owned detention facilities and control structures and maintains approximately 47 miles of storm drain pipe, roadside ditches and bio-swales. This utility serves the City of Oak Harbor.

The *Marina fund #410 and Marina Cumulative Reserve fund #420* accounts for the operations of the City-owned Marina. This full-service marina has moorage berths, dry storage sheds and dry landing storage. Other services provided are: temporary moorage, electricity, fuel, boat dolly, grid and launcher.

Additionally, the City reports its four internal service funds that provide goods and services to other departments or agencies of the City on a cost-reimbursement basis.

The *Equipment Repair fund #501* accounts for the motor-pool operations of the City. Maintenance, operation, and depreciation costs are charged to each user department on a monthly basis.

The *Equipment Replacement fund #502* accumulates funds for future purchases of vehicles and equipment. Cash reserves or "sinking funds" are established to fully fund vehicle and major equipment needs at the time of purchase.

The *Technology fund #505* accounts for the purchase and acquisition of technologically oriented equipment such as computers and other technical equipment.

The *Shop Facility fund #510* accounts for the cost of operating the Public Works Facility Campus and supervision of the various Public Works divisions. The Public Works Campus was constructed following the issuance of a long-term bond. Each division that is housed at the facility is charged space rent, with the annual proceeds used to pay maintenance, overhead, and the annual debt service on the construction bonds.

The City does not currently have Trust or Agency funds.

C. Measurement Focus and Basis of Accounting

Measurement focus is a term used to describe *which* transactions are recorded within the various financial statements. Basis of accounting refers to *when* transactions are recorded regardless of the measurement focus.

The Government-wide Financial Statements and the Proprietary Funds Financial Statements are presented on a *full accrual* basis of accounting with an *economic resource* measurement focus. An economic resource focus concentrates on an entity or fund's net assets. All transactions and events that affect the total economic resources (net assets) during the period are reported. An economic resources measurement focus is inextricably connected with full accrual accounting. Under the full accrual basis of accounting, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of the timing of related cash inflows and outflows.

Governmental Funds Financial Statements are presented on a *modified accrual* basis of accounting with a *current financial resource* measurement focus. This measurement focus concentrates on the fund's resources available for spending in the near future. Only transactions and events affecting the fund's current financial resources during the period are reported. Similar to the connection between an economic resource measurement focus and full accrual accounting, a current financial resource measurement focus is inseparable from a modified accrual basis of accounting. Under modified accrual accounting, revenues are recognized as soon as they are both measurable and available. Revenues are considered to be *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. BARS allows for the recognition of revenues to no more than 60 days however, since the City is not always able to obtain timely information to estimate the accrued amounts it chooses not to accrue taxes received in January or February in order to remain consistent with prior years. Expenditures generally are recorded when a liability is incurred, as under accrual accounting.

A deferred revenue liability arises in the Governmental Funds Balance Sheet when potential revenue does not meet both the *measurable* and *available* criteria for recognition in the current period. This *unavailable* deferred revenue consists primarily of uncollected property taxes and assessments not deemed available to finance operation of the current period. In the Government-wide Statement of Net Assets, with a full accrual basis of accounting, revenue must be recognized as soon as it is earned regardless of its availability. Thus, the liability created on the Governmental Fund Balance Sheet for unavailable deferred revenue is eliminated. Note that deferred revenues also arise outside the scope of measurement focus and basis of accounting, such as when the City receives resources before it has a legal claim to them. For instance, when grant monies are received prior to the incurrence of qualifying expenditures.

Similar to the way its revenues are recorded, governmental funds only record those expenditures that affect current financial resources. Principal and interest on general long-term debt are recorded as fund liabilities only when due, or when amounts have been accumulated in the debt service fund for payments to be made early in the following year. Vested compensated absences are recorded as expenditures only to the extent that they are expected to be liquidated with expendable financial resources. In the Government-wide Financial Statements, however, with a full accrual basis of accounting, all expenditures affecting the economic resource status of the government must be recognized. Thus, the expense and related accrued liability for long term portions of debt and compensated absences must be included.

Since the governmental fund statements are presented on a different measurement focus and basis of accounting than the government-wide statements' governmental column, a reconciliation is necessary to explain the adjustments needed to transform the fund based financial statements into the governmental column of the government-wide presentation. This reconciliation is part of the financial statements.

Amounts reported as program revenues include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the City's Water, Sewer, Solid Waste, Storm Drain and Marina funds are charges to customers for sales and services. The Water, Sewer and Storm Drain funds also recognize fees intended to recover the cost of connecting new customers to the City's utility systems as operating revenue. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

D. Budgetary Information

Biennial appropriated budgets are adopted for the General Fund, Special Revenue funds, Debt Service funds, Capital Projects funds, and Proprietary funds. For governmental funds, there are no differences between the budgetary basis and generally accepted accounting principles. Budgetary accounts are integrated in fund ledgers for all budgeted funds, but the financial statements include budgetary comparisons for annually budgeted governmental funds only.

Biennial appropriated budgets are adopted at the level of the fund and the budget constitutes the legal authority for expenditure at that level. Subsidiary revenue and expenditure ledgers are used to compare the budgeted amounts with actual revenues and expenditures. As a management control device, the subsidiary ledgers monitor expenditures for individual functions and activities by object class.

Appropriations for general and special revenue funds lapse at the end of the second year of the fiscal biennium (except for appropriations for capital outlays, which are carried forward from year to year until fully expended or the purpose of the appropriations has been accomplished or abandoned).

Procedures For Adopting the Original Budget

The City's biennial budget procedures are mandated by RCW 35A.34. The process under which the budget is adopted is described in the following paragraphs.

Prior to the first Tuesday in November the Finance Director submits a proposed budget to the Mayor and City Council. This budget is based on priorities established by the Council and estimates provided by City departments during the preceding months, and balanced with revenue estimates made by the Finance Director.

During the months of November and December, the Council conducts public hearings on the proposed budget for the purpose of obtaining citizens' comments. The Council makes its adjustments and adopts by ordinance a final balanced budget no later than December 31. Within 30 days of adoption, the final budget is available to the public.

Mid-biennial Review and Modification

A mid-biennial review and modification of the biennial budget occurs no sooner than eight months after the start nor later than the conclusion of the first year of the fiscal biennium. The Finance Director prepares the proposed budget modification and provides for publication of notice of hearings consistent with publication of notices for adoption of other City ordinances. Copies of the proposed modification are distributed to members of the City Council. Copies of the proposed modification are available to the public at the office of the City Clerk and at public hearings thereon.

Immediately following the preparation of the proposed budget modification by the Mayor, public hearings on the proposed budget modification are held. The City Clerk publishes a notice once each week for two consecutive weeks stating that the budget modification has been proposed, and a copy thereof will be furnished to any member of the public who will call at the Clerk's office, and that the City Council will meet on or before the first Monday of the month next preceding the beginning of the second year of the fiscal biennium, but not before September 1 of the first year of the fiscal biennium, for the purpose of fixing the budget for the second year of the fiscal biennium, designating the date, time and place of the City Council meeting and that any taxpayer may appear there at and be heard for or against any part of the proposed budget modification. The publication of the notice is made in the official newspaper of the City. The budget modification, if any, is approved in the same manner as other ordinances of the City.

The budget amounts shown in the financial statements do not represent total appropriations for the entire biennial budget period. The budget amounts shown represent appropriations for a single calendar year within the biennial budget.

Amending the Budget

The Finance Director is authorized to transfer budgeted amounts between object classes within departments; however, any revisions that alter the total expenditures of a fund, or that affect the number of authorized employee positions, salary ranges, hours, or other conditions of employment must be approved by the City Council.

When the City Council determines that it is in the best interest of the City to increase or decrease the appropriation for a particular fund, it may do so by ordinance approved by one or more than the majority after holding public hearing(s).

The budget amounts shown in the financial statements are the final authorized amounts as revised during the year.

The financial statements contain the original and final budget information. The original budget is the first complete appropriated budget. The final budget is the original budget adjusted by all reserves, transfers, allocations, supplemental appropriations, and other legally authorized changes applicable for the fiscal year.

Deficit Fund Equity

As of December 31, 2009, the City has one fund reflecting a deficit fund balance. Fund #501 Equipment Repair fund shows a negative balance of \$37,214. This deficit is due to the timing of billings processed to other internal departments. The City anticipates this deficit fund balance will be reversed in 2010.

E. Assets, Liabilities, and Equities

Cash and Investments

It is the City's policy to invest all temporary cash surpluses. As of December 31, 2009, the Treasurer was holding \$42,140,540 in short-term residual investments of surplus cash. This amount is included in the amount classified on the balance sheet as cash and cash equivalents in various funds. The interest on

these investments is prorated to the various funds based upon the fund's average daily cash balance. For purposes of the Statement of Cash Flows, the City considers all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents.

Receivables

Taxes receivable consists of property taxes and related interest and penalties (see Property Taxes Note No. 5). Accrued interest receivable consists of amounts earned on investments, notes, and contracts at the end of the year.

Customer accounts receivable consist of amounts owed from private individuals or organizations for goods and services including amounts owed for which billings have not been prepared. Notes and contracts receivable consist of amounts owed on open account from private individuals or organizations for goods and services rendered.

Amounts Due To and From Other Funds and Governmental Units, Interfund Loans and Advances Receivable

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "interfund loans receivable/payable" or "advances to/from other funds." All other outstanding balances between funds are reported as "due to/from other funds." A separate schedule of interfund loans receivable and payable is furnished in Note No. 15 Interfund Balances and Transfers.

Advances between funds, as reported in the fund financial statements, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

Inventories

Inventories in governmental funds consist of expendable supplies held for consumption. The cost is recorded as an expenditure at the time individual inventory items are purchased. The reserve for inventory is equal to the ending amount of inventory to indicate that a portion of the fund balance is not available for future expenditures. A comparison to market value is not considered necessary.

Inventories in proprietary funds are valued by the FIFO method (which approximates the market value).

Restricted Assets and Liabilities

These accounts contain resources for debt service, landfill closure requirements, a 24" waterline reserve, and certain customer deposits. Specific debt service reserve requirements are described in Note No. 10 Long-term Debt.

The restricted cash of the City is composed of the following:

	Governmental	Business-type
Capital projects	\$252,255	\$129,928
Customer deposits	300	78,597
Debt service	-	953,353
Equipment replacement	292,902	5,671,248
Fire fees	50,800	-
Landfill closure	-	70,157
Park impact fees	148,373	-
Total restricted cash	\$744,630	\$6,903,283

Capital Assets

The City of Oak Harbor has chosen to capitalize and report all of its general infrastructure assets that have been acquired (purchased, constructed and donated) in the year 2002 statements rather than phase in the assets. The City implemented accounting of all its infrastructure retroactively and is depreciating the assets using the traditional straight-line method. Capital assets, which include property, plant, equipment, and infrastructure (e.g. roads, pathways, street lights) are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets are defined by the City as assets with an initial, individual cost of \$5,000 or more, and an estimated useful life of greater than five years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated assets are recorded at estimated fair market value as of the date of the donation. The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of the capital assets of business-type activities is included as part of the capitalized value of the assets constructed.

Compensated Absences

Compensated absences are absences for which employees will be paid, such as vacation and sick leave. In governmental and similar trust funds, compensated absences that are expected to be liquidated with expendable available financial resources are reported as expenditures and fund liability in the fund that will pay for them. The remainder of the compensated absences liability is reported in the General Long-term Debt Account Group. In proprietary funds, compensated absences are recorded as an expense and liability of the fund that will pay for them.

City employees accumulate vacation and sick leave on a monthly basis. Employees earn vacation at a rate of a certain number of hours per year. The number of hours per year depends upon length of service. Annual vacation may be accumulated to a maximum of two years accrual. Sick leave for all employees is earned at a rate of one day per month. A maximum of 180 days sick leave may be accumulated.

At termination of employment, employees with required length of service may receive cash payment for accumulated vacation and a percentage of sick leave with five (5) or more years of service. The payment is based on current wages at the time of termination of service.

Long-term Debt

(See Long-term Debt Note No. 10)

In the government-wide financial statements, and proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type Statement of Net Assets. Bond premiums and discounts are deferred and amortized over the life of the bonds. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are treated as period costs in the year of issue and are shown as other financing uses.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Deferred Revenues

This account includes amounts recognized as receivables but not revenues in governmental funds because the revenue recognition criteria have not been met.

Fund Reserves and Designations

Tentative plans for utilization of fund balances in future periods are recorded as designations of fund balance in the fund-level financial statements. Planned expenditures include future capital projects, debt service, equipment reserves and other commitments for which fund balances have not been appropriated or specifically segregated.

Note 2 – Reconciliation of Government-wide and Fund Financial Statements

Explanation of Certain Differences Between the Governmental Funds Balance Sheet and the Government-wide Statement of Net Assets

The governmental funds' Balance Sheet includes a reconciliation between fund balance – total governmental funds and net assets – governmental activities as reported in the government-wide Statement of Net Assets. The following represent the reconciling items:

Capital assets used in governmental activities are not financial resources and are not reported in funds:		
Historical cost of assets not being depreciated	\$ 9,758,146	
Historical cost of assets being depreciated	36,495,209	
Accumulated depreciation	<u>(23,006,389)</u>	\$ 23,246,966
 Long-term assets not available to pay for current period expenditures and therefore deferred		910,643
 Internal service funds are used by management to charge the costs of fleet management, shop facilities and information systems to individual funds. The assets and liabilities of the internal service funds are included in the governmental activities in the statement of net assets.		603,079
 Some liabilities are not due and payable in the current period and therefore are not reported in the funds, including:		
Accounts payable	\$ (112,936)	
Compensated absences	(648,508)	
Bonds and interest payable	(362,897)	
Other post-employment benefit liabilities	<u>(254,672)</u>	(1,379,013)
 Net adjustment to increase <i>fund balance - total governmental funds</i> to arrive at <i>net assets - governmental activities</i> .		<u><u>\$ 23,381,675</u></u>

Explanation of Certain Differences Between the Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances and the Government-wide Statement of Activities

The governmental funds' Statement of Revenues, Expenditures, and Changes in Fund Balances includes a reconciliation between *net changes in fund balances – total governmental funds* and *changes in net assets of governmental activities* as reported in the government-wide Statement of Activities. Elements of the reconciliation include the net increase in governmental net assets, increases in long-term debt or other long-term liabilities, and certain activities of internal service funds that are allocated to governmental activities outside of the funds themselves. The following represent the reconciling items:

Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as outlays exceeded depreciation in the current period:

Capital outlay	\$ 794,756	
Depreciation	<u>(888,302)</u>	\$ (93,546)

Donated capital increases net assets in the statement of activities, but does not appear in the governmental funds because it is not a financial resource. 348,048

Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds. 61,251

Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets and does not effect the statement of activities 266,313

Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds, including:

Change in accounts payable	\$ 58,508	
Change in compensated absences	(59,709)	
Other post-employment benefit expense	<u>(131,383)</u>	(132,584)

Internal service funds are used by management to charge the costs of fleet management, shop facilities and information systems to individual funds. The net revenues and expenses of the internal service funds are reported with governmental activities in the statement of activities. 67,418

Net adjustment to increase *net changes in fund balance - total governmental funds* to arrive at *changes in net assets of governmental activities*. \$ 516,900

Note 3 – Stewardship, Compliance, and Accountability

None of the City's funds exceeded its authorized appropriation authority for 2009.

Note 4 – Deposits and Investments

As required by state law, all investments and deposits of the City's funds are obligations of the U.S. Government, the State Treasurer's Investment Pool, bankers' acceptances, deposits with Washington State banks and savings and loan institutions.

A reconciliation of cash, cash equivalents (including pooled investments) and investments as shown in the government-wide and fund financial statements is as follows:

Notes	
Investments	\$ 30,148,986
Deposits	19,639,467
Total	\$ 49,788,453
Governmental Financial Statements	
Governmental funds - cash and cash equivalents	\$ 18,206,508
Governmental funds - restricted cash	451,728
Proprietary funds - cash and cash equivalents	23,828,090
Proprietary-type funds - restricted cash	1,232,035
Internal service funds - cash and cash equivalents	105,942
Internal service funds - restricted cash	5,964,150
Total	\$ 49,788,453

Internal service fund assets and liabilities are allocated between governmental and business-type activities for government-wide financial reporting purposes. Accordingly, the following schedule represents the allocation of internal service fund deposits and investments between the two fund types for the purpose of providing reconciliation between governmental fund balances and the balances appearing on the Statement of Net Assets:

Reconciliation of governmental deposits and investments to government-wide deposits and investments	
Governmental funds - cash and cash equivalents	\$ 18,206,508
Allocated internal service fund - cash and cash equivalents	-
Governmental Activities - cash and cash equivalents	18,206,508
Governmental funds - restricted cash	451,728
Allocated internal service fund - restricted cash	292,902
Governmental Activities - restricted cash	744,630
Proprietary-type funds - cash and cash equivalents	23,828,090
Allocated internal service fund - cash and cash equivalents	105,942
Business-type activities - cash and cash equivalents	23,934,032
Proprietary-type funds - restricted cash	1,232,035
Allocated internal service fund - restricted cash	5,671,248
Business-type activities - restricted cash	6,903,283
Total	\$ 49,788,453

Deposits

On December 31, 2009 the carrying amount of the City's cash demand deposits, including money market accounts was \$19,639,467 and the bank balance with US Bank of Washington was \$19,988,084. Petty cash on hand totaled \$7,559. The FDIC insures the first \$250,000 of the City's demand deposits and separately insures the first \$250,000 in the aggregate of the City's time deposits and savings deposits. The remaining deposit balances are insured by the Washington Public Deposit Protection Commission (WPDPC) Act of 1969. The WPDPC is a multiple financial institution collateral pool. State statute permits additional amounts to be assessed on a pro rata basis to members of the pool in the event the pool's collateral should be insufficient to cover a loss.

Investments

The City has \$30,148,986 in the State’s Local Government Investment Pool (LGIP) which is managed by the Washington State Treasurer’s Office. The LGIP is not SEC registered but has oversight provided by the following sources: 1) annually audited by the Office of the State Auditor; 2) annually audited by an outside, independent auditor; 3) an Advisory Committee meets quarterly to advise the State Treasurer on issues regarding the LGIP; 4) monthly statement enclosures detailing portfolio breakdown and earnings information sent to participants; and, 5) quarterly newsletters that include a compliance report and quarterly financials. Financial reports are available at the State Treasurers Office, P.O. Box 40200, Olympia, Washington, 98504-2000.

Long-term investments (maturities over 90 days) are purchased through broker relationships. All of the City’s investments at year-end were held by the Trust Department of the City’s depository bank in the City’s name. The City does not hold any investments for other local governments, individuals or private organizations.

Investments are reported within Cash and Investments of Governmental Activities and within Cash and Cash Equivalents of Investments of Business-type Activities. As of December 31, 2009, the City had the following investments:

Investments	Fair Value	Weighted Average Maturity (Months)
Washington State Investment Pool (LGIP)	\$ 23,970,566	1.30
Federal Home Loan Mortgage Corp.	2,083,820	0.80
Federal Home Loan Bank	4,094,600	0.78
Total fair value	\$ 30,148,986	
Portfolio weighted average maturity		2.88

Interest Rate Risk: In accordance with its investment policy, the City manages its exposure to fair value losses arising from increasing interest rates by limiting the weighted average maturity of its investment portfolio to less than 12 months.

Custodial Credit Risk-investments: This is the risk that, in event of a failure of the counterparty to an investment transaction, the City would not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. As of December 31, 2009, the City did not have any investments that are subject to the custodial credit risk.

Credit Risk: Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The LGIP, a 2a7-like pool, as defined by GASB 31, is unrated. The policy of the LGIP is to invest in securities and instruments that are rated A-1 by Standard and Poor’s Corporation and P-1 by Moody’s Investors Services, Inc.

To limit risk, state law does not allow general governments such as the City to invest in corporate debt. However, the Pension fund is not restricted by state law to invest in corporate debt with ratings equivalent or above the single "A" rating by nationally recognized statistical rating organizations. The ratings of debt securities as of December 31, 2009 are:

Debt Security	S&P Rating
Freddie Mac (Federal Home Loan Mortgage Corporation)	AAA
Federal Home Loan Bank	AAA
Federal Farm Credit Bank	AAA

Concentration of Credit Risk: City of Oak Harbor diversifies its investments by security type and institution. With the exception of U.S. Treasury securities and authorized pools, the City's investment policy does not allow for an investment in any one issuer that is in excess of 50% of the City's total investment portfolio.

Note 5 – Property Taxes

The County Treasurer acts as an agent to collect property taxes levied in the County for all taxing authorities.

Property Tax Calendar	
January 1	Taxes are levied and become an enforceable lien against properties.
February 14	Tax bills are mailed
April 30	First of two equal installment payments are due.
May 31	Assessed value of property established for next year's levy at 100 percent of market value.
October 31	Second installment is due.

Property taxes are recorded as a receivable and revenue when levied. Property taxes collected in advance of the fiscal year to which they apply are recorded as deferred revenue and recognized as revenue of the period to which they apply. No allowance for uncollectible taxes is established because delinquent taxes are considered fully collectible. Prior year tax levies were recorded using the same principal and delinquent taxes are evaluated annually.

The City is permitted by law to levy up to \$3.60 minus the Sno-Isle Library rate of \$0.31 per \$1,000 of assessed valuation for general governmental services, subject to two limitations:

1. Washington State law in RCW 84.55.010 limits the growth of regular property taxes to the lower of the Implicit Price Deflator or 1%, before adjustments for new construction. If the assessed valuation increases by more than 6% due to revaluation, the levy rate will be decreased.
2. The Washington State Constitution limits the regular (non-voted) combined property tax rate applied to an individual's property to 1% (\$10 per \$1,000) of the market valuation. If the taxes of all districts exceed this amount, each is proportionately reduced until the total is at or below the 1% limit.

The City's regular levy for 2009 was \$1.99998 per \$1,000 on an assessed valuation of \$1,897,999,833 for a regular levy of \$3,795,967.

The City's general obligation bond levy for 2009 was \$0.13092 per \$1,000 on an assessed valuation of \$1,885,063,847 for a total bond levy of \$246,800.

Note 6 – Capital Assets and Depreciation

Capital assets, which include property, plant, equipment, and infrastructure assets (e.g. roads, pathways, street lights, etc.) are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. In the governmental fund statements, capital assets are charged to expenditures as purchased, and capitalized in the proprietary fund statements. Capital assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated assets are recorded at estimated fair market value as of the date of the donation.

Capital assets are defined by the City as assets with an initial, individual cost of \$5,000 or more, and an estimated useful life of greater than five years. Additions or improvements and other capital outlays that significantly extend the useful life of an asset, or that significantly increase the capacity of an asset are capitalized. Other costs incurred for repairs and maintenance are expensed as incurred. Depreciation on exhaustible assets is recorded as an allocated expense in the Statement of Activities with accumulated depreciation reflected in the Statement of Net Assets and is provided using the straight-line method over the following estimated useful lives:

Asset	Years
Buildings and improvements	20-50
Improvements other than buildings	10-20
Machinery and equipment	5-10
Vehicles	5-10
Utility systems	20-40
Infrastructure	20-40

Governmental-type capital assets activity for the year ended December 31, 2009 was as follows:

Governmental Activities:	Beginning Balance			Ending Balance
	1/1/2009	Increases	Decreases	12/31/2009
Capital assets not being depreciated:				
Land	\$ 1,895,664	\$ -	\$ -	\$ 1,895,664
Recreation areas	6,447,597	133,442	-	6,581,039
Construction in progress	876,149	550,488	(158,194)	1,268,443
Intangible assets	-	13,000	-	13,000
Total assets not depreciated:	\$ 9,219,410	\$ 696,930	\$ (158,194)	\$ 9,758,146
Assets depreciated:				
Buildings	\$ 12,722,894	\$ 113,642	\$ (4,540,503)	\$ 8,296,033
Capital lease	138,572	-	-	138,572
Improvements	401,833	-	(49,281)	352,552
Machinery & equipment	10,318,115	53,411	(8,218,161)	2,153,365
Infrastructure	25,609,537	426,679	-	26,036,216
Total assets depreciated:	\$ 49,190,951	\$ 593,732	\$ (12,807,945)	\$ 36,976,738
Less accumulated depreciation:				
Buildings depreciation	\$ (4,557,049)	\$ (173,502)	\$ 909,197	\$ (3,821,354)
Capital lease depreciation	(138,572)	-	-	(138,572)
Improvements depreciaton	(72,619)	(17,628)	4,483	(85,764)
Machinery & equipment depreciation	(6,946,740)	(152,354)	6,060,372	(1,038,722)
Infrastructure depreciation	(17,503,213)	(576,323)	-	(18,079,536)
Total accumulated depreciation:	\$ (29,218,193)	\$ (919,807)	\$ 6,974,052	\$ (23,163,948)
Total assets depreciated (net):	\$ 19,972,758	\$ (326,075)	\$ (5,833,893)	\$ 13,812,790
Governmental activities				
total capital assets (net):	\$ 29,192,168	\$ 370,855	\$ (5,992,087)	\$ 23,570,936

During 2009, the City changed the method used to allocate the assets and liabilities of internal service funds between governmental and business-type activities. This change in allocation has resulted in the shifting of assets, and their related accumulated depreciation, from the governmental assets appearing on this schedule to business-type assets. Of the \$12,966,139 decrease in assets, \$171,802 is from normal asset reclassifications or retirements, with the remaining \$12,794, 337 reflecting the shift in assets from governmental to business-type activities. Of the \$6,974,052 decrease in accumulated depreciation, \$65,506 is from the normal reduction due to asset retirements, with the remaining \$6,908,546 reflecting the shift of accumulated depreciation from governmental to business-type activities.

The City purchased The Whidbey Island Marathon, an intangible asset in 2009. The cost of the Marathon is \$50,000 and will be made in 4 annual payments.

Depreciation expense for the various components of governmental activities is as follows:

Governmental Activities:	
General governmental	\$ 53,364
Public safety	95,186
Physical environment	23,049
Transportation	580,205
Mental and physical health	15,045
Cultural and recreational	121,453
Internal service fund capital assets are charged to the various functions based on their usage of the asset	31,505
Total depreciation expense - governmental activities	\$ 919,807

Business-type capital assets activity for the year ended December 31, 2009 was as follows:

Business-type Activities:	Beginning Balance			Ending Balance
	1/1/2009	Increases	Decreases	12/31/2009
Capital assets not being depreciated:				
Land	\$ 1,333,347	\$ -	\$ -	\$ 1,333,347
Construction in progress	1,033,552	2,718,422	(2,274,050)	1,477,924
Total capital assets not depreciated:	\$ 2,366,899	\$ 2,718,422	\$ (2,274,050)	\$ 2,811,271
Capital assets being depreciated:				
Buildings	\$ 4,277,010	\$ 4,540,503	\$ -	\$ 8,817,513
Improvements other than buildings	50,698,488	3,280,467	-	53,978,955
Machinery & equipment	4,325,676	9,095,708	(382,469)	13,038,915
Total assets depreciated:	\$ 59,301,174	\$ 16,916,678	\$ (382,469)	\$ 75,835,383
Less accumulated depreciation:				
Buildings depreciation	\$ (2,795,441)	\$ (1,122,608)	\$ -	\$ (3,918,049)
Improvements other than buildings	(18,100,814)	(1,467,701)	-	(19,568,515)
Machinery & equipment depreciation	(1,944,266)	(6,928,092)	368,873	(8,503,485)
Total accumulated depreciation:	\$ (22,840,521)	\$ (9,518,401)	\$ 368,873	\$ (31,990,049)
Total assets depreciated (net):	\$ 36,460,653	\$ 7,398,277	\$ (13,596)	\$ 43,845,334
Business-type activities				
total capital assets (net):	\$ 38,827,552	\$ 10,116,699	\$ (2,287,646)	\$ 46,656,605

During 2009, the City changed the method used to allocate the assets and liabilities of internal service funds between governmental and business-type activities. This change in allocation has resulted in the shifting of assets, and their related accumulated depreciation, from the governmental assets to the business-type assets appearing on the preceding schedule. Of the \$19,635,100 increase in assets, \$6,840,763 is from normal purchases or asset reclassifications, with the remaining \$12,794,337 reflecting the shift in assets from governmental to business-type activities. Of the \$9,518,401 increase in accumulated depreciation, \$2,609,855 is from the normal changes due to current period depreciation expense and any prior period adjustments, with the remaining \$6,908,546 reflecting the shift of internal service fund accumulated depreciation from governmental to business-type activities. Amount of depreciation expense charged to capital assets by function are as follows:

Depreciation expense for the various components of governmental activities is as follows:

Business-type Activities:	
Water	\$ 664,917
Sewer	891,797
Solid waste	70,366
Storm drain	105,638
Marina	209,750
Internal service	569,551
Total depreciation expense - business-type activities	\$ 2,512,019

The City has active construction projects as of December 31, 2009. The projects include street improvements, redevelopment of the Marina and upgrades to the sewer diversion pump station.

At year end, the government's commitments with contractors are as follows:

Project	Spent to Date	Remaining Commitment
SE Pioneer Way street improvements	\$ 220,926	\$ 398,188
Marina redevelopment	332,635	720,186
N Oak Harbor Street improvements	17,201	107,926
Diversion pump station upgrade	-	119,278
Goldie Road sewer extension	833,802	353,060
Total	\$ 1,404,564	\$ 1,698,638

Note 7 – Pension Plans

Substantially all City of Oak Harbor full-time and qualifying part-time employees participate in one of the following statewide retirement systems administered by the Washington State Department of Retirement Systems, under cost-sharing multiple-employer public employee defined benefit and defined contribution retirement plans. The Department of Retirement Systems (DRS), a department within the primary government of the State of Washington, issues a publicly available comprehensive annual financial report (CAFR) that includes financial statements and required supplementary information for each plan. The DRS CAFR may be obtained by writing to: Department of Retirement Systems, Communications Unit, P.O. Box 48380, Olympia, WA 98504-8380; or it may be downloaded from the DRS website at www.drs.wa.gov. The following disclosures are made pursuant to GASB Statement No. 27, *Accounting for Pensions by State and Local Government Employers* and No. 50, *Pension Disclosures, an Amendment of GASB Statements No. 25 and No. 27*.

Public Employees' Retirement System (PERS) Plans 1, 2 AND 3

Plan Description

PERS is a cost-sharing multiple-employer retirement system comprised of three separate plans for membership purposes: Plans 1 and 2 are defined benefit plans and plan 3 is a defined benefit plan with a defined contribution component.

Membership in the system includes: elected officials; state employees; employees of the Supreme, Appeals, and Superior courts (other than judges in a judicial retirement system); employees of legislative committees; community and technical colleges, college and university employees not participating in national higher education retirement programs; judges of district and municipal courts; and employees of local governments.

PERS participants who joined the system by September 30, 1977, are Plan 1 members. Those who joined on or after October 1, 1977 and by either, February 28, 2002 for state and higher education employees, or August 31, 2002 for local government employees, are Plan 2 members unless they exercise an option to transfer their membership to Plan 3. PERS participants joining the system on or after March 1, 2002 for state and higher education employees, or September 1, 2002 for local government employees have the irrevocable option of choosing membership in either PERS Plan 2 or PERS Plan 3. This option must be exercised within 90 days of employment. An employee is reported in Plan 2 until a choice is made. Employees who fail to choose within 90 days default to PERS Plan 3. Notwithstanding, PERS Plan 2 and Plan 3 members may opt out of plan membership if terminally ill, with less than five years to live.

PERS Plan 1 and Plan 2 defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. PERS retirement benefit provisions are established in state statute and may be amended only by the State Legislature.

PERS Plan 1 members are vested after the completion of five years of eligible service. Plan 1 members are eligible for retirement at any age after 30 years of service, or at age 60 with five years of service, or at the age of 55 with 25 years of service. The annual benefit is two percent of the average final compensation (AFC) per year of service, capped at 60 percent. (The AFC is based on the greatest compensation during any 24 eligible consecutive compensation months.) This annual benefit is subject to a minimum for PERS Plan 1 retirees who have 25 years of service and have been retired 20 years, or who have 20 years of service and have been retired 25 years. Plan 1 members who retire from inactive status prior to the age of 65 may receive actuarially reduced benefits. If a survivor option is chosen, the benefit is further reduced. A cost-of living allowance (COLA) is granted at age 66 based upon years of service times the COLA amount, which is increased three percent annually. Plan 1 members may also elect to receive an optional COLA amount that provides an automatic annual adjustment based on the Consumer Price Index. The adjustment is capped at three percent annually. To offset the cost of this annual adjustment, the benefit is reduced.

PERS Plan 2 members are vested after the completion of five years of eligible service. Plan 2 members may retire at the age of 65 with five years of service with an allowance of two percent of the AFC per year of service. (The AFC is based on the greatest compensation during any eligible consecutive 60-month period.) Plan 2 members who retire prior to the age of 65 receive reduced benefits. If retirement is at age 55 or older with at least 30 years of service, a three percent per year reduction applies; otherwise an actuarial reduction will apply. The benefit is also actuarially reduced to reflect the choice of a survivor option. There is no cap on years of service credit; and a cost-of- living allowance is granted (based on the Consumer Price Index), capped at three percent annually.

PERS Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component. The defined benefit portion provides a benefit calculated at one percent of the AFC per year of service. (The AFC is based on the greatest compensation during any eligible consecutive 60-month period.) Effective June 7, 2006, PERS Plan 3 members are vested in the defined benefit portion of their plan after ten years of service; or after five years of service, if twelve months of that service are earned after age 44; or after five service credit years earned in PERS Plan 2 prior to June 1, 2003. Plan 3 members are immediately vested in the defined contribution portion of their plan. Vested Plan 3 members are eligible to retire with full benefits at age 65, or they may retire at age 55 with 10 years of service. Plan 3 members who retire prior to the age of 65 receive reduced benefits. If retirement is at age 55 or older with at least 30 years of service, a three percent per year reduction applies; otherwise an actuarial reduction will apply. The benefit is also actuarially reduced to reflect the choice of a survivor option. There is no cap on years of service credit; and Plan 3 provides the same cost-of- living allowance as Plan 2.

The defined contribution portion can be distributed in accordance with an option selected by the member, either as a lump sum or pursuant to other options authorized by the Employee Retirement Benefits Board.

There are 1,192 participating employers in PERS. Membership in PERS consisted of the following as of the latest actuarial valuation date for the plans of June 30, 2008:

Type of Members	Number of Participants
Retirees and beneficiaries receiving benefits	73,122
Terminated plan members entitled to but not yet receiving benefits	27,267
Active plan members vested	105,212
Active plan members non-vested	56,456
Total	262,057

Funding Policy

Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates, Plan 2 employer and employee contribution rates, and Plan 3 employer contribution rates. Employee contribution rates for Plan 1 are established by statute at six percent for state agencies and local government unit employees, and 7.5 percent for state government elected officials. The employer and employee contribution rates for Plan 2 and the employer contribution rate for Plan 3 are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. All employers are required to contribute at the level established by the Legislature. Under PERS Plan 3, employer contributions finance the defined benefit portion of the plan, and member contributions finance the defined contribution portion. The Employee Retirement Benefits Board sets Plan 3 employee contribution rates. Six rate options are available ranging from 5 to 15 percent; two of the options are graduated rates dependent on the employee’s age. The methods used to determine the contribution requirements are established under state statute in accordance with chapters 41.40 and 41.45 RCW.

The required contribution rates expressed as a percentage of current year covered payroll, as of December 31, 2009, are as follows:

Contributer	PERS Plan 1	PERS Plan 2	PERS Plan 3
Employer*	5.31%	5.31%	5.31%**
Employee	6.00%	3.90%	***

*The employer rates include the employer administrative expense fee currently set at 0.16%.

**Plan 3 defined benefit portion only.

***Variable from 5.0% minimum to 15.0% maximum based on rate selected by the PERS 3 member.

Both the City of Oak Harbor and the employees made the required contributions. The overall required contributions for the years ended December 31 were as follows:

Year	PERS Plan 1	PERS Plan 2	PERS Plan 3
2009	\$20,790.89	\$405,153.66	\$308,250.13
2008	\$20,567.72	\$403,608.39	\$304,888.29
2007	23,058.02	169,839.74	188,977.45

Law Enforcement Officers' and Fire Fighters' Retirement System (LEOFF) Plans 1 & 2

Plan Description

LEOFF is a cost-sharing multiple-employer retirement system comprised of two separate defined benefit plans. LEOFF participants who joined the system by September 30, 1977 are Plan 1 members. Those who joined on or after October 1, 1977 are Plan 2 members. Membership in the system includes all full-time, fully compensated, local law enforcement commissioned officers, firefighters and, as of July 24, 2005, those emergency medical technicians who were given the option and chose LEOFF Plan 2 membership. LEOFF membership is comprised primarily of non-state employees, with Department of Fish and Wildlife enforcement officers, who were first included prospectively effective July 27, 2003, being an exception.

Effective July 1, 2003, the LEOFF Plan 2 Retirement Board was established by Initiative 790 to provide governance of LEOFF Plan 2. The Board's duties include adopting contribution rates and recommending policy changes to the Legislature for the LEOFF Plan 2 retirement plan.

LEOFF defined benefit retirement benefits are financed from a combination of investment earnings, employer and employee contributions, and a special funding situation in which the state pays through state legislative appropriations. LEOFF retirement benefit provisions are established in state statute and may be amended by the State Legislature.

LEOFF Plan 1 members are vested after the completion of five years of eligible service. Plan 1 members are eligible for retirement with five years of service at the age of 50. The benefit per year of service calculated as a percent of final average salary (FAS) is as follows:

Term of Service	Percent of Final Average Salary
20 or more years	2.00%
10 but less than 20 years	1.50%
5 but less than 10 years	1.00%

The FAS is the basic monthly salary received at the time of retirement, provided a member has held the same position or rank for 12 months preceding the date of retirement. Otherwise, it is the average of the highest consecutive 24 months' salary within the last ten years of service. A cost-of-living allowance is granted (based on the Consumer Price Index).

LEOFF Plan 2 members are vested after the completion of five years of eligible service. Plan 2 members may retire at the age of 50 with 20 years of service, or at the age of 53 with five years of service, with an allowance of two percent of the FAS per year of service. The FAS is based on the highest consecutive 60 months. Plan 2 members who retire prior to the age of 53 receive reduced benefits. Benefits are actuarially reduced for each year that the benefit commences prior to age 53 and to reflect the choice of a survivor option. If the member has at least 20 years of service and is age 50, the reduction is three percent for each year prior to age 53. There is no cap on years of service credit; and a cost-of-living allowance is granted (based on the Consumer Price Index), capped at three percent annually.

There are 375 participating employers in LEOFF. Membership in LEOFF consisted of the following as of the last actuarial valuation date for the plans of June 30, 2008:

Type of Members	Number of Participants
Retirees and beneficiaries receiving benefits	9,268
Terminated plan members entitled to but not yet receiving benefits	650
Active plan members vested	13,120
Active plan members non-vested	3,927
Total	26,965

Funding Policy

Starting on July 1, 2000, LEOFF Plan 1 employers and employees contribute zero percent as long as the plan remains fully funded. Employer and employee contribution rates are developed by the Office of the State Actuary to fully fund the plan. LEOFF Plan 2 employers and employees are required to pay at the level adopted by the LEOFF Plan 2 Retirement Board. All employers are required to contribute at the level required by state law. The Legislature, by means of a special funding arrangement, appropriated money from the state General Fund to supplement the current service liability and fund the prior service costs of LEOFF Plan 2 in accordance with the requirements of the Pension Funding Council and the LEOFF Plan 2 Retirement Board. However, this special funding situation is not mandated by the state constitution and this funding requirement could be returned to the employers by a change of statute.

The required contribution rates expressed as a percentage of current year covered payroll, as of December 31, 2009, were as follows:

Contributer	LEOFF Plan 1	LEOFF Plan 2
Employer*	0.16%	5.24%**
Employee	0.00%	8.46%
State	N/A	3.38%

*The employer rates include the employer administrative expense fee currently set at 0.16%.

**The employer rate for ports and universities is 8.99%.

Both the City of Oak Harbor and the employees made the required contributions. The overall required contributions for the years ending December 31 were as follows:

Year	LEOFF Plan 1	LEOFF Plan 2
2009	\$298.45	\$367,366.04
2008	288.55	350,492.30
2007	274.17	302,508.54

Public Safety Employees' Retirement System (PSERS) Plan 2

Plan Description

PSERS is a cost-sharing multiple-employer retirement system comprised of a single defined benefit plan, PSERS Plan 2. PSERS was created by the 2004 Legislature and became effective July 1, 2006.

PSERS Plan 2 membership includes full-time employees of a covered employer on or before July 1, 2006, who met at least one of the PSERS eligibility criteria, and elected membership during the election period of July 1, 2006 to September 30, 2006; and those full-time employees, hired on or after July 1, 2006 by a covered employer, that meet at least one of the PSERS eligibility criteria.

A *covered employer* is one that participates in PSERS. Covered employers include: State of Washington agencies: Department of Corrections, Department of Natural Resources, Parks and Recreation Commission, Gambling Commission, Washington State Patrol, and Liquor Control Board; Washington state counties; Washington state cities except Seattle, Tacoma and Spokane.

To be eligible for PSERS, an employee must work on a full-time basis and:

- have completed a certified criminal justice training course with authority to arrest, conduct criminal investigations, enforce the criminal laws of Washington, and carry a firearm as part of the job; OR
- have primary responsibility to ensure the custody and security of incarcerated or probationary individuals; OR
- function as a limited authority Washington peace officer, as defined in RCW 10.93.020; OR
- have primary responsibility to supervise eligible members who meet the above criteria.

PSERS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. PSERS retirement benefit provisions are established in state statute and may be amended only by the State Legislature.

PSERS Plan 2 members are vested after the completion of five years of eligible service. PSERS Plan 2 members may retire at the age of 65 with five years of service, or at the age of 60 with at least ten years of PSERS service credit, with an allowance of two percent of the average final compensation (AFC) per year of service. The AFC is the monthly average of the member's 60 consecutive highest-paid service credit months, excluding any severance pay such as lump-sum payments for deferred sick leave, vacation or annual leave. Plan 2 members who retire prior to the age of 60 receive reduced benefits. If retirement is at age 53 or older with at least 20 years of service, a three percent per year reduction for each year between the age at retirement and age 60 applies. There is no cap on years of service credit; and a cost-of-living allowance is granted (based on the Consumer Price Index), capped at three percent annually.

There are 73 participating employers in PSERS. Membership in PSERS consisted of the following as of the latest actuarial valuation date for the plan of June 30, 2008:

Type of Members	Number of Participants
Retirees and beneficiaries receiving benefits	1
Terminated plan members entitled to but not yet receiving benefits	-
Active plan members vested	-
Active plan members non-vested	3,981
Total	3,982

Funding Policy

Each biennium, the state Pension Funding Council adopts PSERS Plan 2 employer and employee contribution rates. The employer and employee contribution rates for Plan 2 are developed by the Office of the State Actuary to fully fund Plan 2. All employers are required to contribute at the level established by the Legislature. The methods used to determine the contribution requirements are established under state statute in accordance with chapters 41.37 and 41.45 RCW.

The required contribution rates expressed as a percentage of current-year covered payroll, as of December 31, 2009 are as follows:

Contributer	PSERS Plan 2
Employer*	7.85%
Employee	6.55%

*The employer rate includes an employer administrative expense fee of 0.16%.

Both the City of Oak Harbor and the employees made the required contributions. The overall required contributions for the years ending December 31 were as follows:

Year	PSERS Plan 2
2009	\$12,070.12
2008	8,544.93
2007	7,900.23

Other Retirement Systems - Volunteer Fire Fighters' Relief and Pension Fund

The Washington State Board for Volunteer Firefighters and Reserve Officers administers the Volunteer Firefighters' and Reserve Officers' Relief and Pension Act; a cost-sharing multiple-employer retirement system created by the Legislature in 1945 under Chapter 41.24 RCW. It provides pension, disability and survivor benefits. Membership in the system requires service with a fire department of an electing municipality of Washington State except those covered by LEOFF. The system is funded through municipal or member pension contributions of \$60 per year; employer disability fee of \$30 per year; 40 percent of the Fire Insurance Premium Tax; and earnings from the investment of money by the Washington State Investment Board. However, members may elect to withdraw their contributions upon termination.

Note 8 – Risk Management

The City of Oak Harbor is a member of the Washington Cities Insurance Authority. Chapter 48.62 authorizes the governing body of any one or more governmental entities to form together into or join a pool or organization for the joint purchasing of insurance, and/or joint self-insuring, and/or joint hiring or contracting for risk management services to the same extent that they may individually purchase insurance, self-insure, or hire or contract for risk management services. An agreement to form a pooling arrangement was made pursuant to the provisions of Chapter 39.34 RCW, the Interlocal Cooperation Act. The pool was formed January 1, 1981 when cities in the State of Washington joined together by signing an Interlocal Governmental Agreement to pool their self-insured losses and jointly purchase insurance and administrative services.

The pool allows members to jointly purchase insurance coverage, provide related services, such as administration, risk management, claims administration, etc. Coverage for Public Officials Liability and all other coverages are on an "occurrence basis". The Pool maintains a self-insurance layer limit of

\$3,000,000 per occurrence, with a reinsured excess layer limit of \$12,000,000 per occurrence. Coverage includes general liability, automobile liability, stop-gap coverage, errors or omissions liability, and employee benefits liability. Claims deductibles run in levels of \$1,000 for property, and \$1,000 for automobile physical damage.

The City proactively participates in on-going training for staff regarding current practices and risk mitigation procedures in order to effectively limit claims loss exposure. Insurance coverage has been greater than claims and settlements for each of the last three years.

Note 9 – Short-term Debt

The City has no outstanding anticipation notes (other than bond anticipation notes that are accounted for as long-term debt), interest-bearing (registered or revenue) warrants, or similar contractual debt in 2009 nor were any issued during the year.

Note 10 – Long-term Debt

The City of Oak Harbor has issued general obligation and revenue bonds to finance the purchase of property and fire trucks, the expansion of the City’s Police department building, and the construction of a new fire station facility. Bonded indebtedness has also been entered into in prior years to advance refund several general obligation and revenue bonds. General obligation bonds have been issued for both general government and business-type activities and are being repaid from the applicable resources. The revenue bonds are repaid by income received from proprietary fund earnings. The City of Oak Harbor is also liable for balances due to other governments for Public Works Trust Fund (“PWTF”) loans entered into for the replacement of the City’s water transmission line, as required by the Washington State Department of Transportation.

General obligation debt currently outstanding is as follows:

Purpose	Maturity Range	Interest Rate	Original Amount	Amount of Installments
1996 GO Refunding of 1987 & 1991 GO Bonds	2010	5.85%	\$2,680,000	\$240,000
2008 OAK0361-1-1 LOCAL Bond	2012	3.42%	\$192,000	\$122,897

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

Year Ending December 31,	Governmental Activities		Business-type Activities	
	Principal	Interest	Principal	Interest
2010	\$287,912	\$17,839	\$ -	\$ -
2011	49,565	2,146	-	-
2012	25,420	435	-	-
Total	\$362,897	\$20,420	\$ -	\$ -

The revenue bonds currently outstanding are as follows:

Purpose	Maturity Range	Interest Rate	Original Amount	Amount of Installments
1996 Water & Sanitary Sewer Revenue Refunding Bonds	2011	5.75% - 5.90%	\$3,495,000	\$745,000
2004 Water & Sewer Revenue Bonds	2024	3.20% - 4.55%	\$2,865,000	\$2,295,000

Revenue bond debt service requirements to maturity are as follows:

Year Ending December 31,	Principal	Interest
2010	\$480,000	\$138,185
2011	500,000	112,970
2012	125,000	86,530
2013	130,000	82,155
2014	135,000	77,410
2015-2019	750,000	303,915
2020-2024	920,000	128,992
Total	\$3,040,000	\$930,157

Balances due to other governments currently outstanding are as follows:

Purpose	Maturity Range	Interest Rate	Original Amount	Amount of Installments
PW-05-691-PRE-106 Public Works Trust Fund Loan	2010	0.50%	\$280,500	\$4,561
PW-05-691-042 Public Works Trust Fund Loan	2025	0.50%	\$834,700	\$367,698
PW-05-691-031 Public Works Trust Fund Loan	2026	0.50%	\$2,694,500	\$482,174

Balances due to other governments debt service requirements to maturity are as follows:

Year Ending December 31,	Principal	Interest
2010	\$55,905	\$4,272
2011	51,344	3,992
2012	51,344	3,736
2013	51,344	3,479
2014	51,344	3,223
2015-2019	256,722	12,262
2020-2024	256,722	5,843
2025-2026	79,708	541
Total	\$854,433	\$37,348

In proprietary funds, unamortized debt issue costs are recorded as deferred charges and bonds are displayed net of premium or discount; annual interest expense is decreased by amortization of debt premium and increased by the amortization of debt issue costs and discount. Restricted assets in proprietary funds contain \$953,353 in reserves as required by bond indentures.

Refunded Debt

The City of Oak Harbor issued a general obligation refunding bond in 1996. Proceeds of the issue were used to perform an advance refunding of \$680,000 of the City's 1987 Unlimited Tax General Obligation Bonds; to perform an advance refunding of \$1,790,000 of the City's 1991 Unlimited Tax General Obligation Bonds; and to pay the costs of issuance of the bonds.

Note 11 – Leases and Contract Obligations

Operating Leases

The City of Oak Harbor leases office equipment with Xerox under non-cancelable operating leases. Total cost for such leases was \$63,260 for the year ending December 31, 2009. The future minimum lease payments for these leases are as follows:

Year Ending December 31	Amount
2010	\$ 30,040
2011	12,255
Total	\$ 42,295

Capital Leases

The City has no capital lease agreements and did not enter into any capital lease agreements during 2009.

Contracts

The City of Oak Harbor entered into a 6-year agreement with Island Thrift, a local non-profit charitable organization for the use of a modular building. This agreement has subsequently been extended for 6 addition years. Island Thrift donated \$125,000 to the City of Oak Harbor, \$105,000 of which was to be put towards the purchase of a modular home. In exchange for the payment, the City purchased a modular for the use of its Adult Day Care Respite program. During the 12-year period under contract, the modular will be kept on City property at 917 East Whidbey Avenue, Oak Harbor, WA, and both Island Thrift and the City of Oak Harbor hold title. At the end of the 12-year period, November 6, 2013, the City will immediately convey the modular to Island Thrift at which time Island Thrift will have 180 days to remove the modular from City property and title to the modular will be conveyed to Island Thrift.

Although the City makes no monthly or annual payments for the modular, the City has chosen to treat this agreement as capital rent for accounting purposes. The modular has been recorded at its total value and expensed over the 6-years of the original agreement.

The asset acquired through this agreement is as follows:

Asset	Governmental Activities
Respite modular	\$ 138,572
Less rent expense	(138,572)
Total	\$ -

Note 12 – Changes in Long-term Liabilities

During the year ended December 31, 2009, the following changes occurred in long-term liabilities (inclusive of both portions due within one year and due in more than one year):

	Beginning Balance 1/1/2009	Additions	Reductions	Ending Balance 12/31/2009	Due Within One Year
Governmental Activities:					
Bonds payable:					
General obligation	\$ 629,210	\$ -	\$ (266,313)	\$ 362,897	\$ 287,912
Less deferred amounts:					
For issuance discounts on refunding	-	-	-	-	-
Total bonds payable:	629,210	-	(266,313)	362,897	287,912
Compensated absences	1,089,168	99,516	(107,838)	1,080,846	432,338
Government activity long-term liabilities:	\$ 1,718,378	\$ 99,516	\$ (374,151)	\$ 1,443,743	\$ 720,250
Business-type Activities:					
Bonds payable:					
Revenue bonds	\$ 3,495,000	\$ -	\$ (455,000)	\$ 3,040,000	\$ 480,000
Less deferred amounts:					
For issuance discounts on refunding	(643)	-	202	(441)	-
Total bonds payable:	3,494,357	-	(454,798)	3,039,559	480,000
Due to other governments - PWTF loans	938,985	-	(84,552)	854,433	55,905
Payable from restricted assets (landfill closure)	70,157	-	-	70,157	-
Compensated absences	174,999	130,726	-	305,725	122,289
Business-type activity long-term liabilities	\$ 4,678,498	\$ 130,726	\$ (539,350)	\$ 4,269,874	\$ 658,194

The City of Oak Harbor's internal service funds serve both governmental and enterprise funds. Accordingly, long-term liabilities for them are included as part of the above totals for both governmental and business-type activities, based on the internal service fund's predominant customer. At year end, there were no internal service funds bonds, notes and loans payable outstanding. However, \$143,480 of internal service funds compensated absences are included in the above business-type amounts. Also, for the governmental activities, claims and judgments and compensated absences are generally liquidated by the general fund.

Note 13 – Contingencies and Litigations

The City of Oak Harbor has recorded in its financial statements all material liabilities, including an estimate for situations that have not yet resolved but where, based on available information, management believes it is probable that the City of Oak Harbor will have to make payment. In the opinion of management, the City of Oak Harbor's insurance policies and/or self-insurance reserves are adequate to pay all known or pending claims.

As discussed in Note No.10 (Long-term Debt), the City of Oak Harbor is contingently liable for repayment of refunded debt.

The City of Oak Harbor participates in a number of federal-assisted and state-assisted programs. These grants are subject to audit by the grantors or their representatives. Such audits could result in requests for reimbursement to grantor agencies for expenditures disallowed under the terms of the grants. Other than the instances described above, City of Oak Harbor management believes that such disallowances, if any, will be immaterial.

Note 14 – Restricted Net Assets

The government-wide Statement of Net Assets reports \$17,553,483 of restricted net assets, of which \$17,553,483 is restricted by enabling legislation.

Note 15 – Interfund Balances and Transfers

Interfund Balances

Due to other funds and due from other funds results from goods issued, work performed, or services rendered to or for the benefit of another fund when cash is not immediately moved between the funds. Interfund balances at December 31, 2009 were as follows:

	Due To	Due From
General	\$ 41	\$43,540
Nonmajor		
governmental	6,156	41
Water	9,868	-
Sewer	13,972	-
Solid waste	5,736	-
Storm drain	1,636	-
Marina	2,901	-
Internal service	3,271	-
Total	\$43,581	\$43,581

Interfund Transfers

The primary purpose of interfund transfers is to support the operations of other funds and contribution for capital projects. Interfund transfers at December 31, 2009 were as follows:

Transfers Out	Transfers In						Total
	General	Nonmajor Governmental	Water Reserve	Storm Drain Reserve	Marina Reserve	Internal Service	
General	\$ 150,000	\$544,004	\$ -	\$ -	\$ -	\$45,013	\$739,017
Nonmajor							
governmental	157,983	65,000	-	-	-	80,939	303,922
Water	293,111	10,000	24,000	-	-	80,939	408,050
Sewer	297,224	-	-	-	-	45,014	342,238
Solid Waste	184,658	-	-	-	-	45,014	229,672
Storm drain	168,136	-	-	25,000	-	45,014	238,150
Marina	90,927	-	-	-	25,000	-	115,927
Internal service	32,018	-	-	-	-	45,013	77,031
Total	\$1,374,057	\$619,004	\$24,000	\$25,000	\$25,000	\$386,946	\$2,454,007

Interfund Loan Activity

There were no interfund loans during 2009.

Note 16 – Receivable Balances

Major receivables of the City’s governmental and enterprise funds come from the State, Island County, and local taxpayers. Total receivables coincide with the following balance sheet line items: “Receivable (net)” and “Due from other governments”.

Receivables at December 31, 2009 were as follows:

Receivables:	Nonmajor		Water	Sewer	Solid Waste	Storm Drain	Marina	Total
	General	Governmental						
Taxes	\$194,348	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$194,348
Municipal court	1,631,130	-	-	-	-	-	-	1,631,130
Accounts Due from other governments	72	156,211	531,891	585,409	438,211	208,254	39,233	1,959,281
	911,179	-	-	-	-	1,606	8,695	921,480
Gross receivables	2,736,729	156,211	531,891	585,409	438,211	209,860	47,928	4,706,239
Less: allowance for uncollectible	(1,386,950)	-	-	-	-	-	-	(1,386,950)
Net total receivables	\$ 1,349,779	\$ 156,211	\$ 531,891	\$ 585,409	\$ 438,211	\$ 209,860	\$ 47,928	\$ 3,319,289

Total governmental activities receivables were \$1,505,990 and business-type activities receivables were \$1,813,299.

Governmental funds report deferred revenue in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period. Governmental funds also defer revenue recognition in connection with resources that have been received but not yet earned. Total governmental activities deferred revenue at December 31, 2009 was \$372,522 and business-type activities deferred revenue was \$25,604.

Note 17 – Post-retirement Benefits Other Than Pension Benefits

Other Post-employment Benefits (OPEB)

Plan Description

As required by the Revised Code of Washington (RCW) Chapter 41.26, the City provides lifetime medical care for members of the Law Enforcement Officers and Firefighters (LEOFF) retirement system hired before October 1, 1977 under a defined benefit healthcare plan administered by the City. The members necessary hospital, medical, and nursing care expenses not payable by worker’s compensation, social security, insurance provided by another employer, other pension plan, or any other similar source are covered. Most medical coverage for eligible retirees is provided by the City’s employee medical insurance program. Under the authorization of the LEOFF Disability Board, direct payment is made for other retiree medical expenses not covered by standard medical plan benefit provisions. Financial reporting for the LEOFF retiree healthcare plan is included in the City’s Comprehensive Annual Financial Report. The City currently has five participants in the LEOFF 1 system consisting of two actively employed and three retired individuals.

Funding Policy

Funding for LEOFF retiree healthcare costs is provided entirely by the City as required by RCW. The City’s funding policy is based upon pay-as-you-go financing requirements.

Annual OPEB Cost and Net OPEB Obligation

The City's annual other post employment benefit cost is calculated based upon the annual required contribution (ARC), an amount determined in accordance with the parameters of GASB Statement 45. A single retirement age of 56.24 was assumed for all active members for the purpose of determining the actuarial accrued liability (AAL) and normal cost. Retirement, disablement, termination, and mortality rates were assumed to follow the LEOFF 1 rates used in the June 30, 2007 actuarial valuation report issued by the Office of the State Actuary (SOA). Healthcare costs and trends were determined by Milliman and used by SOA in the state-wide LEOFF 1 medical study performed in 2007. The results were based on grouped data with four active groupings and four inactive groupings. The actuarial cost method used to determine the AAL was Projected Unit Credit. The AAL and net OPEB obligation (NOO) are amortized on an open basis as a level dollar over 15 years. These assumptions are individually and collectively reasonable for the purposes of this valuation.

The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal cost each year and amortize any unfunded actuarial liabilities over a period of 30 years as of January 1, 2007. The following table shows the components of the City's annual OPEB cost and the change in the City NOO. The NOO of \$254,672 is included as a noncurrent liability on the Statement of Net Assets.

	Fiscal Year Ending	
	12/31/2008	12/31/2009
Determination of annual required contribution		
Normal costs at year end	\$20,563	\$20,617
Amortization of unfunded actuarial accrued liabilities (UAAL)	149,029	144,499
Annual required contribution (ARC)	\$169,592	\$165,116
Determination of net OPEB obligation (NOO)		
Annual required contribution	\$169,592	\$165,116
Interest on NOO	-	5,548
Adjustments to ARC	-	(11,480)
Annual OPEB cost	169,592	159,184
Contribution	(46,303)	(27,801)
Increase (decrease) in NOO	123,289	131,383
NOO - beginning	-	123,289
NOO - ending	\$123,289	\$254,672

Funded Status and Funding Progress

The City's OPEB cost, the percentage of OPEB cost contributed to the plan and the net OPEB obligation were as follows:

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligations
12/31/2008	\$169,592	27.30%	\$123,289
12/31/2009	159,184	17.46%	254,672

As of January 1, 2009, the most recent actuarial valuation date, the plan was 0% funded. The City's actuarial value of assets, accrued liability, UAAL, covered payroll and UAAL as a percentage of covered payroll was as follows:

Fiscal Year Ended	Actuarial Value of Assets	Actuarial Accrued Liability	UAAL	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
12/31/2008	\$ -	\$1,600,503	\$1,600,503	0.00%	\$181,843	880.16%
12/31/2009	-	1,551,851	1,551,851	0.00%	185,436	836.87%

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multi-year trend information that shows whether the actuarial value of the plan assets is increasing or decreasing over time relative to the actuarial liabilities for benefits.

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities, consistent with the long-term perspective of the calculations.

In the January 1, 2008 actuarial valuation, the entry age normal actuarial cost method was used. The actuarial assumptions used included a 5.50% discount rate, which is based upon the long-term investment yield on the investments that are expected to be used to finance payment of benefits. A medical inflation rate of 9%, graded to 5% over eight years was used along with a long term care inflation rate of 4.5%. The UAAL is being amortized over a thirty year period on a closed basis at the assumed discount rate.

Note 18 – Closure and Post Closure Care Costs

The City landfill ceased to receive solid waste as of 1980. From 1980 to present, the City Engineering Department has conducted extensive monitoring of ground water and gas expulsion. The City has prepared a landfill closure plan, conducted Phase I during 1993, and successive Phases implemented throughout 2003. In compliance with GASB Statement 18, the City of Oak Harbor has identified its remaining landfill closure liability to be approximately \$70,157 (the total estimated liability of \$800,000 less accumulated closure costs of \$729,843). This represents an estimate of the expected liability. Inflation, changes in technology, and closure regulations may affect this estimate.

Note 19 – Other Disclosures

Accounting and Reporting Changes

In prior years, 100% of all internal service fund assets and liabilities were allocated to the governmental activities column of the Statement of Net Assets, with Internal Service fund revenues and expenses being allocated into both the governmental and business-type columns of the Statement of Activities based on the percentage of aggregate cash being held for each reporting entity type. For 2009, the City has changed the allocation method used to consolidate internal service fund financial data for government-wide financial statement reporting purposes. Using internal revenues as the measurement basis, each internal service fund operation has been analyzed to determine if the primary service provided by the fund was either governmental or business-type in nature. Based on this analysis, the assets; liabilities; and external revenues and expense of each fund have been consolidated, in their entirety, into the

appropriate activity type column. Accordingly, an adjustment for the cumulative net asset effect of this change in allocation method has been made to the beginning net asset balance of each reporting entity type. The adjustment has resulted in the beginning balances of net assets of the governmental activities column being reduced, with the net assets of the business-type activities column being increased by \$9,070,914. This reciprocal effect of this adjustment represents the shifting of some of the internal service net asset balances from governmental activities to business-type activities.

Subsequent Events

In 1987, the City entered into a 50-year license agreement with the U.S. Navy to utilize certain sanitary sewer treatment facilities located on Navy property. During 2002, the Department of Defense entered in negotiations with the City of Oak Harbor to privatize the treatment of its sewer system aboard the Whidbey Island Naval Air Station. Discussion is still on-going in 2010 regarding sewage treatment options for military infrastructure.

On September 7, 2010 the City awarded a contract for the Marina dredging to Northwest Marine. The amount of this contract was a \$1,893,794.



ABOUT THE STATE AUDITOR'S OFFICE

The State Auditor's Office is established in the state's Constitution and is part of the executive branch of state government. The State Auditor is elected by the citizens of Washington and serves four-year terms.

Our mission is to work in cooperation with our audit clients and citizens as an advocate for government accountability. As an elected agency, the State Auditor's Office has the independence necessary to objectively perform audits and investigations. Our audits are designed to comply with professional standards as well as to satisfy the requirements of federal, state, and local laws.

The State Auditor's Office employees are located around the state to deliver our services effectively and efficiently.

Our audits look at financial information and compliance with state, federal and local laws on the part of all local governments, including schools, and all state agencies, including institutions of higher education. In addition, we conduct performance audits of state agencies and local governments and fraud, whistleblower and citizen hotline investigations.

The results of our work are widely distributed through a variety of reports, which are available on our Web site and through our free, electronic subscription service. We continue to refine our reporting efforts to ensure the results of our audits are useful and understandable.

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