

**CITY OF COVINGTON, KENTUCKY**  
**COMPREHENSIVE ANNUAL FINANCIAL REPORT**  
**YEAR ENDED JUNE 30, 2012**

Prepared by:  
Robert J. Due  
Finance Director

# CITY OF COVINGTON, KENTUCKY

## Comprehensive Annual Financial Report

Year Ended June 30, 2012

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**INTRODUCTORY  
SECTION**



**CITY OF COVINGTON**  
Office of the City Manager

**Administration** OFFICE OF THE CITY MANAGER  
**Code**  
**Enforcement** December 31, 2012  
**Community**  
**Development**  
**Finance** To the Mayor, City Commissioners and Citizens of the City of Covington, Kentucky:  
**Fire**  
**Human Resources** Formal Transmittal of the Comprehensive Annual Annual Report (CAFR)  
**Legal**  
**Neighborhoods,** State law requires that all general-purpose local governments publish within six months of the  
**Parks and** close of each fiscal year a complete set of financial statements presented in conformity with  
**Recreation** generally accepted accounting principles (GAAP) in accordance with the implementation of  
**Police** Government Standards Board (GASB) Statement 34, and audited in accordance with  
**Public** generally accepted auditing standards by an independent firm of licensed certified public  
**Improvements** accountants. Pursuant to that requirement, we hereby issue the comprehensive annual  
**Section 8 Housing** financial report of the City of Covington for the fiscal year ended June 30, 2012.  
**Choice Voucher**

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

To the best of our knowledge and belief, this financial report is complete and reliable in all material respects and fairly presents the financial position and results of the operations of the various funds and component units of the City. All disclosures necessary to enable the reader to gain an understanding of the City's financial activities have been included in this report.

The City of Covington's financial statements have been audited by Decosimo, Certified Public Accountants, a firm of licensed certified public accountants with a local office in Cincinnati, Ohio. The goal of the independent audit was to provide reasonable assurance that the financial statements of the City of Covington for the fiscal year ended June 30, 2012, are free of material misstatement. The independent audit involved examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; assessing the accounting principles used and significant estimates made by management; and evaluating the overall financial statement presentation. The independent auditor concluded, based upon the audit, that there was a reasonable basis for rendering an unqualified opinion that the City of Covington's financial statements for the fiscal year ended June 30, 2012, are fairly presented in conformity with GAAP. The independent auditor's report is presented as the first component of the financial section of this report.

The independent audit of the financial statements of the City of Covington was a part of a broader, federally mandated "Single Audit" designed to meet the special needs of federal grantor agencies. The standards governing Single Audit engagements require the independent auditor to report not only on the fair presentation of the financial statements, but also on the audited government's internal controls and compliance with legal requirements, with special emphasis on internal controls and legal requirements involving the administration of Federal awards. These reports are available in the City of Covington's Single Audit report.

GAAP requires that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with it. The City of Covington's MD&A can be found immediately following the report of the independent auditors.

#### Profile of the Government

The City of Covington, founded in 1815, is located in the northern most part of the state, situated in Kenton County and is part of the Northern Kentucky Region, which ranks as one of the top growth areas in Kentucky. The City of Covington currently occupies a land area of 13.1 square miles and serves an estimated population of 40,640 based on the 2010 U.S. Census. The City of Covington is empowered to levy numerous taxes and fees. Its major revenue sources include an occupational license tax levied on gross wages and net profits of businesses, an insurance premiums tax and a property tax on both real and personal properties.

The City of Covington operates under the City Manager form of government. Legislative authority is vested in the City Board of Commissioners, consisting of the Mayor and four City Commission members. The Board of Commissioners is responsible for among other tasks, passing ordinances, adopting the budget, appointing members to various boards, and it approves the hiring of all full time employees. The City Manager reports directly to the Board of Commissioners and is responsible for carrying out policies and ordinances of the City Board of Commissioners and is responsible for the development of short and long range planning, capital improvement programs, and running the day-to-day operations of the City. The City Board of Commissioners is elected on a non-partisan basis. The Mayor serves a four year term and the City Commissioners serve two year terms. The next election for the Board of Commissioners will be held in November of 2014 and for the Mayor in November of 2016. The new Mayor and City Commission win take office on January 1, 2013. The election for the new Mayor and City Commissioners took place in November of 2012

The City of Covington provides a full range of services including a full time professional police service and full time professional: fire service; advanced life support emergency services; street maintenance and improvement; waste collection services; a full range of recreational areas and activities; cultural events; planning and zoning; housing rehabilitation and development; and public nuisance and zoning code enforcement. In addition to these activities, the governing body is responsible for funding the Employees' Retirement Fund and the Police and Firemen's Retirement Funds.

The annual budget serves as the foundation for the City of Covington's financial planning and control. Budget targets are set for each city department based on current revenue estimates contained in the five year plan adjusted for current trends. All departments of the City of Covington are required to submit budget requests for appropriation to the City Manager. The budget requests must be within budget targets. The City Manager uses these requests as the starting point for developing a proposed balanced budget. The City Manager then presents the

proposed balanced budget to the City Commissioners for review. A structurally balanced budget is required by State law and the Kentucky Constitution. The final budget is adopted prior to July 1 of each year. The appropriated budget is prepared by fund and department (e.g., police). Department heads may make transfers of appropriations within a department with the approval of the City Manager, or his designee. The City Manager cannot make transfers of appropriations between funds without the approval of the City Commissioners. Expenditures may not legally exceed budgeted appropriations at the fund level. Any revisions to the budget that would alter total revenues and total expenditures of any fund must be approved by the City Commissioners. Budget-to-actual comparisons are provided in this report for each individual governmental fund for which an appropriated annual budget has been adopted. For the general fund, this comparison is presented on pages 62-64 as part of the basic financial statements for the governmental funds. For governmental funds with appropriated annual budgets other than the general fund, this comparison is presented in the governmental fund subsection of this report, which starts on page 65. Also included in the governmental fund subsection are project-length budget-to-actual comparisons for each governmental fund for which a project-length budget has been adopted (i.e., the capital projects funds).

#### Information Useful in Assessing the Economic Condition

The information presented in the financial statements is perhaps best understood when it is considered from the broader perspective of the environment within which the City of Covington operates.

**Local Economy:** The City of Covington has maintained its efforts in developing economic resources in the Greater Cincinnati/Northern Kentucky region. The consistent and persistent effort put forth by Covington's elected and appointed officials and other community leaders over the past twenty years has positioned the City for economic growth in the foreseeable future. According to the 2013 Regional Economic Outlook published by the Northern Kentucky Chamber of Commerce, the recovery has been painfully slow. "Both 2011 and 2012 have been marked by slow growth, stubborn unemployment, a slow recovery in the housing market." Employment growth and a reduction in the unemployment rate is still the most important issue facing the economy over the coming years. The local Chamber of Commerce's Economic Advisory Committee consensus forecast predicts continued slow recovery and a slight drop in the unemployment rate from 7.5% to 7.2%.

The City is heavily reliant on economically sensitive revenue. Occupational license fees (payroll tax and net profit taxes) represent 54.7% of all General Fund Revenue. Detailed information can be found in the Management Discussion & Analysis in the Financial Section of this report.

With the reality of little if no growth in economically sensitive revenue and a potential \$20 million shortfall over the next five years, the City planned and implemented a financial recovery plan which began in fiscal year 2013. The plan included the successful negotiation of three collective bargaining agreements with major changes in health care plan design that require greater employee participation in cost sharing, and requiring spouses of employees who are employed and eligible for health insurance coverage with their employer to leave the City's plan and enroll with their respective employers' plans. The agreements will extend through the end of calendar year 2015. Resultant savings will eliminate one half of the \$20 million five year shortfall. The City also relinquished 911 Emergency Dispatch Services to Kenton County. The savings will exceed \$1 million per year. The City will also reduce its payroll tax withholding rate from 2.5% to 2.45% of gross wages effective January 1, 2013, as an inducement to retain and recruit businesses and employers and make the City more competitive with Cincinnati, Louisville, and Lexington. The City's payroll tax rate has remained unchanged since its adoption in 1966.



The final element of the financial recovery plan was a comprehensive review of City operations with an eye toward streamlining processes and taking advantage of the technology available to reduce costs. Full Time Equivalent positions have fallen from 376 in fiscal year 2011 to less than 340 in fiscal year 2013. The impact of this financial recovery plan will not be reflected until the fiscal year 2013 Comprehensive Annual Financial Report.

A new emphasis on reinvestment in infrastructure and economic development have not only stabilized the City's financial status but provided resources to replenish depleted fund balances, jump start reinvestment in infrastructure, and economic development efforts. Two major development projects have recently been announced. A Covington-based business and real-estate investment company, partnering with a proven hotel developer, announced plans to develop a \$25 million destination luxury boutique hotel in a building that now serves as Covington City Hall. The 102 year old building that was formerly a department store will be transformed into a 107 room luxury hotel with a signature restaurant and bar. The hotel's design will blend the historical and architectural uniqueness of the structure with modern-day amenities of a luxury hotel. The project will attract new development, investment, businesses, and visitors to the downtown business district. The same developer has also acquired other properties in close proximity to the hotel project to optimize the impact of their primary investment.

Gateway Community & Technical College (GCTCS), a state funded institution of higher education, plans an ambitious \$81.5 million urban campus. In November of 2012, GCTCS announced the acquisition of more than a half dozen properties in the City's central business district to complement their existing campus and to provide the physical space for their planned expansion of a distributed urban campus in the City's urban core.

Two existing businesses expanded during fiscal year 2012. Plaza Recovery and Tier One both received state and local incentives to remain and grow new jobs in Covington. Plaza Recovery is a new entity but its predecessor, ACB American, has a record of jobs expansion in the City. Plaza Recovery, a debt recovery business with a national clientele, will add 250 new jobs. Tier One, an existing information technology company with a national clientele, opted to remain in Covington and continue its growth in the training and education software development industry.

Life science and technology based industries have been targeted in the City's economic development strategy. Bexion Pharmaceutical, a life science start-up, is also expanding and adding new jobs as well as providing space for other life science start-ups. Covington Latin School completed a \$9.9 million expansion which completely transformed the 87 year old school. The 41,000 square foot addition includes three college level science classrooms/labs, a technology center, a new cafeteria, and dedicated space for physical education and multi-purpose use. The majority of students come from outside the City of Covington. The City was pleased with the school's commitment to the community and the decision to stay in the City urban core. The expansion is featured on the cover of this Comprehensive Annual Financial Report.

#### Financial Policies and Planning

This report has been prepared in compliance with the requirements of Government Accounting Standards Board (GASB) No. 54. The goal of GASB 54 is to report governmental fund balances based on a hierarchy that shows from the highest to the lowest, the level or form of constraints on fund balances and, accordingly, the extent to which governments are bound to honor those constraints. GASB No. 54 also clarified the definition of a Special Revenue Fund. A Special Revenue Fund should not be reported unless one or more specific restricted or committed revenues are the foundation.


## Awards and Acknowledgements

The Government Finance Officers Association (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the City for its comprehensive annual financial report for the fiscal year ended June 30, 2011. This was the nineteenth consecutive year that the City has received this prestigious award. In order to be awarded a Certificate of Achievement, the City published an easily readable and efficiently organized comprehensive annual financial report. This report satisfied both generally accepted accounting principles and applicable legal requirements.

The preparation of this comprehensive annual financial report on a timely basis was made possible by the dedicated service of the entire staff of the Department of Finance. Each member has our sincere appreciation for the contributions made in the preparation of this report. We also acknowledge the efforts of other departments who provided information that helped to make the report far more than a presentation of numbers, with a special thanks to Decosimo & Company. Credit must also be given to the Mayor and Commissioners for their unfailing interest, support, and integrity in directing the City's financial operations.

Respectfully submitted,

  
Larry Klein  
City Manager

  
Robert J. Due  
Finance Director

# Certificate of Achievement for Excellence in Financial Reporting

Presented to

City of Covington  
Kentucky

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
June 30, 2011

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



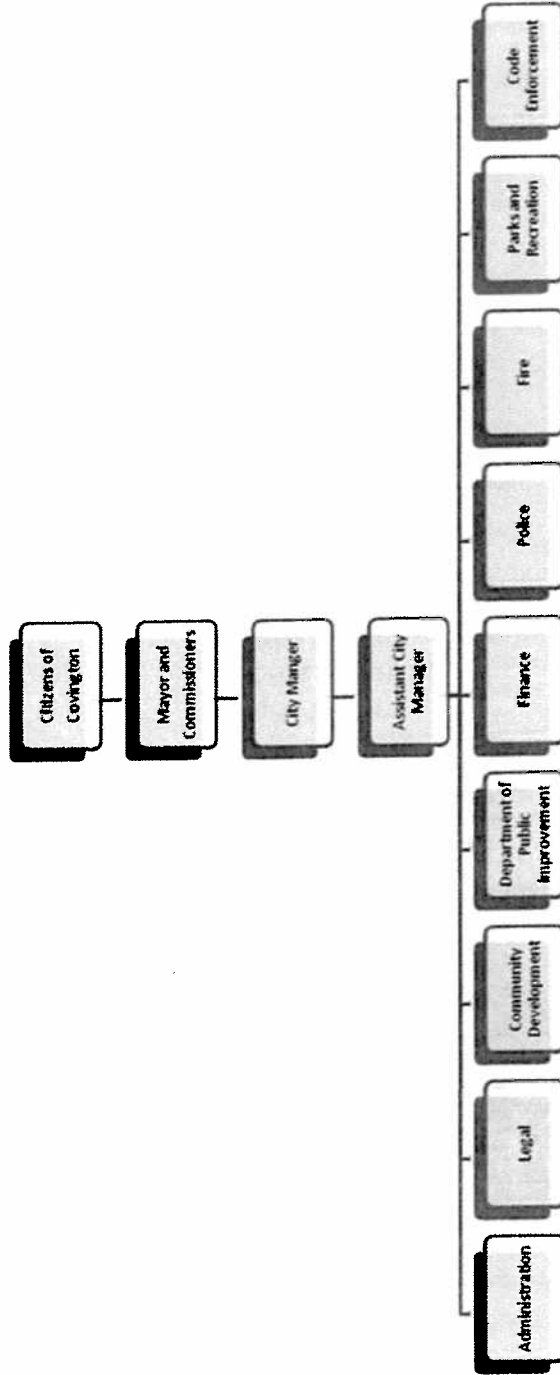
*Linda C. Danison*

President

*Jeffrey R. Enser*

Executive Director

**CITY OF COVINGTON, KENTUCKY  
ORGANIZATIONAL CHART**



**CITY OF COVINGTON, KENTUCKY**

**LIST OF PRINCIPAL OFFICIALS**

**June 30, 2012**

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**MAYOR**

Chuck Scheper

**COMMISSIONERS**

Sherry Carran

Shawn Masters

Steve Casper

Steve Frank

**STAFF**

City Manager - Larry Klein

Assistant City Manager - Larisa Sims

City Solicitor - Frank Warnock

City Clerk - Maggie Nyhan

Finance Director - Robert J. Due

Chief of Police - Lee Russo

Fire Chief - Chuck Norris

Director of Public Improvements/City Engineer - Tom Logan

Community Development Director - Jackson Kinney

Director of Code Enforcement - Keith Bales

Recreation Director - Natalie Gardner

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**FINANCIAL SECTION**

**REPORT OF INDEPENDENT ACCOUNTANTS**

To the Mayor and Council  
Board of Commissioners  
City of Covington, Kentucky

We have audited the accompanying financial statements of the governmental activities, the aggregate discretely presented component unit, each major fund, and the aggregate remaining fund balance information of the City of Covington, Kentucky (the City), as of and for the year ended June 30, 2012, which collectively comprise the City's basic financial statements, as listed in the table of contents. 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 did not audit the financial statements of Devou Properties, Inc. (a non-profit organization), the discretely presented component unit. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for Devou Properties, Inc., is based on the report of the other auditors.

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. The financial statements of Devou Properties, Inc. were not audited in accordance with *Government Auditing Standards*. 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, based on our audit and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the aggregate discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Covington, Kentucky, as of June 30, 2012, and the respective changes in its financial position and its cash flows, where applicable, thereof for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

As described in Note 2 to the financial statements, the City's net asset balances as of June 30, 2011, have been adjusted to correct errors in classification. Our opinion is not modified with respect to that matter.

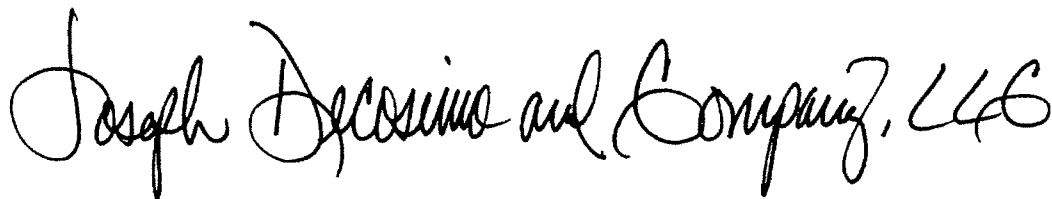
In accordance with *Government Auditing Standards*, we have also issued our report dated December 31, 2012, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and 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.



Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 12 through 21 and 58 through 63, respectively, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Covington, Kentucky's basic financial statements. The other supplementary information as listed in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements. The schedule of expenditures of federal awards is presented for the purpose of additional analysis as required by the U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements. The other supplementary information and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the other supplementary information and the schedule of expenditures of federal awards are fairly stated in all material respects in relation to the financial statements as a whole.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Covington, Kentucky's basic financial statements. The introductory section and statistical section are presented for purposes of additional analysis and are not required parts of the basic financial statements. The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

A handwritten signature in black ink that reads "Joseph Decosimo and Company, LLC". The signature is written in a cursive, flowing style.

Cincinnati, Ohio  
December 31, 2012

# CITY OF COVINGTON, KENTUCKY

## MANAGEMENT'S DISCUSSION AND ANALYSIS

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The Management Discussion and Analysis (MD&A) of the City of Covington, Kentucky's (the City's) financial statements provides readers an overview and analysis of the City's financial position and activities for the fiscal year ended June 30, 2012. The information presented here should be read in conjunction with the City's basic financial statements which immediately follow this analysis.

### USING THIS ANNUAL REPORT

This annual report consists of a series of financial statements. The Statement of Net Assets and the Statement of Activities (on pages 23 and 24) provide information about the activities of the City as a whole and present a longer-term view of the City's finances. Fund financial statements start on page 25. For governmental activities, these statements tell how these services were financed in the short term as well as what remains for future spending. Fund financial statements also report the City's operations in more detail than the government-wide statements by providing information about the City's most financially significant funds.

This report was published under the standards for governmental financial reporting prescribed by the Governmental Accounting Standards Board in their Statement No. 34 (GASB 34). The GASB 34 model is designed to provide improved information through the elimination of fund transfers and the use of consolidated statements. This model is found in the government-wide financial statements.

### Financial Highlights

The assets of the City exceeded its liabilities at the close of the most recent year by \$46,206,205 (net assets), and represent a decrease of \$(1,738,480) from the prior year. This amount includes \$34,173,497 that is invested in capital assets net of related debt and an unrestricted deficit balance of \$(4,806,437). The remaining net assets of \$190,681 and \$16,648,464 are restricted for Capital Projects and HUD Programs, respectively.

As of the close of the current fiscal year, the City's governmental funds reported a combined ending fund balance of \$3,292,864, a change of \$(1,902,263) from the previous year. Following GASB Statement Number 54, the total combined fund balance is \$3,292,864 and consists of \$98,617 as nonspendable, \$1,765,575 as restricted, \$385,496 as committed and \$1,043,176 as unassigned.

### Government-Wide Financial Statements

Government-Wide financial statements include the Statement of Net Assets and the Statement of Activities. These statements utilize the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. Accrual accounting means the financial statements recognize revenue when it is earned and expense when it is incurred regardless of when the cash is actually received or paid.

The Statement of Net Assets presents information on all City assets and liabilities as of June 30, 2012. Net assets are the difference between the assets and liabilities. Over time, increases or decreases in the City's net assets are one indicator of whether its financial health is improving or deteriorating. In assessing the City's condition, other factors must be considered as well, such as changes in the City's property tax base, occupational license tax base, and the condition of the City's capital assets (roads, buildings, equipment, and sidewalks) to assess the overall health of the City.

# CITY OF COVINGTON, KENTUCKY

## MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

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The Statement of Activities presents the City's annual revenues and expenses as well as any other transactions that increase or decrease net assets. Program revenues are offset by program expenses in order to provide net program costs that are financed by general government revenues.

The government-wide statements divide the City functions into two kinds of activities:

- **Governmental activities:** Most of the City's basic services are reported here, including police, fire, street maintenance, parks and recreation, and general administration services. Payroll occupational license fees, property taxes, and net profit license fees, and insurance premiums license tax, and service charges finance most of these activities.
- **Component Unit:** Devou Properties Inc. was formed to maintain and operate the Drees Pavilion at Devou Memorial Overlook for the benefit of Devou Park which is owned by the City. Although a legally separate entity, Devou Properties is included in these financial statements because of its financial accountability to the City.

### **Fund Financial Statements**

Fund financial statements report the City's operations in more detail than the government-wide statements. The analysis of the City's major funds begins on page 58. The non-major fund financial statements begin on page 66. Some funds are required to be established by State law or by bond covenants. However, the City Commission may establish many other funds to help control and manage money for particular purposes (i.e., Police Forfeiture Fund, Devou Park Maintenance Fund, Devou Park Master Plan Fund, etc.) or to show that it is meeting legal responsibilities for grant funds (i.e. Community Development Block Grant Fund, Housing Voucher Fund, HOME Program Fund, etc.). The City reports financial activity under three kinds of funds: governmental, proprietary and fiduciary.

*Governmental funds:* Most of the City's basic services are reported in governmental funds, which focus on how money flows into and out of those funds and the balances left at year-end that are available for spending. These funds are reported using an accounting method called modified accrual accounting, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund statements provide a detailed short-term view of the City's general government operations and the basic services it provides. Governmental fund information helps determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs. The relationship (or differences) between governmental activities (reported in the Statement of Net Assets and the Statement of Activities) and governmental funds is described in a reconciliation (Reconciliation of the Balance Sheet - Governmental Funds to the Statement of Net Assets (page 26) and the Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balance - Governmental Funds to the Statement of Activities (page 28)) attached to the fund financial statements. The City considers the General Fund, Community Development Block Grant Fund, HOME Program Fund and Housing Voucher Program to be major governmental funds.

*Proprietary funds:* When the City charges customers for the full cost of the services it provides whether to outside customers or to other units of the City, these services are reported in proprietary funds. The subcategories of the funds include enterprise funds, which are business-type activities and internal service funds, which report services provided to internal units of government. Proprietary funds are reported in the same way that all activities are reported in the Statement of Net Assets and the Statement of Activities. The City has no enterprise funds and reports two internal service funds, the Liability Self Insurance Fund and the Medical and Dental Self Insurance Fund.

**CITY OF COVINGTON, KENTUCKY**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)**

*Fiduciary funds:* Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the City of Covington's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds. The City is trustee, or fiduciary for two retirement funds. The Police and Firemen's Pension Fund is a closed pension that is held solely for trust beneficiaries. The Employees' Retirement fund has two active employee members and is also held solely for trust beneficiaries.

**Statement of Net Assets**

For the year ended June 30, 2012, net assets changed as follows:

|   | <b>Governmental<br/>Activities<br/>2012</b> | <b>Governmental<br/>Activities<br/>2011</b> | <b>Increase<br/>(Decrease)<br/>from 2011</b> |
|---|---|---|--|
| Current and other assets                | \$ 29,528,713                               | \$ 30,702,886                               | \$ (1,174,173)                               |
| Capital assets                          | 56,255,259                                  | 57,755,623                                  | (1,500,364)                                  |
| Other non-current assets                | <u>4,143,087</u>                            | <u>6,198,385</u>                            | <u>(2,055,298)</u>                           |
| Total assets                            | <u>89,927,059</u>                           | <u>94,656,894</u>                           | <u>(4,729,835)</u>                           |
| Current liabilities                     | 11,802,988                                  | 11,123,949                                  | 679,039                                      |
| Non-current liabilities                 | <u>31,917,866</u>                           | <u>35,588,260</u>                           | <u>(3,670,394)</u>                           |
| Total liabilities                       | <u>43,720,854</u>                           | <u>46,712,209</u>                           | <u>(2,991,355)</u>                           |
| Net Assets:                             |   |   |  |
| Invested in capital assets, net of debt | 34,173,497                                  | 36,088,303                                  | (1,914,806)                                  |
| Restricted for capital projects         | 190,681                                     | 1,577,223                                   | (1,386,542)                                  |
| Restricted for HUD Programs             | 16,648,464                                  | 15,837,661                                  | 810,803                                      |
| Restricted for police                   | -   | 3,321                                       | (3,321)                                      |
| Restricted for grants                   | -   | 24,040                                      | (24,040)                                     |
| Unrestricted                            | <u>(4,806,437)</u>                          | <u>(5,585,863)</u>                          | <u>779,426</u>                               |
| Total net assets                        | <u>\$ 46,206,205</u>                        | <u>\$ 47,944,685</u>                        | <u>\$ (1,738,480)</u>                        |

The total assets of the City on June 30, 2012, were \$89,927,059, while total liabilities were \$43,720,854, resulting in net assets of \$46,206,205. The largest component of the City's net assets, \$34,173,497, or 73.9%, reflects its investment in capital assets. Specific restrictions of net assets have been captured in the 2012 Statement of Net Assets.

As more fully disclosed in Note 2 to the financial statements, Net Assets as of June 30, 2011, have been adjusted for misclassifications. Restricted for HUD Programs net assets were increased by \$14,519,093 and unrestricted net assets were decreased by \$14,519,093. Total net assets did not change but the components of the June 30, 2011, net assets were modified. U.S. Department of Housing & Urban Development (HUD) funded activities previously had been reflected as unrestricted net assets rather than as restricted net assets.

The underlying restricted assets consist of notes issued from HUD funds for first time homebuyer down payment assistance and home rehabilitation loans. Other notes have also been issued by City for economic development purposes to create jobs. As of June 30, 2012, notes receivable on the Statement of Net Assets are \$16,843,635 of which \$14,901,780 are HUD funded. Management's analysis determined that since repayment of the notes by regulation must be reported to HUD and used for HUD purposes, that the resources, when recognized on the Statement of Net Assets, should be restricted rather than classified as unrestricted, resulting in the correction to the opening June 30, 2011, Net Assets.

# CITY OF COVINGTON, KENTUCKY

## MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

The total decrease in net assets of \$1,738,480 is reflective of the City's plan to first structurally balance the budget and stabilize the financial position before implementing plans to reinvest in infrastructure. In that sense, fiscal year 2012 will serve as the spring board for capital investment and economic growth in the future. After a number of years of declining capital investment, fiscal years 2012 and 2011, marked initial steps in addressing the long term infrastructure needs of the City.

### Statement of Activities

|                                    | Governmental<br>Activities<br>2012 | Governmental<br>Activities<br>2011 | Increase<br>(Decrease)<br>from 2011 |
|------------------------------------|------------------------------------|------------------------------------|-------------------------------------|
| Revenues:                          |                                    |                                    |                                     |
| Program revenues:                  |                                    |                                    |                                     |
| Charges for services               | \$ 6,669,237                       | \$ 6,091,457                       | \$ 577,780                          |
| Operating grants and contributions | 12,518,909                         | 13,533,951                         | (1,015,042)                         |
| Capital grants                     | 1,647,156                          | 2,558,805                          | (911,649)                           |
| General revenues:                  |                                    |                                    |                                     |
| Taxes                              | 40,538,696                         | 40,174,583                         | 364,113                             |
| Interest                           | 23,084                             | 47,503                             | (24,419)                            |
| Other                              | <u>2,286,030</u>                   | <u>1,817,908</u>                   | <u>468,122</u>                      |
| Total revenues                     | <u>63,683,112</u>                  | <u>64,224,207</u>                  | <u>(541,095)</u>                    |
| <b>EXPENSES</b>                    |                                    |                                    |                                     |
| General government                 | 4,250,735                          | 3,814,055                          | 436,680                             |
| Police                             | 16,455,964                         | 16,536,402                         | (80,438)                            |
| Fire                               | 15,180,999                         | 15,318,421                         | (137,422)                           |
| Public improvements                | 11,349,786                         | 11,780,808                         | (431,022)                           |
| Recreation                         | 711,584                            | 734,672                            | (23,088)                            |
| Community development              | 15,379,018                         | 13,771,124                         | 1,607,894                           |
| Parking garage                     | 768,661                            | 865,947                            | (97,286)                            |
| Interest on long-term debt         | <u>1,324,845</u>                   | <u>1,676,776</u>                   | <u>(351,931)</u>                    |
| Total expenses                     | <u>65,421,592</u>                  | <u>64,498,205</u>                  | <u>923,387</u>                      |
| Change in net assets               | (1,738,480)                        | (273,998)                          | (1,464,482)                         |
| Net assets - June 30, 2011         | <u>47,944,685</u>                  | <u>48,218,683</u>                  | <u>(273,998)</u>                    |
| Net assets - June 30, 2012         | <u>\$ 46,206,205</u>               | <u>\$ 47,944,685</u>               | <u>\$ (1,738,480)</u>               |

Revenues for the City's governmental activities were \$63,683,112 for 2012, a change of \$(541,095) from the prior year. Taxes which include occupational license fees, property taxes, insurance premiums taxes, and net profit taxes comprise 63.7% of total revenue in fiscal year 2012. The \$364,113 (0.91%) increase in taxes is important. The increase, although modest, is the first time in the past three years that taxes have increased from the previous year.

Operating grants and contributions as well as capital grants both realized a drop off in revenue from the previous year. Federal stimulus money reached its peak in previous fiscal year and will continue to decrease as stimulus funds are fully spent.

Total expenses for the City's governmental activities were \$65,421,592 for 2012, a 1.43% increase from the prior year. Increases in health care costs as well as pension costs exceeded the budget reductions expected to be realized during the fiscal year.

**CITY OF COVINGTON, KENTUCKY**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)**

**Fund Financial Statements**

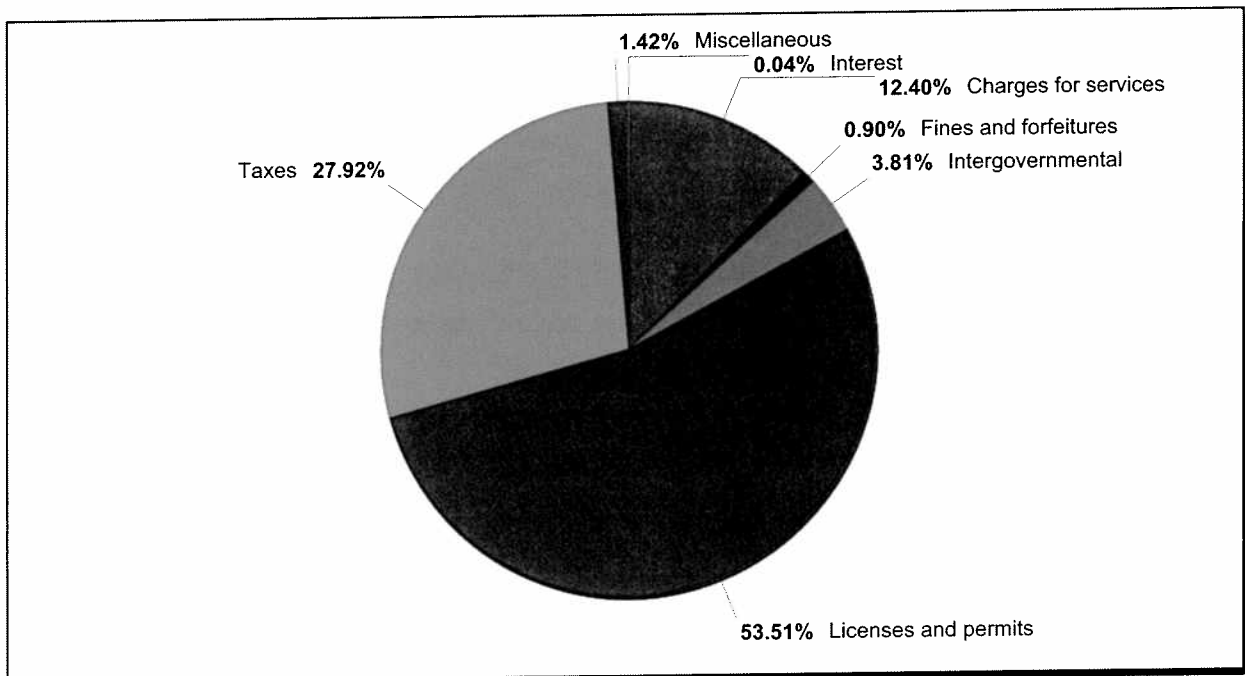
**GENERAL FUND**

The following schedules and charts present a summary of the General Fund revenues and expenditures for the fiscal year ended June 30, 2012, and the amount and percentage of increases and decreases in relation to the prior year.

| <b>Revenues</b>       | <b>FYE 2012<br/>Amount</b> | <b>Percent of Total</b> | <b>Increase<br/>(Decrease) from<br/>FYE 2011</b> | <b>Percent Increase<br/>(Decrease)</b> |
|-----------------------|----------------------------|-------------------------|--|--|
| Taxes                 | \$ 13,657,232              | 27.92 %                 | \$ (148,928)                                     | (1.08)%                                |
| Licenses and permits  | 26,175,310                 | 53.51 %                 | 813,055  | 3.21 %                                 |
| Intergovernmental     | 1,862,791                  | 3.81 %                  | 210,175  | 12.72 %                                |
| Fines and forfeitures | 439,189                    | 0.90 %                  | (119,276)  | (21.36)%                               |
| Charges for services  | 6,063,323                  | 12.40 %                 | 668,975  | 12.40 %                                |
| Interest              | 21,948                     | 0.04 %                  | (23,937)   | (4.29)%                                |
| Miscellaneous         | 695,022                    | 1.42 %                  | 79,161   | 172.52 %                               |
| <b>Total revenues</b> | <b>\$ 48,914,815</b>       | <b>100.00 %</b>         | <b>\$ 1,479,225</b>                              | <b>3.12 %</b>                          |

Taxes which include real estate taxes, personal property taxes, and insurance premiums taxes decreased \$(148,928). Total taxable assessed value decreased \$23.1 million for a total taxable assessed value of \$2.1 billion. Occupational License revenue includes both a payroll occupational license fee and a net profit occupational license fee on businesses. Licenses and permits increased by \$813,055 or 3.21% from the prior fiscal year and are expected to remain relatively flat into the next fiscal year. With revenue growth between 2.52% and 3.21% over the past fiscal years, there will be increasing pressure to further cap or reduce operating expenses.

**2012 General Fund Revenues**

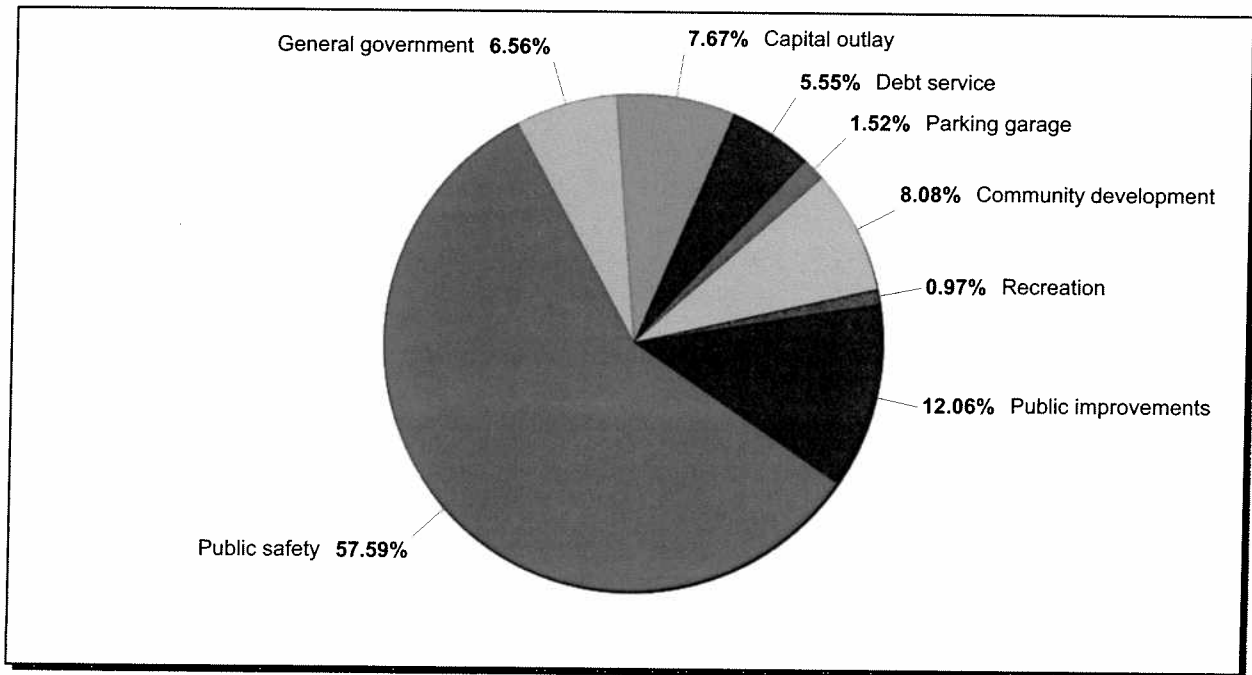


**CITY OF COVINGTON, KENTUCKY**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)**

Expenditures increased from the prior year by 1.69%, or \$811,652.

| <b>Expenditures</b>   | <b>FYE 2012<br/>Amount</b> | <b>Percent<br/>of Total</b> | <b>Increase<br/>(Decrease) from<br/>FYE 2011</b> | <b>Percent<br/>Increase<br/>(Decrease)</b> |
|-----------------------|----------------------------|-----------------------------|--|--|
| General government    | \$ 3,207,768               | 6.56 %                      | \$ 87,881  | 2.82 %                                     |
| Public safety         | 28,143,840                 | 57.59 %                     | (301,590)  | (1.06)%                                    |
| Public improvements   | 5,891,702                  | 12.06 %                     | (377,181)  | (6.02)%                                    |
| Recreation            | 475,601                    | 0.97 %                      | 20,389   | 4.48 %                                     |
| Community development | 3,947,945                  | 8.08 %                      | 198,495  | 5.29 %                                     |
| Parking garage        | 743,506                    | 1.52 %                      | (122,441)  | (14.14)%                                   |
| Debt service          | 2,712,239                  | 5.55 %                      | 354,582  | 15.04 %                                    |
| Capital outlay        | <u>3,743,244</u>           | <u>7.67 %</u>               | <u>951,517</u>                                   | <u>34.08 %</u>                             |
| Total expenditures    | <u>\$ 48,865,845</u>       | <u>100.00 %</u>             | <u>\$ 811,652</u>                                | <u>1.69 %</u>                              |

**2012 General Fund Expenditures**



Capital outlay represents the largest increase in expenditures over the prior year. Approximately \$1.5 million in unspent proceeds from taxable General Obligation Recovery Zone Bonds were carried forward from the prior year and were expended during 2012 on capital items.

**CITY OF COVINGTON, KENTUCKY**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)**

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**Other Governmental Funds**

The City's governmental funds reported a combined ending fund balance of \$3,292,864, a decrease of \$(1,902,263) from the previous year. The General Fund unassigned fund balance is \$1,043,176, or 2.1% of General Fund operating expenses. The City Commission has established a goal of 5.0% of General Fund operating expenses as a minimum fund balance retention policy.

The fiscal year 2011, the Government Funds Balance Sheet included \$1,577,223 in fund balance restricted for capital projects. As noted previously, Taxable General Obligation Recovery Zone Bonds were issued in the amount of \$2,650,000 in fiscal year 2011. At June 30, 2011, \$1,577,223 remained of the \$2,650,000 and was spent in fiscal year 2012 resulting in the majority of the \$1,902,263 decrease in General Fund fund balance.

**Community Development Block Grant -**

The Community Development Block Grant is a cost reimbursement HUD funded program. There is no fund balance and therefore no change in fund balance to report.

**HOME Program -**

There was minimal change in fund balance for the HOME Program of \$239. The HOME program is HUD funded and cost reimbursement. Program income is recognized before drawdowns can be sufficiently reduced which accounts for the fund balance.

**Housing Voucher Program -**

The Housing Voucher Program fund balance increased \$256,087 to \$1,445,087. Reimbursement of units rented is based on how well the City utilizes its unit capacity. Administration is reimbursed on a per unit basis as well. If managed correctly, the jurisdiction can see increases in fund balance. The fund balance is then restricted for Housing Voucher Program purposes.

**General Fund Budgetary Highlights**

Over the course of the fiscal year, the City Commission approved revisions of the General Fund budget one time. The final amended budget resulted in a net \$328,817 increase in appropriations and transfers. Differences between original budget and final amended budget can be summarized as follows:

|             |  |
|-------------|--|
| \$10,000    | increase in Legal                                    |
| \$(1,646)   | decrease in Finance                                  |
| \$(108,174) | decrease in Police                                   |
| \$725,000   | increase in Fire                                     |
| \$(151,363) | decrease in Department of Public Improvements        |
| \$10,000    | increase in Code Enforcement (Community Development) |
| \$(100,000) | decrease in Economic Development                     |
| \$20,000    | increase in Parking Garages                          |
| \$(75,000)  | decrease in transfers                                |

The budget amendment was made to more closely reflect the anticipated actual expense for the year and to formally adopt as part of the budget changes in staff or activities that were approved by the City Commission during the year. It also reflected budget changes required by GASB Statement Number 54. The net budgetary increase was absorbed by unassigned fund balance.

The decreases are primarily due to selectively freezing vacant positions and partially implementing a comprehensive savings plan.

The increase in Fire was a result of the inability of City administration and Firefighter Local 38 to reach a contractual agreement to realize budgeted savings during fiscal year 2012.



**CITY OF COVINGTON, KENTUCKY**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)**

**DEBT AND CAPITAL ASSET ADMINISTRATION**

**Debt Administration**

At year-end, the City had \$35,323,350 in outstanding notes, capital leases, bonds, and compensated absences compared to \$39,127,643 the prior year. The following is a summary of the changes in the City's outstanding long-term debt from fiscal year 2012 to fiscal year 2011.

|   | <b>Governmental Activities</b> |                      |
|---|--------------------------------|----------------------|
|   | <b>2012</b>                    | <b>2011</b>          |
| Mortgage Bonds and Notes Payable (backed by city) | \$ 18,960,628                  | \$ 21,289,349        |
| Capital Lease Obligations (backed by city)        | 15,081,134                     | 16,247,510           |
| Compensated Absences                              | <u>1,281,588</u>               | <u>1,590,784</u>     |
| Totals  | <u>\$ 35,323,350</u>           | <u>\$ 39,127,643</u> |

The Kentucky Constitution states that the total principal amount of indebtedness, which excludes self-supporting obligations, revenue bonds, special assessment debt, and non-tax supported debt, cannot exceed 10% of the value of taxable property in the City. The debt limit for the City of Covington is \$211 million. The City's latest bond rating (December 13, 2010) is A2 from Moody's Investors Service.

The City issues and incurs debt in order to fund capital improvement projects, purchase capital equipment and facilities, and respond to other economic development needs. No debt was issued during fiscal year 2012.

Additional information on the City's long-term debt can be found on pages 46-49.

**Capital Assets**

The City's capital assets, net of depreciation as of June 30, 2012 totaled \$56,255,259, a decrease of \$1,500,364 from last year.

Major capital additions for the year were as follows:

|  |            |
|--|------------|
| RiverCenter plaza and garage restoration                         | \$ 617,336 |
| CAD/RMS system replacement for Police Department                 | \$ 604,060 |
| New parking gates and automated payment systems for City garages | \$ 593,323 |
| Police cruisers (16)   | \$ 386,902 |
| Cardiac monitors and MSA gas detectors for Fire Department       | \$ 347,444 |
| New concession and restroom facility at Devou Park bandshell     | \$ 321,587 |

**CITY OF COVINGTON, KENTUCKY**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)**

The following is a summary by classification, net of accumulated depreciation, of the City's capital assets for fiscal year 2012 and fiscal year 2011.

|                              | <b>Governmental Activities</b> |                      |
|------------------------------|--------------------------------|----------------------|
|                              | <b>2012</b>                    | <b>2011</b>          |
| Land                         | \$ 14,569,320                  | \$ 14,617,829        |
| Land improvements            | 1,551,092                      | 1,427,370            |
| Building                     | 14,060,062                     | 14,650,903           |
| Building Improvements        | 2,749,406                      | 1,581,548            |
| Vehicles                     | 1,209,427                      | 1,102,990            |
| Other equipment              | 1,667,377                      | 715,972              |
| Public domain infrastructure | 19,795,256                     | 23,659,011           |
| Construction in progress     | 653,319                        | -                    |
| <b>Totals</b>                | <b>\$ 56,255,259</b>           | <b>\$ 57,755,623</b> |

Additional information on the City's capital assets can be found on page 43.

**ECONOMIC FACTORS AND NEXT YEAR'S BUDGET**

The unemployment rate for Kenton County fell from 9.7% to 8.9%. Occupational license taxes, which are more than 55% of General Fund revenues, increased from the previous year for the first time in three years during fiscal year 2012. Fiscal Year 2013 revenue targets were budgeted to be flat with one exception. A rate decrease in the payroll occupational license tax from 2.5% to 2.45% was built into the revenue projections. This is the first change of the rate since 1966 and hopefully the City will be able to reduce the rate further. Job growth and job retention will be the focus of the newly reorganized Economic Development Department and the rate reduction will make the City more competitive with surrounding cities.

Collective bargaining agreements have been successfully negotiated with all three unions which extend through the end of calendar year 2015. The most significant aspect of the new collective bargaining agreements is a new health care plan design which will net the City \$2 million per year after pay increases.

As a result of closing the City's 911 dispatch center and allowing Kenton County to provide 911 dispatch services, the City will save approximately \$1 million per year. Sixteen dispatcher positions were eliminated. As a whole, full time equivalents have fallen from approximately 370 during 2012 to an estimated 340 for the upcoming fiscal year.

The Financial Recovery Plan is in place and savings will be used to replenish fund balances and reinvest in capital assets.

**CITY OF COVINGTON, KENTUCKY**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)**

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**CONTACTING THE CITY'S FINANCIAL MANAGEMENT**

This financial report is designed to provide our citizens, taxpayers, customers, and creditors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have questions about this report or need additional financial information, contact Robert J. Due, Finance Director, 638 Madison Avenue, Covington, Kentucky 41011. Questions or requests for additional information can also be e-mailed to [bdue@covingtonky.gov](mailto:bdue@covingtonky.gov).

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**BASIC  
FINANCIAL STATEMENTS**

# City of Covington, Kentucky

## Statement of Net Assets

June 30, 2012

|  | <b>Primary<br/>Government<br/>Governmental<br/>Activities</b> | <b>Component Unit<br/>Devou<br/>Properties, Inc.</b> |
|--|---|--|
| <b>ASSETS</b>  |   |  |
| Current assets                                       |   |  |
| Cash and cash equivalents                            | \$ 4,666,942  | \$ 2,243,245   |
| Receivables (net of allowance for doubtful accounts) |   |  |
| Property taxes                                       | 4,698,470   | -  |
| Intergovernmental                                    | 633,425   | -  |
| Notes  | 16,843,635  | -  |
| Accounts   | 2,587,624   | 105,527  |
| Prepaid items  | 98,617  | 4,404  |
| Total current assets                                 | 29,528,713  | 2,353,176  |
| Noncurrent assets                                    |   |  |
| Deferred charges, net                                | 249,579   | -  |
| Deferred outflow - hedges                            | 1,174,521   | -  |
| Net pension obligation asset                         | 2,718,987   | -  |
| Land and construction in progress                    | 16,773,731  | -  |
| Depreciable capital assets                           | 164,239,777   | 82,388   |
| Less accumulated depreciation                        | (124,758,249)   | (33,518)   |
| Total noncurrent assets                              | 60,398,346  | 48,870   |
| Total assets   | 89,927,059  | 2,402,046  |
| <b>LIABILITIES</b>                                   |   |  |
| Current liabilities                                  |   |  |
| Accounts payable                                     | 2,161,273   | 18,382   |
| Accrued liabilities                                  | 3,153,834   | 330,422  |
| Accrued interest payable                             | 275,762   | -  |
| Unearned revenue                                     | 1,632,114   | -  |
| Accumulated compensated absences                     | 1,281,588   | -  |
| Current portion of capital lease obligations         | 1,218,660   | -  |
| Current portion of bonds and notes payable           | 2,079,757   | -  |
| Total current liabilities                            | 11,802,988  | 348,804  |
| Noncurrent liabilities                               |   |  |
| Noncurrent portion of capital lease obligations      | 13,862,474  | -  |
| Noncurrent portion of bonds and notes payable        | 16,880,871  | -  |
| Derivative instrument - liability                    | 1,174,521   | -  |
| Total noncurrent liabilities                         | 31,917,866  | -  |
| Total liabilities                                    | 43,720,854  | 348,804  |
| <b>NET ASSETS</b>                                    |   |  |
| Invested in capital assets, net of related debt      | 34,173,497  | 48,870   |
| Restricted for capital projects                      | 190,681   | -  |
| Restricted for HUD Programs                          | 16,648,464  | -  |
| Unrestricted   | (4,806,437)   | 2,004,372  |
| Total net assets                                     | \$ 46,206,205   | \$ 2,053,242   |

The accompanying notes are an integral part of the financial statements.

# City of Covington, Kentucky

## Statement of Activities

Year Ended June 30, 2012

| Function/Programs  | Program Revenues     |                      |                                    | Capital Grants and Contributions | Net (Expense) Revenue and Changes in Net Assets |                     |
|--|----------------------|----------------------|------------------------------------|----------------------------------|---|---------------------|
|  | Expenses             | Charges for Services | Operating Grants and Contributions |                                  | Primary Governmental Activities                 | Component Unit      |
| <b>Primary Government</b>                                |                      |                      |                                    |                                  |   |                     |
| <b>Governmental activities</b>                           |                      |                      |                                    |                                  |   |                     |
| General government                                       | \$ 4,250,735         | \$ 936,996           | \$ 762,045                         | \$ 463,010                       | \$ (2,088,684)                                  |                     |
| Police   | 16,455,964           | 189,671              | 915,968                            | 205,958                          | (15,144,367)                                    |                     |
| Fire   | 15,180,999           | 1,333,724            | -                                  | -                                | (13,847,275)                                    |                     |
| Public improvements                                      | 11,349,786           | 2,342,050            | 500,848                            | 978,188                          | (7,528,700)                                     |                     |
| Recreation   | 711,584              | 22,753               | -                                  | -                                | (688,831)                                       |                     |
| Community development                                    | 15,379,018           | 169,209              | 10,340,048                         | -                                | (4,869,761)                                     |                     |
| Parking garage   | 768,661              | 1,674,834            | -                                  | -                                | 906,173   |                     |
| Interest on long-term debt                               | 1,324,845            | -                    | -                                  | -                                | (1,324,845)                                     |                     |
| Total primary government                                 | <u>\$ 65,421,592</u> | <u>\$ 6,669,237</u>  | <u>\$ 12,518,909</u>               | <u>\$ 1,647,156</u>              | <u>(44,586,290)</u>                             |                     |
| <b>Component Unit</b>                                    |                      |                      |                                    |                                  |   |                     |
| Devou Properties, Inc.                                   | \$ 674,992           | \$ 947,378           | \$ -                               | \$ -                             | \$ -  | \$ 272,386          |
| <b>General revenues</b>                                  |                      |                      |                                    |                                  |   |                     |
| Taxes  |                      |                      |                                    |                                  |   |                     |
| Real property taxes, levied for general purposes         |                      |                      |                                    |                                  | 6,141,332                                       | -                   |
| Personal property taxes, levied for general purposes     |                      |                      |                                    |                                  | 796,259   | -                   |
| Public service taxes                                     |                      |                      |                                    |                                  | 1,944,431                                       | -                   |
| Taxes, levied for bank deposits                          |                      |                      |                                    |                                  | 87,014  | -                   |
| Insurance premium taxes                                  |                      |                      |                                    |                                  | 4,988,428                                       | -                   |
| Payroll taxes  |                      |                      |                                    |                                  | 22,764,392                                      | -                   |
| Net profits taxes  |                      |                      |                                    |                                  | 3,011,825                                       | -                   |
| Other taxes  |                      |                      |                                    |                                  | 805,015   | -                   |
| Investment earnings                                      |                      |                      |                                    |                                  | 23,084  | 1,160               |
| Miscellaneous  |                      |                      |                                    |                                  | 2,286,030                                       | -                   |
| Total general revenues                                   |                      |                      |                                    |                                  | <u>42,847,810</u>                               | <u>1,160</u>        |
| <b>Change in net assets</b>                              |                      |                      |                                    |                                  | <u>(1,738,480)</u>                              | <u>273,546</u>      |
| Net assets - beginning of year, as restated (see Note 2) |                      |                      |                                    |                                  | <u>47,944,685</u>                               | <u>1,779,696</u>    |
| Net assets - end of year                                 |                      |                      |                                    |                                  | <u>\$ 46,206,205</u>                            | <u>\$ 2,053,242</u> |

The accompanying notes are an integral part of the financial statements.

**City of Covington, Kentucky**  
**Balance Sheet - Governmental Funds**  
**June 30, 2012**

|  | <u>General<br/>Fund</u>     | <u>Community<br/>Development<br/>Block Grant</u> | <u>HOME<br/>Program</u>    | <u>Housing<br/>Voucher<br/>Program</u> | <u>Non-Major<br/>Governmental<br/>Funds</u> | <u>Total<br/>Governmental<br/>Funds</u> |
|--|-----------------------------|--|----------------------------|--|---|---|
| <b>ASSETS</b>                              |                             |  |                            |  |   |   |
| Cash and cash equivalents                  | \$ 1,405,088                | \$ -   | \$ 25,200                  | \$ 1,307,102                           | \$ 861,059                                  | \$ 3,598,449                            |
| Receivables                                |                             |  |                            |  |   |   |
| Taxes                                      | 4,698,470                   | -  | -                          | -                                      | -   | 4,698,470                               |
| Intergovernmental                          | -                           | 106,322  | 45,283                     | 197,000                                | 284,820                                     | 633,425                                 |
| Notes                                      | 1,941,855                   | 5,953,021  | 5,942,623                  | -                                      | 3,006,136                                   | 16,843,635                              |
| Accounts                                   | 1,732,225                   | -  | -                          | 27,745                                 | 827,654                                     | 2,587,624                               |
| Due from other funds                       | 961,418                     | 145,804  | 59,184                     | 20,867                                 | 3,342                                       | 1,190,615                               |
| Prepaid expenses                           | <u>98,617</u>               | <u>-</u>   | <u>-</u>                   | <u>-</u>                               | <u>-</u>                                    | <u>98,617</u>                           |
| <b>TOTAL ASSETS</b>                        | <b>\$ <u>10,837,673</u></b> | <b>\$ <u>6,205,147</u></b>                       | <b>\$ <u>6,072,290</u></b> | <b>\$ <u>1,552,714</u></b>             | <b>\$ <u>4,983,011</u></b>                  | <b>\$ <u>29,650,835</u></b>             |
| <b>LIABILITIES AND FUND BALANCES</b>       |                             |  |                            |  |   |   |
| <b>LIABILITIES</b>                         |                             |  |                            |  |   |   |
| Accounts payable                           | \$ 1,537,104                | \$ 80,336  | \$ 245                     | \$ 1,872                               | \$ 374,286                                  | \$ 1,993,843                            |
| Accrued liabilities                        | 1,353,543                   | -  | -                          | 14,500                                 | -   | 1,368,043                               |
| Due to other funds                         | 1,377,636                   | -  | -                          | -                                      | 961,418                                     | 2,339,054                               |
| Deferred revenue                           | <u>5,236,916</u>            | <u>6,124,811</u>                                 | <u>5,942,623</u>           | <u>90,870</u>                          | <u>3,261,811</u>                            | <u>20,657,031</u>                       |
| Total liabilities                          | <u>9,505,199</u>            | <u>6,205,147</u>                                 | <u>5,942,868</u>           | <u>107,242</u>                         | <u>4,597,515</u>                            | <u>26,357,971</u>                       |
| <b>FUND BALANCES</b>                       |                             |  |                            |  |   |   |
| Non-spendable                              |                             |  |                            |  |   |   |
| Prepaid expenses                           | 98,617                      | -  | -                          | -                                      | -   | 98,617                                  |
| Restricted for                             |                             |  |                            |  |   |   |
| Capital projects                           | 190,681                     | -  | -                          | -                                      | -   | 190,681                                 |
| HUD projects                               | -                           | -  | 129,422                    | 1,445,472                              | -   | 1,574,894                               |
| Committed for                              |                             |  |                            |  |   |   |
| Devou Park maintenance                     | -                           | -  | -                          | -                                      | 22,464                                      | 22,464                                  |
| Police                                     | -                           | -  | -                          | -                                      | 83,657                                      | 83,657                                  |
| Debt service                               | -                           | -  | -                          | -                                      | 279,375                                     | 279,375                                 |
| Unassigned                                 | <u>1,043,176</u>            | <u>-</u>   | <u>-</u>                   | <u>-</u>                               | <u>-</u>                                    | <u>1,043,176</u>                        |
| Total fund balances                        | <u>1,332,474</u>            | <u>-</u>   | <u>129,422</u>             | <u>1,445,472</u>                       | <u>385,496</u>                              | <u>3,292,864</u>                        |
| <b>TOTAL LIABILITIES AND FUND BALANCES</b> | <b>\$ <u>10,837,673</u></b> | <b>\$ <u>6,205,147</u></b>                       | <b>\$ <u>6,072,290</u></b> | <b>\$ <u>1,552,714</u></b>             | <b>\$ <u>4,983,011</u></b>                  | <b>\$ <u>29,650,835</u></b>             |

The accompanying notes are an integral part of the financial statements.



## City of Covington, Kentucky

### Reconciliation of the Balance Sheet - Governmental Funds to the Statement of Net Assets

June 30, 2012

|  |    |                      |
|--|----|----------------------|
| Total fund balance - Governmental funds  | \$ | 3,292,864            |
| <p>Amounts reported for governmental activities in the statement of net assets are different because:</p>  |    |                      |
| <p>Capital assets used in governmental activities are not current financial resources and therefore are not reported in this fund financial statement, but are reported in the governmental activities of the statement of net assets.</p>   |    |                      |
| Cost of capital assets   |    | 181,013,508          |
| Accumulated depreciation   |    | <u>(124,758,249)</u> |
|  |    | 56,255,259           |
| <p>Certain other long-term assets are not available to pay current period expenditures and are therefore deferred in the funds.</p>  |    |                      |
|  |    | 19,024,917           |
| <p>Internal service funds are used by management to charge the cost of certain activities, such as liability and health and dental insurance, to individual funds. The assets and liabilities of the internal service funds must be added to the statement of net assets.</p>  |    |                      |
|  |    | 263,711              |
| <p>Deferred charges represent costs related to the issuance of new bonds and also refunding costs. Deferred charges are reported as an other use of funds in the governmental funds statements. However, on the government wide statement of net assets these costs are capitalized and reported as a deferred charge, and amortized over the life of the related bonds.</p> |    |                      |
|  |    | 249,579              |
| <p>Net pension obligation asset represents contributions made to the City's pension funds in excess of the actuarially required contribution. The excess contributions are capitalized and amortized.</p>  |    |                      |
|  |    | 2,718,987            |
| <p>Interest payable on long-term debt does not require current financial resources. Therefore accrued interest payable is not reported as a liability in the governmental funds balance sheet.</p>   |    |                      |
|  |    | (275,762)            |
| <p>Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported as liabilities in the funds.</p>   |    |                      |
| <p>Long-term liabilities at year end consist of:</p>   |    |                      |
| Bonds payable  |    | (18,960,628)         |
| Capital lease obligations payable  |    | (15,081,134)         |
| Compensated absences payable   |    | <u>(1,281,588)</u>   |
| Total liabilities  |    | <u>(35,323,350)</u>  |
| Net assets of governmental activities  | \$ | <u>46,206,205</u>    |

The accompanying notes are an integral part of the financial statements.

# City of Covington, Kentucky

## Statement of Revenues, Expenditures and Changes in Fund Balances - Governmental Funds

Year Ended June 30, 2012

|   | General<br>Fund     | Community<br>Development<br>Block Grant | HOME<br>Program   | Housing<br>Voucher<br>Program | Non-Major<br>Governmental<br>Funds | Total<br>Governmental<br>Funds |
|---|---------------------|---|-------------------|-------------------------------|------------------------------------|--------------------------------|
| <b>REVENUES</b>                                   |                     |   |                   |                               |                                    |                                |
| Taxes   | \$ 13,657,232       | \$ -                                    | \$ -              | \$ -                          | \$ 805,015                         | \$ 14,462,247                  |
| Licenses and permits                              | 26,175,310          | -                                       | -                 | -                             | -                                  | 26,175,310                     |
| Intergovernmental                                 | 1,862,791           | 1,324                                   | 383               | 6,815                         | 4,123,559                          | 14,510,735                     |
| Charges for services                              | 6,063,323           | -                                       | -                 | -                             | -                                  | 6,063,323                      |
| Fines and forfeitures                             | 439,189             | -                                       | -                 | -                             | -                                  | 439,189                        |
| Investment earnings                               | 21,948              | -                                       | 132               | 830                           | 174                                | 23,084                         |
| Miscellaneous                                     | 695,022             | 731,849                                 | 66,359            | 1,309                         | 954,483                            | 2,449,022                      |
| Total revenues                                    | <u>48,914,815</u>   | <u>2,056,652</u>                        | <u>450,081</u>    | <u>6,818,131</u>              | <u>5,883,231</u>                   | <u>64,122,910</u>              |
| <b>EXPENDITURES</b>                               |                     |   |                   |                               |                                    |                                |
| Current   |                     |   |                   |                               |                                    |                                |
| General government                                | 3,207,768           | -                                       | -                 | -                             | 411,120                            | 3,618,888                      |
| Police  | 14,902,625          | -                                       | -                 | -                             | 686,153                            | 15,588,778                     |
| Fire  | 13,241,215          | -                                       | -                 | -                             | 601,547                            | 13,842,762                     |
| Public improvements                               | 5,891,702           | -                                       | -                 | -                             | -                                  | 5,891,702                      |
| Recreation  | 475,601             | -                                       | -                 | -                             | -                                  | 475,601                        |
| Community development                             | 3,947,945           | 1,558,287                               | 398,606           | 6,562,044                     | 1,637,680                          | 14,104,562                     |
| Parking garages                                   | 743,506             | -                                       | -                 | -                             | -                                  | 743,506                        |
| Debt service                                      |                     |   |                   |                               |                                    |                                |
| Principal   | 2,147,521           | -                                       | -                 | -                             | 1,535,000                          | 3,682,521                      |
| Interest and other charges                        | 564,718             | 18,046                                  | -                 | -                             | 640,782                            | 1,223,546                      |
| Capital outlay                                    | 3,743,244           | 147,819                                 | 51,236            | -                             | 1,905,241                          | 5,847,540                      |
| Total expenditures                                | <u>48,865,845</u>   | <u>1,724,152</u>                        | <u>449,842</u>    | <u>6,562,044</u>              | <u>7,417,523</u>                   | <u>65,019,406</u>              |
| Excess (deficiency) of revenues over expenditures | <u>48,970</u>       | <u>332,500</u>                          | <u>239</u>        | <u>256,087</u>                | <u>(1,534,292)</u>                 | <u>(896,496)</u>               |
| <b>OTHER FINANCING SOURCES (USES)</b>             |                     |   |                   |                               |                                    |                                |
| Transfers in                                      | 1,595,013           | -                                       | -                 | -                             | 2,495,181                          | 4,090,194                      |
| Proceeds from sale of capital assets              | 5,517               | -                                       | -                 | -                             | -                                  | 5,517                          |
| Transfers out                                     | <u>(3,937,681)</u>  | <u>(332,500)</u>                        | <u>-</u>          | <u>-</u>                      | <u>(831,297)</u>                   | <u>(5,101,478)</u>             |
| Total other financing sources (uses)              | <u>(2,337,151)</u>  | <u>(332,500)</u>                        | <u>-</u>          | <u>-</u>                      | <u>1,663,884</u>                   | <u>(1,005,767)</u>             |
| <b>NET CHANGE IN FUND BALANCES</b>                | (2,288,181)         | -                                       | 239               | 256,087                       | 129,592                            | (1,902,263)                    |
| <b>FUND BALANCES - beginning of year</b>          | <u>3,620,655</u>    | <u>-</u>                                | <u>129,183</u>    | <u>1,189,385</u>              | <u>255,904</u>                     | <u>5,195,127</u>               |
| <b>FUND BALANCES - end of year</b>                | <u>\$ 1,332,474</u> | <u>\$ -</u>                             | <u>\$ 129,422</u> | <u>\$ 1,445,472</u>           | <u>\$ 385,496</u>                  | <u>\$ 3,292,864</u>            |

The accompanying notes are an integral part of the financial statements.

## City of Covington, Kentucky

### Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balance - Governmental Funds to the Statement of Activities

Year Ended June 30, 2012

|   |                       |
|---|-----------------------|
| Changes in fund balances - Total governmental funds   | \$ (1,902,263)        |
| Amounts reported for governmental activities in the statement of activities are different because:  |                       |
| Capital outlays to purchase or build capital assets are reported in governmental funds as expenditures. However, for governmental activities those costs are shown in the statement of net assets and allocated over their estimated useful lives as annual depreciation expense in the statement of activities. This is the amount by which depreciation expense exceeds capital outlays in the period.              |                       |
| Depreciation expense  | (5,979,132)           |
| Capital outlays   | <u>4,527,277</u>      |
|   | (1,451,855)           |
| Governmental funds report the entire net sales price (proceeds) from sale of an asset as revenue because it provides current financial resources. In contrast, the statement of activities reports only the gain or loss on the sale of the assets. Thus, the change in net assets differs from the change in fund balance by the net book value of the asset sold.   | (48,509)              |
| Governmental funds do not present revenues that are not available to pay current obligations. In contrast, such revenues are reported in the statement of activities when earned.   | (396,806)             |
| Repayment of bond, note and capital lease principal is an expenditure in the governmental funds, but it reduces long-term liabilities in the statement of net assets and does not affect the statement of activities.   | 3,682,521             |
| The statement of activities reports annual pension cost, which includes the actuarially required contribution along with an interest factor and adjustment of the net pension obligation asset.   | (1,895,035)           |
| Accrued interest not reflected on governmental funds.   | (45,118)              |
| In the statement of activities, compensated absences (sick leave) are measured by the amounts earned during the year. In the governmental funds, however, expenditures for these items are measured by the amount of financial resources used (essentially, the amounts actually paid). The additional expense reported in the statement of activities is a result of the change in long-term accumulated sick leave. | 309,196               |
| Costs related to the issuance of bonds and deferred refunding costs are reported as an other use of funds in the governmental funds financial statements. However, on the government-wide statement of net assets, these costs are capitalized and reported as a deferred charge, and subsequently amortized over the life of the related bonds.  | (56,181)              |
| Internal service funds are used by management to charge the costs of certain activities, such as fleet maintenance and information technology, to individual funds. The net revenue (expense) of certain internal service funds is reported with the governmental activities.   | <u>65,570</u>         |
| Total change in net assets - governmental activities  | <u>\$ (1,738,480)</u> |

The accompanying notes are an integral part of the financial statements.

**City of Covington, Kentucky**  
**Statement of Net Assets - Proprietary Funds**  
**June 30, 2012**

|                                | <u>Governmental<br/>Activities</u><br>Internal Service<br>Funds |
|--------------------------------|---|
| <b>ASSETS</b>                  |   |
| Current assets                 |   |
| Cash and cash equivalents      | \$ 1,068,493  |
| Due from other funds           | <u>1,148,439</u>  |
| Total assets                   | <u>2,216,932</u>  |
| <b>LIABILITIES</b>             |   |
| Current liabilities            |   |
| Accounts payable               | 167,430   |
| Estimated liability for claims | <u>1,785,791</u>  |
| Total liabilities              | <u>1,953,221</u>  |
| <b>NET ASSETS</b>              |   |
| Unrestricted                   | <u>\$ 263,711</u>   |

The accompanying notes are an integral part of the financial statements.

**City of Covington, Kentucky**

**Statement of Revenues, Expenses and Changes in Fund Net Assets - Proprietary Funds**  
**Year Ended June 30, 2012**

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|                                       | <u>Governmental<br/>Activities</u><br><u>Internal Service<br/>Funds</u> |
|---------------------------------------|---|
| <b>OPERATING REVENUES</b>             |   |
| Insurance premium payments            | \$ 5,803,748  |
| Other operating revenues              | <u>420,478</u>  |
| Total operating revenues              | <u>6,224,226</u>  |
| <b>OPERATING EXPENSES</b>             |   |
| Contractual services                  | 693,045   |
| Claims and judgments                  | <u>6,477,166</u>  |
| Total operating expenses              | <u>7,170,211</u>  |
| <b>OPERATING LOSS</b>                 | (945,985)   |
| <b>NON-OPERATING REVENUES</b>         |   |
| Investment income                     | <u>271</u>  |
| Loss before transfers                 | (945,714)   |
| Transfers in                          | <u>1,442,500</u>  |
| Transfers out                         | <u>(431,216)</u>  |
| <b>CHANGE IN NET ASSETS</b>           | 65,570  |
| <b>NET ASSETS - beginning of year</b> | <u>198,141</u>  |
| <b>NET ASSETS - end of year</b>       | <u>\$ 263,711</u>   |

The accompanying notes are an integral part of the financial statements.

**City of Covington, Kentucky**  
**Statement of Cash Flows - Proprietary Funds**  
**Year Ended June 30, 2012**

|   | <b>Governmental<br/>Activities</b> |
|---|------------------------------------|
|   | <b>Internal<br/>Service Funds</b>  |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>   |                                    |
| Cash received from other funds  | \$ 5,900,917                       |
| Cash received from other activities   | 420,478                            |
| Cash paid for claims  | <u>(6,136,211)</u>                 |
| <b>Net cash flows from operating activities</b>   | 185,184                            |
| <br><b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>                                  |                                    |
| Transfers from other funds  | 844,588                            |
| <br><b>CASH FLOWS FROM INVESTING ACTIVITIES</b>   |                                    |
| Interest income   | <u>271</u>                         |
| <br><b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>  | 1,030,043                          |
| <br><b>CASH AND CASH EQUIVALENTS - beginning of year</b>                                    | <u>38,450</u>                      |
| <br><b>CASH AND CASH EQUIVALENTS - end of year</b>  | <u><u>\$ 1,068,493</u></u>         |
| <br><b>RECONCILIATION OF OPERATING LOSS TO NET<br/>CASH FLOWS FROM OPERATING ACTIVITIES</b> |                                    |
| Operating loss  | \$ (945,985)                       |
| Changes in operating assets and liabilities   |                                    |
| Accounts receivable   | 186,350                            |
| Due from other funds  | (89,181)                           |
| Accounts payable  | 86,169                             |
| Estimated liability claims  | <u>947,831</u>                     |
| <br><b>NET CASH FLOWS FROM OPERATING ACTIVITIES</b>   | <u><u>\$ 185,184</u></u>           |

The accompanying notes are an integral part of the financial statements.

**City of Covington, Kentucky**  
**Statement of Fiduciary Net Assets - Fiduciary Funds**  
**June 30, 2012**

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|                                    | <b>Employees'<br/>Retirement</b> | <b>Police and<br/>Firemen's<br/>Retirement</b> |
|------------------------------------|----------------------------------|--|
| <b>ASSETS</b>                      |                                  |  |
| Cash and cash equivalents          | \$ 207,003                       | \$ 345,627                                     |
| Investments                        | 3,253,079                        | 7,716,619                                      |
| Total assets                       | 3,460,082                        | 8,062,246                                      |
| <b>NET ASSETS</b>                  |                                  |  |
| Held in trust for pension benefits | \$ 3,460,082                     | \$ 8,062,246                                   |

The accompanying notes are an integral part of the financial statements.

**City of Covington, Kentucky**  
**Statement of Changes in Fiduciary Net Assets - Fiduciary Funds**  
**Year Ended June 30, 2012**

|   | <u>Employees'</u><br><u>Retirement</u> | <u>Police and</u><br><u>Firemen's</u><br><u>Retirement</u> |
|---|--|--|
| <b>ADDITIONS</b>                              |  |  |
| Employee contributions                        | \$ 1,010                               | \$ -   |
| Impounding lot                                | <u>-</u>                               | <u>83,534</u>  |
| Total revenues                                | <u>1,010</u>                           | <u>83,534</u>  |
| Investment return                             |  |  |
| Interest and dividends                        | 104,985                                | 237,389  |
| Net depreciation in fair value of investments | <u>(122,301)</u>                       | <u>(272,566)</u>   |
| Total net investment return                   | <u>(17,316)</u>                        | <u>(35,177)</u>  |
| Total additions                               | <u>(16,306)</u>                        | <u>48,357</u>  |
| <b>DEDUCTIONS</b>                             |  |  |
| Benefit payments                              | 512,552                                | 1,526,236  |
| Administration                                | <u>13,230</u>                          | <u>33,777</u>  |
| Total deductions                              | <u>525,782</u>                         | <u>1,560,013</u>   |
| <b>CHANGE IN NET ASSETS</b>                   | (542,088)                              | (1,511,656)  |
| <b>NET ASSETS - beginning of year</b>         | <u>4,002,170</u>                       | <u>9,573,902</u>   |
| <b>NET ASSETS - end of year</b>               | <u>\$ 3,460,082</u>                    | <u>\$ 8,062,246</u>  |

The accompanying notes are an integral part of the financial statements.



**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

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**Note 1 - Summary of Significant Accounting Policies**

***Basis of Presentation***

The basic financial statements of the City of Covington, Kentucky, have been prepared in conformity with U.S. generally accepted accounting principles (GAAP) as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The significant accounting policies of the City are described below.

***Financial Reporting Entity***

The City of Covington is a municipality that operates under a City Manager form of government. Legislative authority is vested in the elected Mayor and four City Commissioners. As required by U.S. generally accepted accounting principles, these financial statements present the government and its component units, entities for which the government is considered to be financially accountable.

Blended component units, although legally separate entities are, in substance, part of the government's operations and so data from these units are combined with data of the primary government. Each blended component unit of the City has a June 30 year end. The component units discussed below are included in the City's reporting entity as part of the primary government because of the significance of its operational and/or financial relationship with the City.

**Blended Component Units Included Within the Reporting Entity**

***City of Covington Non-Uniformed Employees' Pension Fund***

Certain City employees participate in the non-uniformed employee pension fund. The fund functions for the benefit of these employees and is governed by a four member board of trustees. The mayor, finance director, and two appointed and approved employees constitute the board. The City and plan participants are obligated to fund all costs based upon actuarial valuations.

***City of Covington Police and Firemen's Pension Fund***

All public safety employees who retired prior to August 1, 1989, participate in the Police & Firemen's Pension Fund. The fund functions for the benefit of the retirees and is governed by a four member board of trustees, consisting of the mayor, finance director and two public safety retirees. The City is obligated to fund all costs based upon actuarial valuations.

***City of Covington Municipal Properties Corporation***

The City of Covington Municipal Properties Corporation was formed to act as an agent and to be instrumental in the financing of public improvements and projects of a capital nature for the City and for the particular purpose of acquiring real estate located within the City and constructing, acquiring and equipping thereon capital improvements, facilities, buildings, structures and related appurtenances. The Corporation finances these projects by the issuance of debt. These debt issues are secured by (1) first mortgage liens on the projects, (2) lease and option agreements between the Corporation and the City, the construction agreements and pledged receipts. The lease and option agreements require the City to pay rental, on a yearly basis with the option to renew each year, equal to the amount of bonds and interest coupons coming due in that year. If the City renews the leases from year-to-year, and pays the rentals for each year as stipulated, and when the Corporation has fully paid and retired all of the bonds, the Corporation agrees it will convey the properties to the City free and clear.

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

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**Note 1 - Summary of Significant Accounting Policies - continued**

**Discretely Presented Component Units Included Within the Reporting Entity**

Devou Properties, Inc. (a non-profit organization) is included in the City's financial statements as a discretely presented component unit. Although a legally separate entity, Devou Properties, Inc. is included in these financial statements because of its financial accountability to the City. Devou Properties, Inc. was formed to maintain and operate the Drees Pavilion at Devou Memorial Overlook for the City of Covington, for the benefit of Devou Park. Devou Properties, Inc. is responsible for renting out the facilities for events, including weddings, receptions and corporate events. Directors of Devou Properties, Inc. are appointed by the City's Board of Commissioners, upon the recommendation of the Mayor. Any excess funds from operations of the facility are to be set aside to be used on Devou Park projects. As a discretely presented component unit, the financial statements of Devou Properties, Inc. are only included on the City's government-wide financial statements in a column that makes it clearly separate from the primary government. Devou Properties, Inc. operates on a calendar year-end basis; therefore, the financial statements for the year ended December 31, 2011, are included in the City's current financial statements. Audited financial statements of Devou Properties, Inc. are available and may be obtained by contacting the City Manager.

**Basis of Presentation Government-Wide Financial Statements**

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the non-fiduciary activities of the primary government. For the most part, the effect of interfund activity has been removed from these statements; however, interfund services provided and used are not eliminated. Governmental activities, which are normally 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.

The statement of activities demonstrates the degree to which direct expenses of a given function or segments are offset by program revenues. Direct expenses are those 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.

Amounts paid to acquire capital assets are capitalized as assets in the government-wide financial statements, rather than reported as an expenditure. Proceeds of long-term debt are recorded as a liability in the government-wide financial statements, rather than as another financing source. Amounts paid to reduce long-term indebtedness of the reporting government are reported as a reduction of the related liability, rather than as an expenditure.

**Measurement Focus, Basis of Accounting and Financial Statement Presentation**

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting as are the proprietary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of the related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

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**Note 1 - Summary of Significant Accounting Policies - continued**

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of 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.

For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Material revenues susceptible to accrual are payroll license fees, insurance fees and grant revenues. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

The government reports the following funds of the financial reporting entity:

- The general fund is the government's primary operating fund. It accounts for all financial resources of the general government, except for those required to be accounted for in another fund.
- The special revenue funds are used to account for the proceeds of specific revenue sources that are restricted to expenditures for specific purposes.
- The debt service funds are used to account for the accumulation of resources for, and the payment of, general long-term debt principal and interest.
- Proprietary funds distinguish operating revenues and expenses from non-operating revenues and expenses. Operating revenues and expenses generally result from providing services in connection with a proprietary fund's principal ongoing operations. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

The government reports the following proprietary funds:

- The City has two internal service funds. One fund is for self-insurance for the City's health and dental insurance program for City employees. The second fund is for the self-insurance of the City's liability claims.

Additionally, the City reports two fiduciary funds. The two pension trust funds account for the activities of the Employees' Retirement Fund and the Police and Firemen's Pension Fund. These funds are for the accumulation of resources for pension benefit payments to qualified retired employees.

The City reports the following major governmental funds:

- The General Fund is the government's primary operating fund. It accounts for all financial resources of the general government that are not accounted for in the other funds.
- The Community Development Block Grant Fund accounts for entitlements to the City under the provisions of Title 1 of the Housing and Development Act of 1974. Resources include a combination of block and other entitlement grants. Resources may only be used for activities which are directed toward developing urban communities and economic opportunities for persons of low and moderate income.
- The HOME Program Fund accounts for resources provided by the U.S. Department of Housing and Urban Development under the HOME Program. Proceeds are used for deferred loans which are used to acquire, construct or rehabilitate housing for low income families.

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

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**Note 1 - Summary of Significant Accounting Policies - continued**

- The Housing Voucher Fund accounts for funds provided to the City by the U.S. Department of Housing and Urban Development Section 8 rent subsidy program. Resources are used for the payment of rent subsidies to landlords on behalf of qualified tenants.

In addition, the City reports the following non-major governmental funds:

***Special Revenue Funds***

- Police and Fire Incentive Pay – This fund was established to account for entitlements received under the State of Kentucky's Policemen and Firemen's Supplemental Pay Programs.
- Devou Park Maintenance – This fund was established by Commissioners' ordinance in 1973 to account for the maintenance of roadways and streets within Devou Park.
- Devou Park Master Plan – This fund is used to account for revenues and expenditures of funds allocated for use in Devou Park, from proceeds of the operation of the Drees Pavilion.
- Federal and State Grant Funds – This fund was established to account for the revenues and expenditures related to grants awarded by federal and state agencies.
- Police Forfeiture – This fund was established to account for the resources provided for by police forfeitures.
- CAD System – This fund was established to account for revenues and expenditures related to the installation of a computer assisted dispatch system, and the subsequent debt service payments for the related capital lease.
- Renaissance Grant Fund – This fund was established to account for revenues and expenses related to renaissance grants received by the City.
- Home Consortium Fund – This fund was established to administer a HOME Program for a consortium of non entitlement cities in Northern Kentucky, including Newport, Bellevue, Dayton, Ludlow and Bromley. HOME funds are used to provide assistance to persons to purchase a home, owner-occupied rehab programs, and housing development activities with Community Housing Development organizations.
- Homeless Prevention Fund – This fund is used to administer U.S. Department of Housing and Urban Development funds to be used for foreclosure remediation.
- Neighborhood Stabilization Program – This fund was established to administer a U.S. Department of Housing and Urban Development grant to develop low income rental units and owner occupied homes purchased out of foreclosure.

***Debt Service Funds***

- 2004 Pension Obligation Bonds – The proceeds of this issue were used to fund the Employees' Retirement Fund and the Police and Fire Retirement Fund
- 2005 Refunding Bonds – The proceeds of this issue were used to refund the 1995 First Mortgage Bonds.

**Assets, Liabilities and Net Assets or Equity**

***Cash and Cash Equivalents***

Cash and cash equivalents includes amounts in demand deposits as well as short-term investments with an initial maturity date within three months of the date acquired by the City.

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

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**Note 1 - Summary of Significant Accounting Policies - continued**

The City is authorized by state statute to invest in:

- Obligations of the United States and of its Agencies and Instrumentalities
- Certificates of Deposits
- Bankers' Acceptances
- Commercial Paper
- Bonds of Other State or Local Governments
- Mutual Funds

***Investments***

In accordance with Government Accounting Standards Board requirements, investments held at June 30, 2012, are recorded at fair value based on quoted market prices.

Types of investments allowable in the Pension Trust Funds are governed by the Pension Board of Trustees. All investments are stated in accordance with GASB requirements.

***Property Tax Receivable***

Property taxes are levied as of January 1 on property values assessed as of the same date. The taxes are billed on approximately August 15 and are due and payable on September 30. On October 1, the bill becomes delinquent and penalties and interest may be assessed by the City. A lien may be placed on the property on October 1.

***Notes Receivable***

Notes receivable are carried at their unpaid principal balance.

***Short-Term Interfund Receivables/Payables***

During the course of operations, numerous transactions occur between individual funds for goods provided or services rendered. These receivables and payables are classified as "due from/to other funds" on the balance sheet. Short-term interfund loans are classified as "interfund receivables/payables."

***Prepaid Items***

Payments made to vendors for services that will benefit periods beyond June 30, 2012, are recorded as prepaid items in both the government-wide and fund statements. The consumption method is used in the fund statements.

***Capital Assets***

General capital assets are those assets not specifically related to activities reported in a propriety fund. These assets are reported in the governmental activities column of the government-wide statement of net assets.

The accounting and reporting treatment applied to capital assets associated with a fund are determined by its measurement focus. General capital assets are long-lived assets of the City as a whole. When purchased, such assets are recorded as expenditures in the governmental funds and capitalized. Infrastructure, such as streets, traffic signals and signs are capitalized, including infrastructure acquired prior to the implementation of the GASB Statement entitled "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments." The valuation basis for general capital assets are historical costs, or where historical cost is not available, estimated historical

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

**Note 1 - Summary of Significant Accounting Policies - continued**

cost based on replacement cost. Donated capital assets are recorded at their fair market value on the date donated. Repairs and maintenance are recorded as expenses. Renewals and betterments are capitalized. The City maintains a capitalization threshold of one thousand dollars with the exception of infrastructure for which the threshold is twenty-five thousand dollars.

Capital assets used in operations are depreciated over their estimated useful lives using the straight-line method in the government-wide financial statements. Depreciation is charged as an expense against operations and accumulated depreciation is reported on the respective balance sheet. The range of lives used for depreciation purposes for each capital asset class is as follows:

| <u>Description</u>           | <u>Governmental Activities<br/>Estimated Lives</u> |
|------------------------------|--|
| Buildings                    | 30 years   |
| Buildings and improvements   | 10 - 20 years                                      |
| Public domain infrastructure | 25 - 35 years                                      |
| Vehicles                     | 5 - 10 years                                       |
| Office equipment             | 3 - 10 years                                       |

***Compensated Absences***

Vested or accumulated vacation leave that has matured and is expected to be liquidated with expendable available financial resources is reported as an expenditure and a fund liability of the governmental fund that will pay it. In accordance with the provisions of Governmental Accounting Standards, no liability is recorded for non-vesting accumulating rights to receive sick pay benefits.

***Long-Term Obligations***

The accounting treatment of long-term debt depends on whether the assets are used in governmental fund operations or proprietary fund operations and whether they are reported in the government-wide or fund financial statements.

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 governmental activities, statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds.

Long-term debt for governmental funds is not reported as a liability in the fund financial statements. The debt proceeds are reported as revenue and payment of principal and interest reported as expenditures. The accounting for the proprietary fund is the same in the fund statements as it is in the government-wide statements.

***Unearned/Deferred Revenue***

In the government-wide financial statements, unearned revenue represents the amount for which revenue recognition criteria have not been met. In subsequent periods, when the incurrence of qualifying expenditures has been made, the liability for the unearned revenue is removed and the revenue is recognized. In the governmental fund financial statements, revenues are deferred for amounts that are unearned or unavailable.

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

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**Note 1 - Summary of Significant Accounting Policies - continued**

***Fund Equity***

Net assets are the difference between assets and liabilities. Net assets invested in capital assets, net of related debt, are capital assets less accumulated depreciation and any outstanding debt related to the acquisition, construction or improvement of those assets.

In the governmental fund financial statements, fund balances are classified as follows:

- Non-spendable – Amounts that cannot be spent either because they are in a non-spendable form or because they are legally or contractually required to be maintained intact.
- Restricted – Amounts that can be spent only for specific purposes because of the City Charter, the City Code, state or federal laws, or externally imposed conditions by grantors or creditors.
- Committed – Amounts that can be used only for specific purposes determined by a formal action by City Commission ordinance or resolution.
- Assigned – Amounts that are designated by the Mayor for a particular purpose but are not spendable until a budget ordinance is passed or there is a majority vote approval (for capital projects or debt service) by City Commission.
- Unassigned – All amounts not included in other spendable classifications.

When an expense is incurred that can be paid using either restricted or unrestricted resources (net assets), the City's policy is to first apply the expense toward restricted resources and then toward unrestricted resources. In governmental funds, when both restricted and unrestricted resources are available for use, it is the City's policy to use externally restricted resources first, then unrestricted resources - committed, assigned and unassigned - in order as needed.

**Revenues, Expenditures and Expenses**

***Operating Revenues and Expenses***

Operating revenues and expenses for the proprietary fund are those that result from internal insurance premiums. It also includes all revenue and expenses related to capital and related financing, noncapital financing or investing activities.

***Expenditures/Expenses***

In the government-wide financial statements, expenses are classified by function for governmental activities. In the fund financial statements, governmental funds are classified as follows:

Governmental Funds – by Character

Current - Further Classified by Function  
Debt Service  
Capital Outlay

Proprietary Fund – by Operating and Non-Operating

In the fund financial statements, governmental funds report expenditures of financial resources. Proprietary funds report expenses related to the use of economic resources.

***Interfund Transactions***

Interfund services provided/used are accounted for as revenues, expenditures or expenses. Transactions that constitute reimbursements to a fund for expenditures/expenses initially made from it that are properly applicable to another fund, are recorded as expenditures/expenses in the reimbursing fund and as reductions of expenditures/expenses in the fund that is reimbursed.

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

**Note 1 - Summary of Significant Accounting Policies - continued**

***Use of Estimates***

The process of preparing financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, and designated fund balances, and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

***Budgetary Information***

Annual budgets are adopted on a basis consistent with U.S. generally accepted accounting principles for all governmental funds and for proprietary funds.

**Note 2 - Correction of Net Asset Balances in Prior Year**

The City's net assets as of June 30, 2011, have been adjusted to correct errors in classification of net asset balances. The adjustment had no effect on the change in net assets for the year ended June 30, 2011. The effect of the correction of net asset balances as of June 30, 2012, is as follows:

| <b>Net Assets</b>                               | <b>June 30, 2011<br/>(As Originally Reported)</b> | <b>Effect of<br/>Adjustment</b> | <b>June 30, 2011<br/>(As Restated)</b> |
|---|---|---------------------------------|--|
| Invested in capital assets, net of related debt | \$ 36,088,303                                     | \$ -                            | \$ 36,088,303                          |
| Restricted for capital projects                 | 1,577,223   | -                               | 1,577,223                              |
| Restricted for HUD Programs                     | 1,318,568   | 14,519,093                      | 15,837,661                             |
| Restricted for Police Incentive                 | 3,321   | -                               | 3,321                                  |
| Restricted for grant programs                   | 24,040  | -                               | 24,040                                 |
| Unrestricted                                    | <u>8,933,230</u>                                  | <u>(14,519,093)</u>             | <u>(5,585,863)</u>                     |
|   | <u>\$ 47,944,685</u>                              | <u>\$ -</u>                     | <u>\$ 47,944,685</u>                   |

**Note 3 - Stewardship, Compliance and Accountability**

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

- In accordance with City ordinance, prior to June 1, the City Manager submits to the Board of Commissioners, a proposed operating budget for the fiscal year commencing the following July 1. The operating budget includes proposed expenditures and the means of financing them for the upcoming year.
- A public meeting is conducted to obtain taxpayer comment.
- Prior to June 30, the budget is legally enacted through passage of an ordinance.
- The City Manager is required by Kentucky revised statutes to present a quarterly report to the Mayor and Board of Commissioners explaining any variance from the approved budget.
- Appropriations continue in effect until a new budget is adopted.

The Board of Commissioners may authorize supplemental appropriations during the year.



**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

**Note 3 - Stewardship, Compliance and Accountability - continued**

Expenditures may not legally exceed budgeted appropriations at the fund level. Any amendments to the budget that would change fund level totals must be approved by the Board of Commissioners. Encumbrance accounting is not employed by the City. During the year, the Board of Commissioners adopted two supplementary appropriation ordinances. Appropriations lapse at year end unless a new budget has not been adopted.

***Excess of Expenditures over Appropriations***

The following funds had expenditures in excess of legally adopted appropriations for the year ended June 30, 2012:

|                      | Budget       |    | Actual    |
|----------------------|--------------|----|-----------|
| 2005 Refunding Bonds | \$ 1,186,760 | \$ | 1,186,971 |
| Liability Insurance  | 600,000      |    | 1,366,887 |

**Note 4 - Deposits**

***Cash and Cash Equivalents***

The City maintains deposits with financial institutions insured by the Federal Deposit Insurance Corporation (FDIC). As allowed by law, the depository bank should pledge securities along with FDIC insurance at least equal to the amount on deposit at all times.

As of June 30, 2012, \$250,000 of the City's deposits are insured by the FDIC, and \$9,287,829 of the City's deposits are collateralized with securities held by the pledging institution's trust department but not in the City's name. As of June 30, 2012, the City did not have any deposits in excess of insured and/or collateralized amounts.

As of December 31, 2011, Devou Properties, Inc. (a component unit of the City) had \$1,993,245 in cash in excess of insured limits.

***Investments***

Investments are made by the City as an agent for the City Employee's Retirement Fund and the Police and Firemen's Pension Fund. The City maintains investment accounts with brokerage institutions which hold the investments registered in the City's name. As of June 30, 2012, all of the City's investments were covered by SIPC coverage or excess SIPC coverage provided by the institution, and are therefore not subject to custodial credit risk.

***Custodial Credit Risk***

For deposits and investments, custodial credit risk is the risk that in the event of the failure of the counterparty, the City will not be able to recover the value of its cash, investments or collateral securities that are in the possession of an outside party. The City has no formal policy on custodial credit risk. As of June 30, 2012, the City had \$9,287,829 of deposits collateralized with securities held by the pledging institution's trust department but not in the City's name.

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

**Note 5 - Capital Assets and Depreciation**

Capital asset activity for the fiscal year ended June 30, 2012, was as follows:

|  | <u>Balance<br/>Beginning<br/>of Year</u> | <u>Additions</u>      | <u>Retirements/<br/>Deletions</u> | <u>Balance<br/>End of Year</u> |
|--|--|-----------------------|-----------------------------------|--------------------------------|
| <b>Governmental Activities</b>                   |  |                       |                                   |                                |
| Capital assets not being depreciated             |  |                       |                                   |                                |
| Land   | \$ 14,617,829                            | \$ -                  | \$ 48,509                         | \$ 14,569,320                  |
| Land improvements                                | 1,427,370                                | 123,722               | -                                 | 1,551,092                      |
| Construction in progress                         | -  | 653,319               | -                                 | 653,319                        |
| Total capital assets not being depreciated       | <u>16,045,199</u>                        | <u>777,041</u>        | <u>48,509</u>                     | <u>16,773,731</u>              |
| Depreciable capital assets                       |  |                       |                                   |                                |
| Buildings  | 24,146,530                               | 8,591                 | 87,226                            | 24,067,895                     |
| Building improvements                            | 9,962,263                                | 1,515,643             | -                                 | 11,477,906                     |
| Infrastructure                                   | 110,886,873                              | 416,701               | -                                 | 111,303,574                    |
| Machinery and equipment                          | 4,927,527                                | 1,374,014             | 207,679                           | 6,093,862                      |
| Vehicles   | 10,933,659                               | 435,287               | 72,406                            | 11,296,540                     |
| Total depreciable capital assets                 | <u>160,856,852</u>                       | <u>3,750,236</u>      | <u>367,311</u>                    | <u>164,239,777</u>             |
| Less accumulated depreciation                    |  |                       |                                   |                                |
| Buildings  | 9,495,627                                | 599,432               | 87,226                            | 10,007,833                     |
| Building improvements                            | 8,380,715                                | 347,785               | -                                 | 8,728,500                      |
| Infrastructure                                   | 87,227,862                               | 4,280,456             | -                                 | 91,508,318                     |
| Machinery and equipment                          | 4,211,555                                | 422,609               | 207,679                           | 4,426,485                      |
| Vehicles   | 9,830,669                                | 328,850               | 72,406                            | 10,087,113                     |
| Total accumulated depreciation                   | <u>119,146,428</u>                       | <u>5,979,132</u>      | <u>367,311</u>                    | <u>124,758,249</u>             |
| Total depreciable capital assets, net            | <u>41,710,424</u>                        | <u>(2,228,896)</u>    | <u>-</u>                          | <u>39,481,528</u>              |
| Governmental activities capital assets, net      | <u>\$ 57,755,623</u>                     | <u>\$ (1,451,855)</u> | <u>\$ 48,509</u>                  | <u>\$ 56,255,259</u>           |
| <b>Component Unit</b>                            |  |                       |                                   |                                |
| Devou Properties, Inc.                           |  |                       |                                   |                                |
| Depreciable capital assets                       |  |                       |                                   |                                |
| Property and equipment                           | \$ 71,238                                | \$ 11,150             | \$ -                              | \$ 82,388                      |
| Less accumulated depreciation                    | <u>21,697</u>                            | <u>11,821</u>         | <u>-</u>                          | <u>33,518</u>                  |
| Total component unit property and equipment, net | <u>\$ 49,541</u>                         | <u>\$ (671)</u>       | <u>\$ -</u>                       | <u>\$ 48,870</u>               |

Depreciation was charged to functions as follows:

|  |                     |
|--|---------------------|
| Governmental activities                            |                     |
| General government                                 | \$ 307,540          |
| Police   | 386,470             |
| Fire   | 227,864             |
| Public improvements                                | 4,821,275           |
| Recreation   | <u>235,983</u>      |
| Total governmental activities depreciation expense | <u>\$ 5,979,132</u> |

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

**Note 6 - Interfund Activity**

Interfund receivables/payables represent short-term loans from one fund to another to cover cash overdrafts.

Much of the City's revenue is received in the general fund, then transferred to various other funds in order to fund immediate expenditures. Interfund receivables/payables were as follows at June 30, 2012:

**Due From/To Other Funds**

| <u>Receivable Fund</u>            | <u>Payable Fund</u>                | <u>Amount</u>       |
|-----------------------------------|------------------------------------|---------------------|
| General fund                      | Devou Park master plan             | \$ 523,319          |
|                                   | Police forfeiture                  | 171                 |
|                                   | CAD system                         | 60,213              |
|                                   | Police and fire incentive          | 85,299              |
|                                   | Devou Park maintenance             | 95,330              |
|                                   | Federal and state grant            | 91,807              |
|                                   | Home consortium                    | 54,239              |
|                                   | Neighborhood Stabilization Program | 40,433              |
|                                   | 2005 Refunding bonds               | <u>10,607</u>       |
|                                   |                                    | 961,418             |
| Community development block grant | General fund                       | 145,804             |
| HOME Program                      | General fund                       | 59,184              |
| Housing voucher program           | General fund                       | 20,867              |
| 2004 Pension obligation           | General fund                       | 3,342               |
| Liability insurance               | General fund                       | 851,667             |
| Medical and dental insurance      | General fund                       | <u>296,772</u>      |
|                                   |                                    | <u>\$ 2,339,054</u> |

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

**Note 6 - Interfund Activity - continued**

**Interfund Transfers**

Transfers are typically used to move unrestricted revenues collected in one fund to finance various programs accounted for in another fund in accordance with budgetary authorizations and to fund debt service payments when they become due. Much of the City's revenue is received in the general fund, then transferred to various other funds in order to fund immediate expenditures. The City made the following transfers during the fiscal year:

| <u>Transfers From</u>                 | <u>Transfer To</u>      | <u>Amount</u>       |
|---------------------------------------|-------------------------|---------------------|
| General fund                          | Devou Park maintenance  | \$ 18,307           |
|                                       | 2004 Pension obligation | 1,262,841           |
|                                       | 2005 Refunding bonds    | 1,214,033           |
|                                       | Liability insurance     | <u>1,442,500</u>    |
| Total transfers from the General fund |                         | 3,937,681           |
| Community development block grant     | General fund            | 332,500             |
| Devou Park master plan                | General fund            | 15,750              |
| Medical and dental insurance          | General fund            | 431,216             |
| CAD system                            | General fund            | <u>815,547</u>      |
|                                       |                         | <u>\$ 5,532,694</u> |

**Note 7 - Short-Term Debt**

On July 1, 2011 the city issued a Tax and Revenue Anticipation Note (TRAN) in the amount of \$3,500,000 for the purpose of providing working capital in advance of tax and revenue cash flows. This note carried a fixed interest rate of 1.24% and matured on June 30, 2012 at which time it was repaid out of the general fund.

During fiscal year 2012, the City maintained a line of credit to facilitate real estate development. The total amount of credit available is \$500,000 and the debt charges interest at 5.5%. This line of credit matures on August 1, 2012, and had an outstanding balance at June 30, 2012, of \$0. Subsequent to year end, this line of credit was not renewed.

During the year ended June 30, 2012, the following changes occurred in the City's short term debt:

|                   | <u>Balance</u><br><u>July 1, 2011</u> | <u>Issued</u>       | <u>Redeemed</u>     | <u>Balance</u><br><u>June 30, 2012</u> |
|-------------------|---------------------------------------|---------------------|---------------------|--|
| <b>Debt Issue</b> |                                       |                     |                     |  |
| TRAN              | \$ -                                  | \$ 3,500,000        | \$ 3,500,000        | \$ -                                   |
| Line of credit    | <u>187,424</u>                        | <u>-</u>            | <u>187,424</u>      | <u>-</u>                               |
|                   | <u>\$ 187,424</u>                     | <u>\$ 3,500,000</u> | <u>\$ 3,687,424</u> | <u>\$ -</u>                            |

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

**Note 8 - General Long-Term Debt**

**Capital Lease Obligations**

Capital lease obligations in the government-wide financial statements are reported as liabilities at lease inception. The related assets along with depreciation are reported at that time. Lease payments are reported as a reduction of the liability. For capital lease obligations in governmental funds, "Other Financing Sources – Lease Proceeds" and the expenditure are recorded at lease inception. Lease payments are recorded as expenditures.

The following capital lease obligations payable are payable from governmental fund revenues. The City has entered into various lease agreements as lessee for financing the acquisition of capital assets. These lease agreements qualify as capital leases for accounting purposes and therefore, have been recorded at the present value of the future minimum lease payments as of the date of their inception. The following is an analysis of the capital assets acquired through capital leases as of June 30, 2012.

|                          | <b>Capital Assets</b> |
|--------------------------|-----------------------|
| Buildings                | \$ 8,664,929          |
| Building improvements    | 534,589               |
| Equipment                | 597,819               |
| Land                     | 6,952,070             |
| Infrastructure           | 989,002               |
| Vehicles                 | 2,208,054             |
| Total cost               | 19,946,463            |
| Accumulated depreciation | 4,221,181             |
| Net book value           | \$ 15,725,282         |

The following is a schedule of the future minimum lease payments under these capital leases, and the present value of the net minimum lease payments at June 30, 2012.

|  | <b>Amount</b> |
|--|---------------|
| <b>Fiscal years ending June 30,</b>            |               |
| 2013   | \$ 1,687,510  |
| 2014   | 1,697,554     |
| 2015   | 1,708,289     |
| 2016   | 1,610,392     |
| 2017   | 1,625,857     |
| 2018 - 2022                                    | 6,909,418     |
| 2023 - 2027                                    | 2,224,925     |
| 2028 - 2032                                    | 201,331       |
| Total minimum lease payments                   | 17,665,276    |
| Less amounts representing interest             | 2,584,142     |
| Present value of future minimum lease payments | 15,081,134    |
| Less current portion                           | 1,218,660     |
| Non current portion                            | \$ 13,862,474 |

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

**Note 8 - General Long-Term Debt - continued**

The City is the lessor of office space located in the City building. These leases are on a year to year basis with cancelable terms. The City's investment in property on operating leases and property held for lease as of June 30, 2012, is as follows:

|                      |    |           |
|----------------------|----|-----------|
| Cost                 | \$ | 1,500,000 |
| Carrying amount      | \$ | 1,133,333 |
| Current depreciation | \$ | 50,000    |

**Mortgage Bonds and Notes Payable**

The following schedule summarizes outstanding long-term mortgage bonds and notes payable at June 30, 2012.

|                                  | <u>Purpose</u>    | <u>Interest Rate</u> | <u>Maturity Dates June 30,</u> | <u>Amounts</u>       |                      |
|----------------------------------|-------------------|----------------------|--------------------------------|----------------------|----------------------|
|                                  |                   |                      |                                | <u>Issued</u>        | <u>Outstanding</u>   |
| <b>Mortgage bonds</b>            |                   |                      |                                |                      |                      |
| 2003 Series                      | Refunding         | 2.00-4.50%           | 2018                           | \$ 4,996,000         | \$ 2,427,000         |
| KY Infrastructure Auth.          | Infrastructure    | 4.55%                | 2014                           | 460,327              | 50,628               |
| 2004 Series                      | Pension funding   | Variable             | 2030                           | 14,410,000           | 11,960,000           |
| 2005 Series                      | Refunding         | 3.00-3.30%           | 2013                           | 7,405,000            | 1,170,000            |
| KY Infrastructure Auth.          | Rainwater project | 2.00%                | 2030                           | 1,197,390            | 538,000              |
| KY Bond Corp. 2010 Series A      | Refinance         | 2.00%                | 2030                           | 315,000              | 165,000              |
| Recovery Zone Economic Dev Bonds | River Center      | 4.90-7.00%           | 2030                           | <u>2,650,000</u>     | <u>2,650,000</u>     |
| Total                            |                   |                      |                                | <u>\$ 31,433,717</u> | <u>\$ 18,960,628</u> |

Interest on the variable rate 2004 Series Pension Obligation Bonds is paid at the rate of interest determined by the Remarketing Agent, determined on a weekly basis. The rate was 0.192% at June 30, 2012.

The bonds may be called prior to maturity at rates and redemption premiums specified in each issue. Assuming no issues are called prior to maturity, the minimum obligations of the City at June 30, 2012, are as follows:

|                                     | <u>Principal</u>     | <u>Interest</u>     | <u>Total</u>         |
|-------------------------------------|----------------------|---------------------|----------------------|
| <b>Fiscal years ending June 30,</b> |                      |                     |                      |
| 2013                                | \$ 2,079,757         | \$ 822,700          | \$ 2,902,457         |
| 2014                                | 1,055,036            | 604,293             | 1,659,329            |
| 2015                                | 1,047,200            | 720,592             | 1,767,792            |
| 2016                                | 1,050,791            | 674,911             | 1,725,702            |
| 2017                                | 1,095,310            | 627,457             | 1,722,767            |
| 2018 - 2022                         | 4,260,696            | 2,512,962           | 6,773,658            |
| 2023 - 2027                         | 4,754,312            | 1,510,733           | 6,265,045            |
| 2028 - 2032                         | <u>3,617,526</u>     | <u>323,978</u>      | <u>3,941,504</u>     |
| Totals                              | <u>\$ 18,960,628</u> | <u>\$ 7,797,626</u> | <u>\$ 26,758,254</u> |

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

**Note 8 - General Long-Term Debt - continued**

**Interest Rate Swap**

*Objective of the Interest Rate Swap.* As a means to lower its borrowing costs, when compared against fixed-rate bonds at the time of issuance in May 2005, the City entered into an interest rate swap in connection with its \$14.4 million 2004 Series variable-rate general obligation bonds. The intention of the swap was to effectively change the City's variable interest rate on the bonds to a synthetic fixed rate of 4.56 percent. The interest rate swap is considered a hedging derivative instrument.

*Terms.* The bonds mature on December 1, 2029, and the related swap agreement matures on December 1, 2014. The swap's initial notional amount of \$14.4 million matched the \$14.4 million variable-rate bonds on an amortizing schedule. The swap was entered at the same time the bonds were issued (December 2004). Starting in fiscal year 2006, the notional value of the swap and the principal amount of the associated debt decline. Under the swap, the City pays the counterparty a fixed payment of 4.56 percent and receives a variable payment based on the London Interbank Offered Rate (LIBOR). Conversely, the bond's variable-rate coupons are based on a rate determined by the remarketing agent in accordance with the indenture.

*Fair Value.* The swap had a fair value of \$(1,174,521) as of June 30, 2012. The swap's fair value may be countered by a reduction in total interest payments required under the variable-rate bonds, creating a lower synthetic interest rate. Because the coupons on the City's variable-rate bonds adjust to changing interest rates, the bonds do not have a corresponding fair value increase or decrease.

*Credit Risk.* As of June 30, 2012, the City was exposed to credit risk in the amount of the swap's fair value. The swap counterparty was rated AA by Standard & Poor's and Aa2 by Moody's Investors Service as of June 30, 2012.

*Swap Payments and Associated Debt.* For the year ended June 30, 2012, the City did not receive any payments from the agreement. Using rates as of June 30, 2012, debt service requirements of the variable-rate debt and net swap payments, assuming current interest rates remain the same for their term, were as follows. As rates vary, variable-rate bond interest payments and net swap payments will vary.

| Fiscal years ending June 30, | <u>Variable-Rate Bonds</u> |                     | <u>Swap, Net</u>    | <u>Total</u>         |
|------------------------------|----------------------------|---------------------|---------------------|----------------------|
|                              | <u>Principal</u>           | <u>Interest</u>     |                     |                      |
| 2013                         | \$ 425,000                 | \$ 53,820           | \$ 496,290          | \$ 975,110           |
| 2014                         | 445,000                    | 51,908              | 477,144             | 974,052              |
| 2015                         | 470,000                    | 289,917             | 228,461             | 988,378              |
| 2016                         | 490,000                    | 468,950             | -                   | 958,950              |
| 2017                         | 515,000                    | 446,237             | -                   | 961,237              |
| 2018 - 2022                  | 3,000,000                  | 1,847,550           | -                   | 4,847,550            |
| 2023 - 2027                  | 3,825,000                  | 1,080,167           | -                   | 4,905,167            |
| 2028 - 2032                  | <u>2,790,000</u>           | <u>193,230</u>      | <u>-</u>            | <u>2,983,230</u>     |
| Totals                       | <u>\$ 11,960,000</u>       | <u>\$ 4,431,779</u> | <u>\$ 1,201,895</u> | <u>\$ 17,593,674</u> |

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

**Note 8 - General Long-Term Debt - continued**

**Conduit Debt Obligations**

The City has issued Industrial Revenue Bonds to provide financial assistance to private-sector entities for the acquisition and construction of industrial and commercial facilities deemed to be in the public interest. The bonds are secured by the property financed and are payable solely from payments received on the underlying mortgage loans. Upon repayment of the bonds, ownership of the acquired facilities transfers to the private-sector entity served by the bond issuance. Neither the City, state, nor any political subdivision thereof, is obligated in any manner for repayment of the bonds. Accordingly, the bonds are not reported as liabilities in the accompanying financial statements. As of June 30, 2012, there were four series of Industrial Revenue Bonds outstanding, with an aggregate principal amount payable of \$61.2 million.

During the year ended June 30, 2012, the following changes occurred in noncurrent liabilities:

| <u>Debt Issue</u>                                     | <u>Balance July 1,<br/>2011</u> | <u>Additions of<br/>New Debt</u> | <u>Repayments<br/>and Defeased</u> | <u>Balance<br/>June 30, 2012</u> | <u>Amounts<br/>Expected to be<br/>Paid in<br/>One Year</u> |
|---|---------------------------------|----------------------------------|------------------------------------|----------------------------------|--|
| Mortgage bonds and notes                              |                                 |                                  |                                    |                                  |  |
| 2003 Refunding  | \$ 2,775,000                    | \$ -                             | \$ 348,000                         | \$ 2,427,000                     | \$ 365,000   |
| HUD 108   | 330,000                         | -                                | 330,000                            | -                                | -  |
| KY Infrastructure Auth.                               | 82,531                          | -                                | 31,903                             | 50,628                           | 33,376   |
| 2005 Refunding Bonds                                  | 2,300,000                       | -                                | 1,130,000                          | 1,170,000                        | 1,170,000  |
| 2004 Series A   | 12,365,000                      | -                                | 405,000                            | 11,960,000                       | 425,000  |
| KIA Rainwater Harvest                                 | 561,818                         | -                                | 23,818                             | 538,000                          | 24,296   |
| KY Bond Corp 2010<br>Series A                         | 225,000                         | -                                | 60,000                             | 165,000                          | 62,085   |
| Recovery zone bonds                                   | <u>2,650,000</u>                | <u>-</u>                         | <u>-</u>                           | <u>2,650,000</u>                 | <u>-</u>   |
| Total mortgage bonds and notes                        | 21,289,349                      | -                                | 2,328,721                          | 18,960,628                       | 2,079,757  |
| Capital lease obligations<br>infrastructure/equipment | 16,247,510                      | -                                | 1,166,376                          | 15,081,134                       | 1,218,660  |
| Compensated absences                                  | <u>1,590,784</u>                | <u>1,213,651</u>                 | <u>1,522,847</u>                   | <u>1,281,588</u>                 | <u>1,281,588</u>   |
| Total noncurrent liabilities                          | <u>\$ 39,127,643</u>            | <u>\$ 1,213,651</u>              | <u>\$ 5,017,944</u>                | <u>\$ 35,323,350</u>             | <u>\$ 4,580,005</u>  |

Compensated absences will be liquidated by the City's general fund. Compensated absences are required to be used within one year, therefore the balance is classified as a current liability.



**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

**Note 9 - Risk Management**

The City is exposed to various risks to loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters. The City has established a Liability Self Insurance Fund (an internal service fund) to account for and finance its uninsured risks of loss. Under this program, the Liability Self Insurance Fund provides coverage for all losses. The City purchases commercial insurance for fire and extended coverage losses.

All funds of the City participate in the program and make payments to the Liability Self Insurance Fund; however, the payments are not based on actuarial estimates of the amounts needed to pay prior and current-year claims but are intended to establish a reserve for catastrophic losses. That reserve was \$792,500 at June 30, 2012, and is a designation of the Liability Self Insurance Fund retained earnings. The claims liability reported in the Fund at June 30, 2012, is based on the requirements of governmental accounting standards, which requires that a liability for claims be reported if information prior to the issuance of the financial statements indicates that it is probable that a liability has been incurred at the date of the financial statements and the amount of the loss can be reasonably estimated. Changes in the Fund's claims liability amount were:

| <u>July 1, 2010</u> | <u>Claims and<br/>Changes in<br/>Estimates</u> | <u>Claims<br/>Payments</u> | <u>June 30, 2011</u> | <u>Claims and<br/>Changes in<br/>Estimates</u> | <u>Claims<br/>Payments</u> | <u>June 30, 2012</u> |
|---------------------|--|----------------------------|----------------------|--|----------------------------|----------------------|
| \$ 820,823          | \$ 269,930                                     | \$1,090,753                | \$ -                 | \$ 1,199,357                                   | \$ 406,857                 | \$ 792,500           |

The City has also established a Medical Self Insurance Fund. Employees may elect to participate in this program or certain other medical insurance programs offered by the City. Under this program the first \$125,000 of a participants' medical claims are payable by the Medical Self Insurance Fund. The City purchases insurance for claims in excess of coverage provided by the fund. All funds of the City participate in the program and make payments to the Medical Self Insurance Fund based on historical estimates of the amounts needed to pay prior and current year claims. The claims liability of \$993,291 reported in the fund at June 30, 2012, is based upon the requirements of governmental accounting standards, as explained above. Changes in the fund's claims liability amount during the year ended June 30, 2012, were as follows:

| <u>July 1, 2010</u> | <u>Claims and<br/>Changes in<br/>Estimates</u> | <u>Claims<br/>Payments</u> | <u>June 30, 2011</u> | <u>Claims and<br/>Changes in<br/>Estimates</u> | <u>Claims<br/>Payments</u> | <u>June 30, 2012</u> |
|---------------------|--|----------------------------|----------------------|--|----------------------------|----------------------|
| \$ 873,533          | \$ 6,376,011                                   | \$6,411,584                | \$ 837,960           | \$ 5,277,809                                   | \$ 5,122,478               | \$ 993,291           |

There have been no significant reductions in insurance coverage from the prior year.

There have been no settlements in excess of insurance coverage in the past three years.

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

**Note 10 - Employee Retirement Plans**

The City of Covington maintains two single employer, defined benefit pension plans: Employees' Pension Plan and Police and Firemen's Pension Plan. A separate, audited post-employment benefit plan report prepared in accordance with U.S. generally accepted accounting principles is not available for these plans.

**Summary of Significant Accounting Policies**

*Basis of Accounting.* The plan's financial statements are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions to each plan are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of each plan.

*Method Used to Value Investments.* Investments are reported at fair value. Short-term investments are reported at cost, which approximates fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Mortgages are valued on the basis of future principal and interest payments, and are discounted at prevailing interest rates for similar instruments. The fair value of real estate investments is based on independent appraisals. Investments that do not have an established market are reported at estimated fair value. The plans issued separate financial statements which may be obtained by request from the City of Covington.

**Plan Descriptions and Contribution Information**

Membership of each plan consisted of the following at the date of the latest actuarial valuation:

| Group   | Employees'<br>Pension Plan<br>July 1, 2012 | Police and<br>Firemen's<br>Pension Plan<br>July 1, 2012 |
|---|--|---|
| Retirees and beneficiaries currently receiving benefits | 50   | 78  |
| Active employees - fully vested                         | <u>2</u>                                   | <u>-</u>  |
|   | <u>52</u>                                  | <u>78</u>   |

**Employees' Pension Plan**

*Plan Description.* The Employees' Pension Plan is a single employer defined benefit pension plan that covers substantially all non public safety employees hired prior to April 1, 1997. The plan provides retirement, disability and death benefits to plan members and their beneficiaries. Cost-of-living adjustments (COLA) are provided at the discretion of the Board of Trustees. Benefits are provided and may be amended by City ordinance.

*Contributions.* Plan members are required to contribute 8% of their annual covered salary. The City is required to contribute at an actuarially determined rate. Contribution requirements of the plan members and the City are established and may be amended by City ordinance. Administrative costs are financed through investment earnings.

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

**Note 10 - Employee Retirement Plans - continued**

**Police and Firemen's Pension Plan**

*Plan Description.* The Police and Firemen's Pension Plan is a single employer defined benefit pension plan that covers all retired police and firemen who were receiving benefits prior to August 1, 1989. The plan provides retirement, disability, and death benefits to plan members and their beneficiaries. Cost-of-living adjustments are provided at the discretion of the Board of Trustees. Benefits are provided under Kentucky Revised Statutes (KRS) 95.852 to 95.991.

*Contributions.* There are no active employees contributing to the plan. The City is required to contribute at an actuarially determined rate. Contribution requirements of the City are established under KRS 95.868. Administrative costs are financed through investment earnings.

**Employer Contributions**

| Years Ended June 30, | Employees' Pension Plan      |                    |                        | Police and Firemen's Pension Plan |                    |                        |
|----------------------|------------------------------|--------------------|------------------------|-----------------------------------|--------------------|------------------------|
|                      | Annual Required Contribution | Contributions Made | Percentage Contributed | Annual Required Contribution      | Contributions Made | Percentage Contributed |
| 2012                 | \$ 304,163                   | \$ -               | - %                    | \$ 796,500                        | \$ -               | - %                    |
| 2011                 | \$ 304,163                   | \$ -               | - %                    | \$ 342,169                        | \$ -               | - %                    |
| 2010                 | \$ 304,163                   | \$ -               | - %                    | \$ 396,747                        | \$ -               | - %                    |

During the year ended June 30, 2005, the City issued Pension Obligation Bonds for the purpose of funding both Pension Plans. As a result, the City has a net pension obligation asset on the government-wide statement of net assets. As of June 30, 2012, the Plan liabilities in both the Police and Firemen's Pension Plan and the Employees' Pension Plan exceeded the assets. Therefore, the City did have an unfunded accrued liability in the Police and Firemen's Pension Plan or the Employees' Pension Plan. The City is required by state statute to contribute impounding lot income and required contributions into the Police and Firemen's Pension Plan each year.

**Funded Status and Funding Progress**

| Actuarial Valuation Date July 1,         | Actuarial Value of Assets (a) | Actuarial Accrued Liability (AAL) Entry Age (b) | Unfunded AAL (UAAL) (b-a) | Funded Ratio (a/b) | Covered Payroll (c) | UAAL as a Percentage of Covered Payroll [(b-a)/c] |
|--|-------------------------------|---|---------------------------|--------------------|---------------------|---|
| <b>Employees' Pension Plan</b>           |                               |   |                           |                    |                     |   |
| 2011                                     | \$ 4,002,169                  | \$ 5,363,292                                    | \$ 1,361,123              | 75 %               | \$ 105,615          | 1,289 %   |
| 2009                                     | 3,867,919                     | 5,955,714                                       | 2,087,795                 | 65 %               | 105,381             | 1,981 %   |
| 2007                                     | 6,650,730                     | 6,605,645                                       | (45,085)                  | 101 %              | 114,311             | N/A   |
| <b>Police and Firemen's Pension Plan</b> |                               |   |                           |                    |                     |   |
| 2012                                     | \$ 8,062,246                  | \$ 11,315,285                                   | \$ 3,253,039              | 71 %               | N/A                 | N/A   |
| 2011                                     | 9,573,902                     | 11,003,692                                      | 1,429,790                 | 87 %               | N/A                 | N/A   |
| 2010                                     | 9,116,577                     | 11,465,252                                      | 2,348,675                 | 80 %               | N/A                 | N/A   |

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

**Note 10 - Employee Retirement Plans - continued**

An actuarial valuation report was not prepared as of July 1, 2010 or July 1, 2012, for the Employees' Pension Plan.

**Annual Pension Cost and Net Pension Obligation**

The City's annual pension cost and net pension obligation to each plan for the current year were as follows:

|                                       | <u>Employees'<br/>Pension Plan</u> | <u>Police and<br/>Firemen's<br/>Pension Plan</u> |
|---------------------------------------|------------------------------------|--|
| Annual Required Contribution (ARC)    | \$ 304,163                         | \$ 796,500                                       |
| Interest on Net Pension Obligation    | (97,634)                           | (248,418)  |
| Adjustment to ARC                     | <u>321,755</u>                     | <u>818,669</u>                                   |
| Annual Pension Cost                   | 528,284                            | 1,366,751  |
| Actual Contributions Made             | <u>-</u>                           | <u>-</u>   |
| Increase in Net Pension Obligation    | 528,284                            | 1,366,751  |
| Net Pension Asset - beginning of year | <u>(1,301,784)</u>                 | <u>(3,312,238)</u>                               |
| Net Pension Asset - end of year       | \$ <u>(773,500)</u>                | \$ <u>(1,945,487)</u>                            |

**Three-Year Trend Information**

| <u>Years Ended</u>                       | <u>Annual Pension<br/>Cost (APC)</u> | <u>Percentage of<br/>APC Contributed</u> | <u>Change in Net<br/>Pension<br/>Obligation</u> | <u>Balance of<br/>Net Pension<br/>Asset</u> |
|--|--------------------------------------|--|---|---|
| <b>Employees' Pension Plan</b>           |                                      |  |   |   |
| June 30, 2012                            | \$ 528,284                           | - %                                      | \$ 528,284                                      | \$ (773,500)                                |
| June 30, 2011                            | 638,151                              | - %                                      | 638,151   | (1,301,784)                                 |
| June 30, 2010                            | 663,563                              | - %                                      | 663,562   | (1,939,935)                                 |
| <b>Police and Firemen's Pension Plan</b> |                                      |  |   |   |
| June 30, 2012                            | \$ 1,366,751                         | - %                                      | \$ 1,366,751                                    | \$ (1,945,487)                              |
| June 30, 2011                            | 1,102,176                            | - %                                      | 1,102,176                                       | (3,312,238)                                 |
| June 30, 2010                            | 1,167,270                            | - %                                      | 1,167,270                                       | (4,414,414)                                 |

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

**Note 10 - Employee Retirement Plans - continued**

The information presented in this note was determined as part of the actuarial valuations at the dates indicated. The entry age or the projected unit credit actuarial cost method is used in the valuations. Additional information as of the latest actuarial valuation follows

|                               | <b>Employees'<br/>Pension Plan</b> | <b>Police and<br/>Firemen's<br/>Pension Plan</b> |
|-------------------------------|------------------------------------|--|
| Valuation date                | July 1, 2011                       | July 1, 2012                                     |
| Actuarial cost method         | Entry Age                          | Unit Credit                                      |
| Amortization method           | Level Percent                      | Level Percent                                    |
|                               | Closed                             | Closed   |
| Remaining amortization period | Ten Years                          | Ten Years  |
| Asset valuation method        | Market                             | Market   |
| Actuarial assumptions         |                                    |  |
| Investment rate of return *   | 7.5 %                              | 7.5 %  |
| Projected salary increases *  | 6.0 %                              | - %  |
| * includes inflation at       | - %                                | - %  |
| Cost-of-living adjustments    | - %                                | - %  |

**County Employees Retirement System (CERS)**

City employees hired subsequent to April 1, 1977, who work at least 100 hours per month participate in the County Employees Retirement System (CERS). Under the provisions of Kentucky Revised Statute 61.645, the Board of Trustees of Kentucky Retirement Systems administers the CERS.

The plan issues separate financial statements which may be obtained by request from Kentucky Retirement Systems, 1260 Louisville Road, Frankfort, Kentucky 40601.

Plan Description – CERS is a cost-sharing multiple-employer defined benefit pension plan that covers substantially all regular full-time members employed in positions of each county and school board, and any additional eligible local agencies electing to participate in the System. The plan provides for retirement, disability, and death benefits to plan members. Retirement benefits may be extended to beneficiaries of plan members under certain circumstances. Cost-of-living adjustments are provided at the discretion of the state legislature.

Non-Hazardous Contributions – For the year ended June 30, 2012, plan members were required to contribute 5% (for members before September 1, 2008) and 6% (for members on or after September 1, 2008) of their annual creditable compensation. Participating employers were required to contribute at an actuarially determined rate. Per Kentucky Revised Statute Section 61.565(3), normal contribution and past service contribution rates shall be determined by the Board on the basis of an annual valuation last preceding July 1 of a new biennium. The Board may amend contribution rates as of the first day of July of the second year of a biennium, if it is determined on the basis of a subsequent actuarial valuation that amended contribution rates are necessary to satisfy requirements determined in accordance with actuarial bases adopted by the Board. For the year ended June 30, 2012, participating employers contributed 18.96% of creditable compensation. Administrative costs of CERS are financed through employer contributions and investment earnings.

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

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**Note 10 - Employee Retirement Plans - continued**

Hazardous Contributions – For the year ended June 30, 2012, plan members were required to contribute 8% (for members before September 1, 2008) and 9% (for members on or after September 1, 2008) of their annual creditable compensation. The City was required to contribute at an actuarially determined rate. Per Kentucky Revised Statute Section 61.565(3), normal contribution and past service contribution rates shall be determined by the Board on the basis of an annual valuation last preceding July 1 of the second year of a biennium, if it is determined on the basis of a subsequent actuarial valuation that amended contribution rates are necessary to satisfy requirements determined in accordance with actuarial bases adopted by the Board. For the year ended June 30, 2012, participating employers contributed 35.76% of each employee's creditable compensation. Administrative costs of CERS are financed through employer contributions and investment earnings.

**Note 11 - Contingencies**

The City is a defendant in various lawsuits. Although the outcome of these lawsuits is not presently determinable, in the opinion of the City's attorney, the resolution of these matters will not have a material adverse effect on the financial condition of the City.

The City is a defendant in a lawsuit. The suit was filed by an individual for development rights and damages. The suit does not specify damages however; the City's counsel has advised that the case has potential for a large judgment, up to \$300,000. The City's counsel has advised that at this stage in the proceeding he cannot offer an opinion as to the probable outcome. The City believes the action is without merit and intends to vigorously defend its position.

The City is party to a potential action filed by the firefighters union regarding calculation of overtime pay. The union is seeking to have its members compensated for an overtime calculation over and above what was specified by the collective bargaining agreement. The parties have reached a settlement, pending approval from the labor cabinet, on the amount to be paid each firefighter. The reserve for this contingency of \$644,000 is recorded as an estimated liability for claims in the Liability Self Insurance Fund.

The City is a defendant in a lawsuit. The suit was filed by a company for wrongful death. The suit does not specify damages, however, the City's counsel has advised that the case has potential for a large judgment, up to \$100,000. The City's counsel has advised that at this stage in the proceeding he cannot offer an opinion as to the probable outcome. The City believes the action is without merit and intends to vigorously defend its position.

A potential liability exists related to the City's medical self insurance fund for a health insurance claim that the City's stop loss insurance carrier has denied. The City and its third party administrator are challenging this determination and have joined other cities in filing suit against the insurance carrier for payment of this and similar claims. In the event the City is unsuccessful in this challenge, the claim, totaling \$1.8 million, will be paid by the City's medical self insurance fund. At this time the City cannot offer an opinion as to the probable outcome.

**City of Covington, Kentucky**  
**Notes To The Basic Financial Statements**  
**For the Year Ended June 30, 2012**

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**Note 11 - Contingencies - continued**

Amounts grantor agencies pay to the City are subject to audit and adjustments by the grantor, principally the federal government. The grantor may require refunding by the City for any disallowed costs. Management cannot determine amounts grantors may disallow in future periods. However, based on prior experience, management believes any refunds would be immaterial to its financial statement as of June 30, 2012.

**Note 12 - Subsequent Events**

The Company has evaluated subsequent events for potential recognition and disclosure through December 31, 2012, the date the financial statements were available to be issued.

**Note 13 - Future Accounting Pronouncements**

The City plans to adopt GASB. Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, required for periods beginning after December 15, 2011. This statement establishes accounting and financial reporting requirements for service concession arrangements. Management is in the process of determining the effects that the adoption of this Statement will have on the City's financial statements.

The City plans to adopt GASB. Statement No. 61, *The Financial Reporting Entity: Omnibus-an Amendment of GASB Statements No. 14 and No. 34*, required for periods beginning after June 15, 2012. This Statement amends certain reporting entity issues related to component units and equity interests in joint ventures. Management is in the process of determining the effects that the adoption of this Statement will have on the City's financial statements.

The City plans to adopt GASB. Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, required for periods beginning after December 15, 2011. This Statement incorporates into the GASB's authoritative literature certain accounting and financial reporting guidance, included in certain FASB and AICPA pronouncements issued prior to November 30, 1989, which does not conflict with or contradict GASB pronouncements. Management is in the process of determining the effects that the adoption of this Statement will have on the City's financial statements.

The City plans to adopt GASB. Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position*, required for periods beginning after December 15, 2011. This Statement provides financial reporting guidance for deferred outflows and deferred inflows of resources, and identifies net position as the residual of all other elements presented in a statement of financial position. Management is in the process of determining the effects that the adoption of this Statement will have on the City's financial statements.

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