

**City of Lock Haven,
Pennsylvania**

Financial Statements and
Supplementary Information

December 31, 2012

City of Lock Haven, Pennsylvania

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Independent Auditors' Report

Honorable Members of City Council
City of Lock Haven, Pennsylvania

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Lock Haven, Pennsylvania (the "City"), as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the Lock Haven Area Flood Protection Authority (the "Flood Protection Authority"), which represents 100% of the assets, net position, and revenues of the discretely presented component unit. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Flood Protection Authority, is based solely 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

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 business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Lock Haven, Pennsylvania, as of December 31, 2012, and the respective changes in net position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Management has omitted Management's Discussion and Analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not 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. Our opinion on the basic financial statements is not affected by this missing information.

Accounting principles generally accepted in the United States of America require that the Schedule of Funding Progress – Pension Trust Funds, Schedule of Employer Contributions – Pension Trust Funds, and Notes to Required Supplementary Information Pension Trust Funds on pages 48 - 50 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.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's financial statements. The schedule of expenditures of federal awards, required by the U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates 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 other 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 schedule of expenditures of federal awards is fairly stated in all material respects in relation to the financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated September 3, 2013 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.

ParenteBeard LLC

Williamsport, Pennsylvania
September 3, 2013

City of Lock Haven, Pennsylvania

Statement of Net Position

December 31, 2012

	Primary Government			Component Unit - Flood Protection Authority
	Governmental Activities	Business-type Activities	Total	
Assets				
Cash and cash equivalents	\$ 692,954	\$ 1,822,919	\$ 2,515,873	\$ 3,821
Restricted cash	-	972,178	972,178	-
Receivables (net of allowance for uncollectibles):				
Taxes	309,181	-	309,181	-
Loans	415,500	-	415,500	-
Other	11,126	725,678	736,804	-
Internal balances	328,437	(328,437)	-	-
Due from other governments	141,611	3,244,710	3,386,321	-
Other current assets	-	5,422	5,422	-
Capital assets:				
Public utility systems (including equipment)	-	16,249,748	16,249,748	84,590,355
Land and improvements	5,021,113	2,621,863	7,642,976	-
Infrastructure and infrastructure in progress	2,617,349	-	2,617,349	-
Buildings	3,925,614	-	3,925,614	-
Equipment and furniture	3,094,670	741,095	3,835,765	-
Construction in progress	1,194,198	13,233,167	14,427,365	-
Less: accumulated depreciation	(6,488,160)	(9,513,741)	(16,001,901)	(11,842,644)
Total capital assets	9,364,784	23,332,132	32,696,916	72,747,711
Deferred charges	31,323	220,946	252,269	-
Total assets	11,294,916	29,995,548	41,290,464	72,751,532
Liabilities				
Accounts payable and accrued expenses	97,684	3,515,758	3,613,442	538
Due to other governments	-	4,865	4,865	-
Deferred revenues	400,224	5,875	406,099	-
Long-term liabilities:				
Due within one year:				
Bonds and notes payable	333,136	593,778	926,914	-
Due in more than one year:				
Bonds and notes payable	805,137	14,559,697	15,364,834	-
Compensated absences	159,303	59,415	218,718	-
Other postemployment benefit obligation	1,823,746	-	1,823,746	-
Total liabilities	3,619,230	18,739,388	22,358,618	538
Net Position				
Net investment in capital assets	8,257,834	9,371,781	17,629,615	72,747,711
Restricted for:				
Capital projects	574,790	-	574,790	-
Program purposes	67,580	-	67,580	-
Unrestricted	(1,224,518)	1,884,379	659,861	3,283
Total net position	\$ 7,675,686	\$ 11,256,160	\$ 18,931,846	\$ 72,750,994

See notes to financial statements

City of Lock Haven, Pennsylvania

Statement of Activities
Year Ended December 31, 2012

Functions/Programs	Net (Expenses) Revenue And Changes In Net Assets						Component Unit
	Program Revenues		Primary Government Business-type Activities		Total		
	Charges for Services	Operating Grants And Contributions	Capital Grants And Contributions	Governmental Activities	Business-type Activities	Flood Protection Authority	
Primary Government							
Governmental activities:							
General government	\$ 861,946	\$ 453,581	\$ 199,302	\$ 111,228	\$	\$ 111,228	
Public safety	2,336,750	438,866	-	(1,745,378)	-	(1,745,378)	
Public works	588,155	182,558	-	(332,412)	-	(332,412)	
Health, welfare and sanitation	25,940	3,660	-	(22,280)	-	(22,280)	
Culture and recreation	170,358	-	-	(170,358)	-	(170,358)	
Buildings and property	242,972	-	-	(242,972)	-	(242,972)	
Interest on long-term debt	50,786	-	-	(50,786)	-	(50,786)	
Employee benefits and insurance	1,353,690	247,578	-	(1,106,112)	-	(1,106,112)	
Other	158,323	-	-	(14,750)	-	(14,750)	
Unallocated depreciation	501,735	-	-	(501,735)	-	(501,735)	
Total governmental activities	6,260,655	1,326,243	199,302	(4,075,555)		(4,075,555)	
Business-type activities:							
Public utility services - Water	1,803,185	-	224,983	-	\$ 42,652	42,652	
Public utility services - Sanitary sewer	1,729,621	-	6,750,214	-	7,551,739	7,551,739	
William T. Piper Memorial Airport	488,365	-	786,374	-	649,655	649,655	
Total business-type activities	4,021,171	-	7,761,571	-	8,244,046	8,244,046	
Total primary government	\$ 10,281,826	\$ 1,326,243	\$ 7,960,873	(4,075,555)	8,244,046	4,168,491	
Component Unit,							
Lock Haven Area Flood Protection Authority	\$ 855,315	\$ 9,000	\$ -	\$ -	\$ -	\$ -	\$ (846,315)
General Revenues:							
Taxes				2,737,224		2,737,224	
Grants and contributions not restricted to specific programs				235,419		235,419	
Unrestricted investment earnings				1,908	13,216	15,124	1
Miscellaneous				192,135	63,255	255,390	-
Gain on sale of asset				-	12,184	12,184	-
Transfers				(6,410)	6,410	-	-
Total general revenues				3,160,276	95,065	3,255,341	1
Change in Net Position				(915,279)	8,339,111	7,423,832	(846,314)
Net Position - Beginning				8,590,965	2,917,049	11,508,014	73,597,308
Net Position, Ending				\$ 7,675,686	\$ 11,256,160	\$ 18,931,846	\$ 72,750,994

See notes to financial statements

City of Lock Haven, Pennsylvania

Balance Sheet
 Governmental Funds
 December 31, 2012

	<u>General Fund</u>	<u>Capital Projects</u>	<u>Nonmajor Governmental Funds</u>	<u>Total Governmental Funds</u>
Assets				
Cash and cash equivalents	\$ 65,283	\$ 492,838	\$ 134,833	\$ 692,954
Receivables:				
Taxes	309,181	-	-	309,181
Loans	-	-	415,500	415,500
Other governments	100,612	-	40,999	141,611
Due from other funds	<u>110,542</u>	<u>81,952</u>	<u>338,412</u>	<u>530,906</u>
Total assets	<u>\$ 585,618</u>	<u>\$ 574,790</u>	<u>\$ 929,744</u>	<u>\$ 2,090,152</u>
Liabilities and Fund Balances				
Liabilities:				
Vouchers (accounts) payable	\$ 38,853	\$ -	\$ 9,231	\$ 48,084
Accrued liabilities	36,389	-	3,963	40,352
Due to other funds	191,623	-	829	192,452
Deferred revenue	<u>278,267</u>	<u>-</u>	<u>397,743</u>	<u>676,010</u>
Total liabilities	<u>545,132</u>	<u>-</u>	<u>411,766</u>	<u>956,898</u>
Fund balances:				
Restricted	-	574,790	539,985	1,114,775
Assigned	65,283	-	-	65,283
Unassigned	<u>(24,797)</u>	<u>-</u>	<u>(22,007)</u>	<u>(46,804)</u>
Total fund balances	<u>40,486</u>	<u>574,790</u>	<u>517,978</u>	<u>1,133,254</u>
Total liabilities and fund balances	<u>\$ 585,618</u>	<u>\$ 574,790</u>	<u>\$ 929,744</u>	<u>\$ 2,090,152</u>

See notes to financial statements

City of Lock Haven, Pennsylvania

Reconciliation of the Governmental Funds Balance Sheet
to the Statement of Net Position
December 31, 2012

Total Fund Balance, Governmental Funds \$ 1,133,254

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

Capital assets used in governmental activities are not current
financial resources and therefore are not reported in the
fund financial statements, but are reported in the governmental
activities of the statement of net position. 9,364,784

Some of the City's taxes will be collected after year-end, but
are not available soon enough to pay for the current period's
expenditures, and therefore are reported as deferred revenue
in the funds. 275,786

Deferred financing costs related to issuance of debt are
deferred and amortized over life of the debt in statement
of activities. 31,323

Internal service funds are used by management to charge the
costs of certain activities to individual funds. The assets
and liabilities of the internal service fund are included in the
governmental activities of the statement of net position. (8,139)

Long-term liabilities applicable to the City's governmental activities
are not due and payable in the current period and accordingly,
are not reported as fund liabilities. All liabilities, both current and long-term,
are reported in the statement of net position. Balances at December
31, 2012 are:

Bonds and notes payable	(1,138,273)
Other postemployment benefit obligation	(1,823,746)
Compensated absences	<u>(159,303)</u>

Net Assets of Governmental Activities
in the Statement of Net Position \$ 7,675,686

See notes to financial statements

City of Lock Haven, Pennsylvania

Statement of Revenues, Expenditures and Changes in Fund Balances

Governmental Funds

Year Ended December 31, 2012

	General Fund	Capital Projects	Nonmajor Governmental Funds	Total
Revenues				
Taxes	\$ 2,699,178	\$ -	\$ -	\$ 2,699,178
Licenses and permits	205,227	-	-	205,227
Fines and forfeits	152,506	-	-	152,506
Interest, rents and royalties	756	622	530	1,908
Intergovernmental	395,185	199,302	1,076,797	1,671,284
Charges for service	116,658	-	43,185	159,843
Collections on loans	-	-	125,909	125,909
Miscellaneous	107,463	-	43,326	150,789
Total revenues	3,676,973	199,924	1,289,747	5,166,644
Expenditures				
Current:				
General government	344,314	-	355,257	699,571
Employee benefits and insurance	1,339,624	-	13,934	1,353,558
Buildings and property	242,713	-	-	242,713
Community and economic development	-	-	31,120	31,120
Public works - highways and streets	376,123	-	318,296	694,419
Health and sanitation	25,940	-	-	25,940
Public safety	1,307,631	-	438,876	1,746,507
Culture and recreation	125,288	-	36,198	161,486
Other	10,615	-	15,749	26,364
Capital outlay	-	328,429	285	328,714
Debt service	213,282	681,008	-	894,290
Total expenditures	3,985,530	1,009,437	1,209,715	6,204,682
Deficiency of Revenues Over Expenditures	(308,557)	(809,513)	80,032	(1,038,038)
Other Financing Sources (Uses)				
Proceeds from the sale of capital assets	5,774	-	-	5,774
Proceeds from long-term debt, net	-	1,996	-	1,996
Transfers in	40,000	46,572	28,429	115,001
Transfers out	(81,411)	(40,000)	-	(121,411)
Total other financing (uses) sources, net	(35,637)	8,568	28,429	1,360
Change in Fund Balances	(344,194)	(800,945)	108,461	(1,036,678)
Fund Balance, Beginning	384,683	1,375,735	409,513	2,169,931
Fund Balance, Ending	\$ 40,486	\$ 574,790	\$ 517,978	\$ 1,133,254

See notes to financial statements

City of Lock Haven, Pennsylvania

Reconciliation of The Statement of Revenues, Expenditures
and Changes in Fund Balances of Governmental
Funds to the Statement of Activities
Year Ended December 31, 2012

Net Change in Fund Balances - Total Governmental Funds	\$ (1,036,678)
Amounts reported for governmental activities in the statement of activities are different because:	
Governmental funds report outlays for capital assets as expenditures because such outlays use current financial resources. In contrast, the statement of activities reports only a portion of the outlay as expense. The outlay is allocated over the assets' estimated useful lives as depreciation expense for the period. This is the amount by which depreciation, \$501,735 exceeded capital outlays, \$359,491, in the current period.	(142,244)
Revenues related to real estate taxes in the statement of activities that do not provide current financial resources are not reported as revenues in the funds. This amount represents the change in deferred tax revenues for the year ended December 31, 2012.	38,045
The issuance of long-term debt (e.g. bonds, notes, etc.) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Also, governmental funds report the effect of costs of issuance of debt when the debt is originally issued, whereas these amounts are deferred and amortized in the statement of activities. During 2012, the following transactions factor into this reconciliation:	
Issuance of long-term debt	(1,996)
Retirement of principal of long-term debt	856,455
Amortization of issuance costs	<u>(14,948)</u>
	839,511
Certain compensated absences payable are considered long-term in nature, and are not reported as liabilities within the funds. Such liabilities are, however, reported within the statement of net assets, and changes in these liabilities are reflected within the statement of activities. This amount represents the change in long-term compensated absences payable for the year ended December 31, 2012.	(4,374)
Other postemployment benefit ("OPEB") expense reported in the statement of activities is recognized on the accrual basis. The net OPEB obligation is adjusted for any difference between OPEB expense and contributions made in relation to the annual required contribution (ARC).	(605,404)
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 within governmental activities.	<u>(4,135)</u>
Change in Net Assets of Governmental Activities	<u>\$ (915,279)</u>

See notes to financial statements

City of Lock Haven, Pennsylvania

Statement of Revenues, Expenditures and
Changes in Fund Balance - General Fund
Budget and Actual
Year Ended December 31, 2012

	Budgeted Amounts		Actual Amounts	Adjustments	Actual Amounts	Variance
	Original	Final	GAAP Basis	Budgetary Basis	Budgetary Basis	With Final Budget
Revenues						
Taxes	\$ 2,705,800	\$ 2,785,397	\$ 2,699,178	\$ (56,879)	\$ 2,642,299	\$ (143,098)
Licenses And Permits	67,200	204,086	205,227	-	205,227	1,141
Fines And Forfeits	161,500	161,500	152,506	-	152,506	(8,994)
Interest, Rents And Royalties	800	800	756	-	756	(44)
Intergovernmental	360,605	406,605	395,185	-	395,185	(11,420)
Charges For Services	114,230	130,913	116,658	-	116,658	(14,255)
Miscellaneous	106,100	94,271	107,463	-	107,463	13,192
Total revenues	3,516,235	3,783,572	3,676,973	(56,879)	3,620,094	(163,478)
Expenditures:						
Current:						
General Government	317,700	352,330	344,314	(582)	343,732	8,598
Employee Benefits And Insurance	1,248,701	1,340,991	1,339,624	(1,768)	1,337,856	3,135
Public Safety	1,222,074	1,310,389	1,307,631	(20,089)	1,287,542	22,847
Public Works - Highways And Streets	264,872	336,598	376,123	(7,083)	369,040	(32,442)
Building And Property	222,809	246,909	242,713	(2,622)	240,091	6,818
Health And Sanitation	28,175	26,766	25,940	-	25,940	826
Culture And Recreation	105,539	106,131	125,288	(1,600)	123,688	(17,557)
Other	7,148	7,971	10,615	-	10,615	(2,644)
Debt Service, Principal	212,716	213,484	213,282	-	213,282	202
Total expenditures	3,629,734	3,941,569	3,985,530	(33,744)	3,951,786	(10,217)
(Deficiency) Excess of Revenues Over Expenditures	(113,499)	(157,997)	(308,557)	(23,135)	(331,692)	(173,695)
Other Financing Sources (Uses):						
Proceeds From the Sale of Capital Assets	1,000	5,498	5,774	-	5,774	276
Proceeds From Long-term Debt, Net	83,000	83,000	-	-	-	(83,000)
Transfers In	-	40,000	40,000	-	40,000	-
Transfers Out	(6,100)	(6,100)	(81,411)	78,911	(2,500)	3,600
Appropriated Fund Balance	35,599	35,599	-	-	-	(35,599)
Total other financing (uses) sources, net	113,499	157,997	(35,637)	78,911	43,274	(114,723)
(Deficiency) Excess of Revenues Over Expenditures After Other Financing Sources (Uses)	\$ -	\$ -	\$ (344,194)	\$ 55,776	\$ (288,418)	\$ (288,418)

See notes to financial statements

City of Lock Haven, Pennsylvania

Statement of Net Position

Proprietary Funds

December 31, 2012

	Enterprise Funds				Internal Service Fund
	Water	Sewer	Airport Operating	Total	
Assets					
Current assets:					
Cash and cash equivalents	\$ -	\$ 1,822,919	\$ -	\$ 1,822,919	\$ -
Other accounts receivable, (net of allowance)	331,311	359,261	35,106	725,678	11,126
Due from other funds	71,576	86,320	40,166	198,062	-
Due from other governments	9,044	3,222,481	13,185	3,244,710	-
Restricted cash	-	972,178	-	972,178	-
Bond issuance costs	24,475	179,003	17,468	220,946	-
Other current assets	5,422	-	-	5,422	-
Total current assets	441,828	6,642,162	105,925	7,189,915	11,126
Capital assets:					
Public utility systems (including related equipment)	7,508,493	8,741,255	-	16,249,748	-
Land and improvements	-	500,000	2,121,863	2,621,863	-
Equipment and vehicles	-	-	741,095	741,095	-
Construction in progress	-	13,231,397	1,770	13,233,167	-
Less accumulated depreciation	(3,021,018)	(5,648,768)	(843,955)	(9,513,741)	-
Total capital assets, net	4,487,475	16,823,884	2,020,773	23,332,132	-
Total assets	\$ 4,929,303	\$ 23,466,046	\$ 2,126,698	\$ 30,522,047	\$ 11,126
Liabilities					
Current liabilities:					
Current portion of bonds payable	\$ 33,850	\$ 213,730	\$ 7,896	\$ 255,476	\$ -
Current portion of notes payable	204,967	133,335	-	338,302	-
Vouchers (accounts) payable:					
Trade	4,180	35,916	17,899	57,995	9,248
Construction contracts, including retainage	-	3,439,290	-	3,439,290	-
Accrued liabilities	4,120	12,620	1,733	18,473	-
Due to other funds	225,509	27,925	273,065	526,499	10,017
Deferred revenue	-	4,400	1,475	5,875	-
Total current liabilities	472,626	3,867,216	302,068	4,641,910	19,265
Non-current liabilities:					
Compensated absences	23,704	34,876	835	59,415	-
Long-term portion of bonds payable	509,081	5,950,057	166,885	6,626,023	-
Long-term portion of notes payable	3,081,314	4,852,360	-	7,933,674	-
Payable to other governments	4,865	-	-	4,865	-
Total non-current liabilities	3,618,964	10,837,293	167,720	14,623,977	-
Total liabilities	4,091,590	14,704,509	469,788	19,265,887	19,265
Net Position					
Net investment in capital assets	682,738	6,825,583	1,863,460	9,371,781	-
Unrestricted	154,975	1,935,954	(206,550)	1,884,379	(8,139)
Total net position	837,713	8,761,537	1,656,910	11,256,160	(8,139)
Total liabilities and net position	\$ 4,929,303	\$ 23,466,046	\$ 2,126,698	\$ 30,522,047	\$ 11,126

See notes to financial statements

City of Lock Haven, Pennsylvania

Statement of Revenues, Expenses and Changes in Fund Net Position
 Proprietary Funds
 Year Ended December 31, 2012

	Enterprise Funds				Internal Service Funds
	Water	Sewer	Airport Operating	Total	
Revenues					
Charges for services	\$ 1,620,854	\$ 2,531,146	\$ 351,646	\$ 4,503,646	\$ 143,573
Operating Expenses					
Personnel services	378,902	850,556	107,133	1,336,591	-
Utilities (including water filtration costs)	1,043,945	162,336	28,884	1,235,165	-
Depreciation	277,327	273,026	142,686	693,039	-
Materials, supplies and maintenance	11,845	123,159	187,078	322,082	147,708
Administrative expense	28,618	113,200	1,864	143,682	-
Sludge disposal	-	94,649	-	94,649	-
Insurance	6,393	26,578	9,589	42,560	-
Miscellaneous	(1,384)	9,720	3,940	12,276	-
Total operating expenses	1,745,646	1,653,224	481,174	3,880,044	147,708
Operating (loss) income	(124,792)	877,922	(129,528)	623,602	(4,135)
Non-Operating Revenues (Expenses)					
Subsidies from other governments:					
State	-	6,750,214	786,374	7,536,588	-
Local	224,983	-	-	224,983	-
Interest income	5,689	7,527	-	13,216	-
Rental income	9,788	53,467	-	63,255	-
Proceeds from sale of assets	10,599	1,060	525	12,184	-
Interest expense	(57,539)	(76,397)	(7,191)	(141,127)	-
Total non-operating revenues, net	193,520	6,735,871	779,708	7,709,099	-
Income (Loss) Before Other Financing Sources	68,728	7,613,793	650,180	8,332,701	(4,135)
Other Financing Sources					
Transfers in	-	-	6,410	6,410	-
Net Income	68,728	7,613,793	656,590	8,339,111	(4,135)
Net Position, Beginning	768,985	1,147,744	1,000,320	2,917,049	(4,004)
Net Position, Ending	\$ 837,713	\$ 8,761,537	\$ 1,656,910	\$ 11,256,160	\$ (8,139)

See notes to financial statements

City of Lock Haven, Pennsylvania

Statement Of Cash Flows
 Proprietary Funds
 Year Ended December 31, 2012

	Business-Type Activities			Totals	Governmental
	Water Fund	Sewer Fund	Airport Fund		Activities Internal Service Inventory Fund
Cash Flows From Operating Activities					
Cash received from users	\$ 1,529,263	\$ 2,497,132	\$ 388,607	\$ 4,415,002	\$ 149,996
Cash payments to employees for services	(378,630)	(847,383)	(116,151)	(1,342,164)	-
Cash paid to suppliers for goods and services	(1,087,055)	(633,194)	(219,502)	(1,939,751)	(149,996)
Net cash (used in) provided by operating activities	63,578	1,016,555	52,954	1,133,087	-
Cash Flows From Non-Capital Financing Activities					
Operating subsidies and transfers from (to) other funds	-	-	6,410	6,410	-
Cash Flows Provided by Investing Activities:					
Rental income	9,788	53,467	-	63,255	-
Earnings on investments	5,689	7,527	-	13,216	-
Net cash provided by investing activities	15,477	60,994	-	76,471	-
Cash Flows From Capital and Related Financing Activities					
Payments for capital acquisitions	(97,668)	(7,610,329)	(835,124)	(8,543,121)	-
Capital subsidies from other governments	224,983	3,532,663	786,374	4,544,020	-
Principal payments on long-term debt	(159,430)	(325,158)	(3,948)	(488,536)	-
Proceeds from long term debt	-	5,580,741	-	5,580,741	-
Interest paid	(57,539)	(169,648)	(7,191)	(234,378)	-
Proceeds from sale of assets	10,599	1,061	525	12,185	-
Net cash provided by capital and related financing activities	(79,055)	1,009,330	(59,364)	870,911	-
Increase (Decrease) in Cash and Cash Equivalents	-	2,086,879	-	2,086,879	-
Cash and Cash Equivalents, Beginning	-	708,218	-	708,218	-
Cash and Cash Equivalents, Ending	\$ -	\$ 2,795,097	\$ -	\$ 2,795,097	\$ -
Displayed as:					
Cash and cash equivalents	\$ -	\$ 1,822,919	\$ -	\$ 1,822,919	\$ -
Restricted cash	-	972,178	-	972,178	-
Total	\$ -	\$ 2,795,097	\$ -	\$ 2,795,097	\$ -
Reconciliation of Operating Income (Loss) to Net Cash Provided by (Used In) Operating Activities:					
Operating income (loss)	\$ (124,792)	\$ 877,922	\$(129,528)	\$ 623,602	\$ (4,135)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:					
Depreciation	277,327	273,026	142,686	693,039	-
Changes in assets and liabilities:					
Accounts receivable, other	(16,343)	13,078	4,618	1,353	(1,191)
Due from/to other governments and funds	(75,248)	(46,692)	36,497	(85,443)	7,614
Other current assets	(590)	-	-	(590)	-
Deferred charges	2,924	(88,892)	2,145	(83,823)	-
Vouchers payable	(562)	(14,660)	9,708	(5,514)	(2,288)
Deferred revenue	-	(400)	(4,154)	(4,554)	-
Accrued and other liabilities	862	3,173	(9,018)	(4,983)	-
Net Cash Provided by (Used In) Operating Activities	\$ 63,578	\$ 1,016,555	\$ 52,954	\$ 1,133,087	\$ -

See notes to financial statements

City of Lock Haven, Pennsylvania

Statement of Fiduciary Net Position

December 31, 2012

	<u>Pension and OPEB Trust Funds</u>
Assets	
Cash and cash equivalents	\$ 220,067
Contributions receivable	<u>7,052</u>
Total	<u>227,119</u>
Investments:	
Fixed income securities	3,123,693
Equity securities	5,429,013
Mutual funds	<u>923,751</u>
Total investments	<u>9,476,457</u>
Total assets	<u><u>\$ 9,703,576</u></u>
Net Position	
Held in trust for benefits and other purposes	<u><u>\$ 9,703,576</u></u>

See notes to financial statements

City of Lock Haven, Pennsylvania

Statement of Changes in Fiduciary Net Position
Year Ended December 31, 2012

	<u>Pension and OPEB Trust Funds</u>
Additions	
Contributions:	
Employees	\$ 91,903
Commonwealth of Pennsylvania	<u>247,578</u>
Total contributions	<u>339,481</u>
Investment earnings:	
Net increase in fair value of investments	710,127
Interest and dividends	<u>208,648</u>
Total investment earnings	<u>918,775</u>
Total additions	<u>1,258,256</u>
Deductions	
Benefits	473,058
Other	<u>38,742</u>
Total deductions	<u>511,800</u>
Change In Net Position	746,456
Net Position, Beginning	<u>8,957,120</u>
Net Position, Ending	<u><u>\$ 9,703,576</u></u>

See notes to financial statements

1. Summary of Significant Accounting Policies

The accounting methods and procedures adopted by the City of Lock Haven, Pennsylvania (the "City") conform to accounting principles generally accepted in the United States of America as applied to state and local governmental entities. The following notes to the basic financial statements are an integral part of the City's financial statements.

Reporting Entity

Incorporated as a City of the Third Class in 1870, the City of Lock Haven is the county seat of Clinton County and is located in north central Pennsylvania. The City lies between the banks of the West Branch of the Susquehanna River and the Bald Eagle Creek. The City is the largest municipality in Clinton County, encompassing 2.3 square miles with a population of approximately 9,000 people.

The City operates under a Council-Manager form of government. City Council consists of six council members and a mayor, each serving a four-year term.

The financial reporting entity includes all of the services provided by the City to residents and businesses within its boundaries. Municipal services provided include public safety (police, fire, emergency management and protective inspection), community development, street construction and maintenance, recreation, public works, library and general administration. In evaluating the City as a primary government in accordance with GASB Statement Nos. 14 and 39, management has addressed all potential component units. Consistent with applicable guidance, the criteria used by the City to evaluate the possible inclusion of related entities within its reporting entity are financial accountability and the nature and significance of the relationship. In determining financial accountability in a given situation, the City reviews the applicability of the following criteria:

The City is financially accountable for:

- 1.) Organizations that make up the legal municipal entity;
- 2.) Legally separate organizations if the City Council appoints a voting majority of the organizations' governing bodies and the City is able to impose its will on the organization or if there is a potential for the organization to provide specific financial benefits to, or impose specific financial burden on, the City.
 - a.) **Imposition of Will** – Exists if the City can significantly influence the programs, projects, or activities of, or the level of services performed or provided by the organization.
 - b.) **Financial Benefit or Burden** – Exists if the City (1) is entitled to the organization's resources or (2) is legally obligated or has otherwise assumed the obligation to finance the deficits of, or provide support to, the organization or (3) is obligated in some manner for the debt of the organization.
- 3.) Organizations that are fiscally dependent on the City. Fiscal dependency is established if the organization is unable to adopt its budget, levy taxes or set rates or charges, or issue bonded debt without approval by the City.

City of Lock Haven, Pennsylvania

Notes to Financial Statements

December 31, 2012

The financial statements of the City include the accounts of the City's primary government and two component units over which the City exercises significant influence. Significant influence or accountability is based primarily on operational or financial relationships with the City (as distinct from legal relationships). City Council appoints a voting majority to the Board of Directors of both component units. The Lock Haven City Authority issues separately audited financial statements, which can be obtained from the City Authority Office at 20 East Church Street, Lock Haven, Pennsylvania, 17745. The Lock Haven Area Flood Protection Authority also issues separately audited financial statements, which can be obtained from the Authority Office at 20 East Church Street, Lock Haven, Pennsylvania, 17745.

Blended Component Unit	Brief Description of Activities and Relationship to the City
Lock Haven City Authority (the "City Authority") functions as a financing medium for capital activity of City water and sewer systems.	The City Authority's board members are appointed by City Council. A continuing financial relationship exists between these parties in that the City is leasing the water and sewer systems from the City Authority.
Discretely Presented Component Unit	Brief Description of Activities and Relationship to the City
The Lock Haven Area Flood Protection Authority (the "Flood Protection Authority") was created for the purpose of implementing the Lock Haven Flood Protection Project and accomplishing the related duties of the "local sponsor."	The Flood Protection Authority's board, consisting of seven (7) members, is appointed by City Council (five appointments) and the Woodward Township Board of Supervisors (two appointments).

Government – Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net position and the statement of activities) report information on all of the nonfiduciary activities of the primary government and its component units. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported separately from certain legally separate discretely presented component units for which the primary government is financially accountable.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include: 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

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 and fiduciary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of 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.

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 City considers revenues to be available if they are collected within 60 days of the end of the current fiscal period.

Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures are recorded only when payment is due.

Property taxes, intergovernmental revenues, charges for services and interest associated with the current fiscal period are all generally considered to be susceptible to accrual and have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the government.

Generally, the effect of interfund activity has been eliminated from the government-wide financial statements.

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

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the enterprise funds are charges for utility services (water and sewer). Operating expenses for the enterprise funds include the cost of services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the City's policy to use restricted resources first, then unrestricted resources as they are needed.

Governmental Funds

General Fund

The General Fund is the general operating fund of the City. It is used to account for all financial resources except those required to be accounted for in another fund. All general tax revenues and other receipts that are not restricted by law or contractual agreement to some other fund are accounted for within this fund. General operating expenditures, fixed charges and capital improvement costs that are not paid by other funds are paid from the General Fund.

Special Revenue Funds

Special Revenue Funds are used to account for the proceeds of specific revenue sources (other than special assessments, expendable trusts, or major capital projects) that are legally restricted to specified purposes. Special Revenue Funds reported as nonmajor funds by the City include:

- The Rural Business Enterprise Grant Fund accounts for revenues used to provide support to various projects and programs benefiting local businesses.
- The Off Street Parking Fund accounts for revenues and expenditures related to operation, maintenance, fines and enforcement as related to off-street parking lots.
- The Recreation Fund accounts for the public contributions and event revenues used to provide recreational activities for City residents.
- The Interchange Fund accounts for revenues and expenditures for maintenance and electricity related to street lighting for the U.S. Route 220 Interchange.
- The Triangle Park and Hoberman Project Funds account for public contributions used for equipment purchases and improvements for those two parks.
- The Highway Aid Fund accounts for liquid fuel tax revenues used for building, improving and maintaining City streets.

City of Lock Haven, Pennsylvania

Notes to Financial Statements

December 31, 2012

- The Rehabilitation/Sidewalk Fund accounts for the operations of the City's Housing Rehabilitation Program, which is funded in part by federal funds whose use is restricted for the provision of specified home rehabilitation services to eligible City residents.
- The Federal Enterprise Program Fund accounts for revenues used to provide support to various projects and programs benefiting City residents.
- The CDBG Funds account for the operations of the City's Community Development Block Grant program, which are funded with federal funds passed through the Commonwealth of Pennsylvania and whose use is restricted for the provision of community services under four specific federal criteria.
- The Hoberman Park Fund accounts for certain recreational activities conducted at the Hoberman Park Playground.
- The Housing Home Program Fund accounts for federal HOME revenues used to provide assistance to low to moderate income homeowners for housing repairs to meet minimum building code requirements.
- The Owner Occupied Housing Fund accounts for housing assistance to low income families.
- The New Communities Main Street Fund accounts for certain City revitalization projects.

Capital Projects Fund

The Capital Projects Fund is used to account for financial resources to be used for the acquisition or construction of capital facilities or assets (other than those financed by proprietary funds).

Proprietary Funds

Enterprise Funds - Water, Sewer, and Airport Operating Funds

Enterprise funds are used to account for operations (a) that are financed primarily through user charges, or (b) where the governing body has decided that determination of net income is appropriate for capital maintenance, public policy, management control, accountability or other purposes. The City's major enterprise funds account for the operations of its Water, Sewer, and Airport operations.

Internal Service Fund - Inventory Fund

This fund is used to account for the financing of goods or services provided by one department to other departments of the City on a cost-reimbursement basis. The Inventory Fund comprises this fund type. The Inventory Fund is used to allocate the cost of fuel and postage among the various City departments and programs that use these items.

Fiduciary Funds

Pension and OPEB Trust Funds

Pension and OPEB trust funds are used to report the resources that are required to be held in trust for the members and beneficiaries of defined benefit pension or OPEB plans. The City maintains two, single-employer defined benefit pension trust funds, the Police Pension Fund and the City Employees Retirement Fund. In addition, the City maintains a single-employer defined benefit OPEB trust fund, the Police Death Benefit Fund.

New Accounting Principle

The City adopted Governmental Accounting Standards Board ("GASB") Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, for the year ended December 31, 2012. GASB No. 62 directly incorporates the applicable guidance from those FASB and AICPA pronouncements, issued prior to November 30, 1989, into the state and local government accounting and financial reporting standards. The City implemented the accounting and reporting requirement of GASB 62 as of January 1, 2012. This implementation did not materially change the City's accounting and reporting policies.

The City adopted GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position*, for the year ended December 31, 2012. GASB No. 63 standardized the presentation of deferred outflows of resources and deferred inflows of resources and their effect on net position. The City implemented the presentation requirements of GASB No. 63 as of January 1, 2012.

Cash Equivalents

The City considers highly liquid short-term instruments purchased with a maturity of three months or less (excluding certain short-term instruments which are classified as investments) to be cash equivalents.

Investments

Marketable securities are stated at their fair values. Other investments, including cash investment funds and certificates of deposit, are carried at cost, which approximates market. Adjustments to reflect increases or decreases in fair value, referred to as unrealized gains and losses, are reported as investment income.

Receivables and Payables

Interfund Receivables and Payables

Activities between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as "due to/from other funds." Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances." All receivables are shown net of an allowance for doubtful accounts, if applicable.

Trade and Property Tax Receivables

All receivables are reported at net realizable value. Amounts are written off when they are determined to be uncollectible based upon management's assessment of individual amounts. The allowance for doubtful accounts is estimated based upon a combination of the City's historical losses and a percentage of aged receivables. The allowance for uncollectible real estate and debt service taxes as of December 31, 2012 amounted to approximately \$101,027. The allowance for doubtful accounts related to the Water, Sewer, and Airport proprietary funds amounted to approximately \$23,032, \$24,419, and \$1,338, respectively, as of December 31, 2012.

Capital Assets

Purchased or constructed capital assets are reported at cost or estimated historical cost. Donated fixed assets are recorded at their estimated fair value at the date of donation. Capital assets with initial, individual costs that equal or exceed \$1,000 and estimated useful lives in excess of one year are recorded as capital assets. Major outlays for capital assets and improvements are capitalized as projects completed.

Beginning on January 1, 2004, the City began to prospectively capitalize its investment in infrastructure assets pursuant to GASB Statement No. 34. Infrastructure assets include long-lived, immovable capital assets such as road systems, bridges, curbs and gutters, sidewalks, drainage systems, and lighting systems. Prior to 2004, infrastructure was not capitalized.

Normal maintenance and repairs are charged to expense as incurred; major renewals or betterments which extend the life or increase the value of assets are capitalized.

Capital assets are depreciated using the straight-line method over the following estimated useful lives:

	<u>Governmental Activities</u>	<u>Business-Type Activities</u>	<u>Component Unit</u>
Buildings and improvements	40 years	40 years	-
Machinery and equipment	5-30 years	5-30 years	-
Vehicles	8 years	8 years	-
Infrastructure	10-65 years	-	100 years

Liabilities for Compensated Absences

Pursuant to various union contracts, City employees are awarded sick time each year based primarily upon the number of years served through December 31st of the preceding year. The City's policy generally provides that employees will be compensated for some portion of earned but unused sick time at retirement or termination.

Deferred Revenues

Deferred revenues consists of receivables not collected within 60 days subsequent to the City's year-end (fund-perspective financial statements), and loans receivable (principal and interest on these loans are recognized as program income as received) and grant proceeds for which the related expenditures had yet to be incurred. It is expected that these items will be included in revenues of future fiscal years.

At December 31, 2012, the General, Non-major Governmental, Sewer and Airport Operating Funds had deferred revenues of \$278,267, \$397,743, \$4,400, and \$1,475, respectively.

Governmental Fund Balance Classifications/Policies and Procedures

In accordance with GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, the City classifies its governmental fund balances as follows:

- *Non-spendable* – includes fund balance amounts that cannot be spent either because it is not in spendable form or because of legal or contractual constraints
- *Restricted* – includes fund balance amounts that are constrained for specific purposes which are externally imposed by providers, such as creditors or amounts constrained due to constitutional provisions or enabling legislation
- *Committed* – includes fund balance amounts that are constrained for specific purposes that are internally imposed by the City through formal action of the City's "highest level of decision-making authority" which do not lapse at year-end
 - City Council is its highest level of decision-making authority, and
 - City Council commits funds through a formal ordinance.
- *Assigned* – includes fund balance amounts that are constrained for specific purposes that are internally imposed by the City, but not through formal action of City Council. The City Manager is authorized to make assignments.
- *Unassigned* – includes fund balance within the General Fund which has not been classified within the above mentioned categories and negative fund balances in other governmental funds.

In governmental funds when an expenditure is incurred that can be paid using either restricted or unrestricted resources, the City's policy is generally to first apply the expenditure toward restricted resources and then to unrestricted resources.

When an expenditure is incurred that can be paid using either committed, assigned, or unassigned amounts, the City's policy is generally to apply the expenditure to committed resources, then to assigned resources, and then to unassigned resources.

Pension Plans

The City provides separate defined benefit pension plans for general employees and police department personnel. It is the City's policy to fund its annual required contribution.

OPEB Plan

The City provides a \$4,000 death benefit for all police officers who retired from the police force after age 55 or who served at least 20 years. It is the City's policy to fund this benefit as officers are hired.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. Budgetary Procedures and Budgetary Accounting

The City utilizes the Executive Budget approach to budgetary control. This approach requires the City Manager, together with the Department Heads, to prepare and submit a governing financial plan to the legislative body on an annual basis.

The City Manager is authorized to transfer the lesser of 5% or \$5,000 between departments within any fund. All other transfers or supplemental appropriations must be enacted by City Council. Actual expenditures and operating transfers out may not legally exceed "budget" appropriations at the individual fund level. Budgetary control, however, is maintained at the department level.

The City prepares its budgets for each fund type on the cash basis of accounting. Adjustments between the cash basis of accounting and the modified accrual basis of accounting consist of short-term cash receivable that occur shortly after year-end for which the services were rendered or the obligating event occurred prior to year-end.

Accounting principles generally accepted in the United States of America require that the City include a combined statement of revenues, expenditures and changes in fund balances - budgeted and actual - for the General Fund and for each major special revenue fund for which annual budgets have been legally adopted. A statement of revenues, expenditures and changes in fund balance - budgeted and actual - General Fund is presented on page 10 of the accompanying financial statements. During 2012, the City had no major special revenue funds that adopted an annual budget.

3. Cash, Cash Equivalents, and Investments

Under Section 1804.1 of the Third Class City Code of the Commonwealth of Pennsylvania, the City is authorized to invest in the following:

- A. United States Treasury bills.
- B. Short-term obligations of the United States government or its agencies or instrumentalities.
- C. Savings accounts or time deposits, other than certificates of deposit, or share accounts of institutions insured by the Federal Deposit Insurance Corporation ("FDIC").
- D. Obligations of the United States or any of its agencies or instrumentalities backed by the full faith and credit of the United States, the Commonwealth, or of any agencies or instrumentalities backed by the full faith and credit of the Commonwealth or of any political subdivision of the Commonwealth or any of its agencies or instrumentalities backed by the full faith and credit of the political subdivision. The City may also invest in shares of a registered investment company under the Investment Company Act of 1940, whose shares are registered under the Securities Act of 1933.
- E. Certificates of deposit purchased from institutions which are insured by federal agencies. For any amounts in excess of the insured maximum, such deposits shall be collateralized by a pledge or assignment of assets pursuant to Act No. 72 of the General Assembly.
- F. Pension or retirement funds may be invested by the City according to the "Prudent Man Rule" as defined by the Decedents, Estates, and Fiduciaries Act, 20 PAC.S.CH.73, which is referred to in the City Code.

GASB Statement No. 40, *Deposit and Investment Risk Disclosures*, requires disclosures related to the following deposit and investment risks; credit risk, custodial credit risk, concentration of credit risk, interest rate risk, and foreign currency risk. The following is a description of the City's deposit and investment risks.

Deposits

Custodial credit risk is the risk that in the event of a bank failure, the City will not recover its deposit or will not be able to recover collateral securities that are in the possession of an outside party. The City does not have a formal deposit policy for custodial credit risk. As of December 31, 2012, the aggregate bank balance of bank deposits was \$4,296,508, of which \$1,097,949 was covered by federal depository insurance and \$220,065 was covered by SIPC insurance. The uninsured remaining bank deposits of \$2,978,494 were covered by pledged pools of assets maintained in accordance with Act 72 of the General Assembly that requires the institution pool collateral for all governmental deposits. The carrying amount of these bank deposits was \$3,708,118 at December 31, 2012.

City of Lock Haven, Pennsylvania

Notes to Financial Statements
December 31, 2012

Investments - Pension Trust Funds

As of December 31, 2012, the City had the following investments:

Investment	Maturities	Fair Value
Equity securities	N/A	\$ 5,429,013
Mutual funds	N/A	923,751
Corporate bonds	Average of 8 years	901,944
Government bonds	Average of 4 years	796,245
U.S. Treasury securities	Average of 9 years	487,589
Government asset backed securities	Average of 20 years	398,764
Corp. mortgage/asset backed securities	Average of 23 years	271,009
Government mortgage pools	Average of 24 years	268,142
Total		<u>\$ 9,476,457</u>

Custodial Credit Risk

For an investment, 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 investments or collateral securities that are in the possession of an outside party. At December 31, 2012, all of the City's Pension and OPEB Trust Fund investments were held by Charles Schwab and were insured by SIPC up to \$500,000 per account.

Credit Risk

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a credit rating by a nationally recognized organization.

As of December 31, 2012, The City's credit quality distribution of securities as a percentage of total investments is as follows:

Corporate bonds	BBB to AAA	43.80	%
U.S. Treasury securities	AA+	23.68	%
Government mortgage pools	AA to AA+	19.36	%
Corp. mortgage/asset backed securities	A+ to AAA	13.16	%
Total fixed income		<u>100.00</u>	<u>%</u>

The City's investment policy limits investments as follows:

- At least 50% of its total assets are invested in securities issued by the U.S. Treasury and Government Agencies;
- Bonds must be rated as "investment grade" by Moody's and/or Standard & Poor's.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of the City's investment in a single issuer. As a means of limiting its exposure to fair-value losses arising from interest rates, the City's investment policy outlines an asset mix the investment manager must adhere to in order to achieve desired investment returns.

Interest Rate Risk

Interest rate risk is the risk that changes in market rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. As a means of limiting its exposure to fair-value losses arising from interest rates, the City's investment policy outlines an asset mix the investment manager must adhere to in order to achieve desired investment returns.

Foreign Currency Risk

Foreign currency risk is the risk that changes in the foreign exchange rate will adversely affect the fair value of an investment. There are currently no investments in securities exchanged in foreign denominations. As a means of limiting its exposure to fair-value losses arising from foreign currency exchange rates, the City's investment policy outlines an asset mix the investment manager must adhere to in order to achieve desired investment returns.

Restricted Cash

The City's Sewer Fund reports the unspent bond proceeds for future capital activity as restricted cash. At December 31, 2012, the unspent bond proceeds amounted to \$972,178.

Component Unit – Flood Protection Authority

Cash

At December 31, 2012 the carrying amount and bank balance of the Flood Protection Authority's deposits were \$3,821, all of which was covered by federal depository insurance.

4. Property Taxes

The City is responsible for the collection of property taxes for the City. The City's property tax is levied on the taxable real property within the City each January 1 and is payable in one installment on the following terms: 2% discount March 1 through April 30; face amount May 1 through June 30; and 10% penalty after June 30 following the levy date. Taxes not paid or exonerated become delinquent on December 31. The City collects taxes up to December 31 of the same year (payments post-marked by December 31 but received shortly after year-end are considered as having been collected for accounting purposes). Subsequent to year-end, all unpaid property taxes are certified to the Clinton County Delinquent Tax Office for further collection and possible tax sales over an additional 36-month period.

City of Lock Haven, Pennsylvania

Notes to Financial Statements
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The assessed value at January 1, 2012, upon which the 2012 levy was based, was \$280,529,800 of taxable property, which approximates the estimated market value of taxable property. Current tax collections for the year ended December 31, 2012 were 90.80% of the tax levy.

The City is permitted by the Third Class City Code to levy taxes up to 25 mills (\$25 per \$1,000 of assessed valuation) for general governmental services. The City imposes a split rate tax on real estate, with the millage on land being different from that on improvements. The millage on land as levied is 20.08 mills and the millage on improvements as levied is 4.12 mills. Since this is a split rate the two amounts cannot be simply added to determine the total millage. An equivalent single tax rate can be calculated by dividing the total tax revenue by the total assessed value.

The City's equivalent single tax rates at December 31, 2012 were:

General Governmental Services	5.864 mills
Levee System Operations	0.325 mills
Debt Service	0.671 mills

The City has a tax margin of 18.811 mills (25.00 mills limit less 5.864 mills for general government, less 0.325 mills for levee maintenance = 18.811 mills).

5. Due From Other Governments

The amount reported in the City's various governmental and proprietary funds at December 31, 2012 as due from other governments is summarized below:

	<u>Federal</u>	<u>State</u>	<u>Local</u>	<u>Total</u>
General Fund	\$ -	\$ -	\$ 100,612	\$ 100,612
Other Nonmajor Governmental Funds	26,867	-	14,132	40,999
Water Fund	-	-	9,044	9,044
Sewer Fund	-	3,217,551	4,930	3,222,481
Airport Fund	12,603	-	582	13,185
Total	<u>\$ 39,470</u>	<u>\$ 3,217,551</u>	<u>\$ 129,300</u>	<u>\$ 3,386,321</u>

Amounts due from the federal government are primarily grants receivable related to the City's various federal grant programs. Amounts due from local governments are primarily reimbursements for intergovernmental services performed during 2012.

City of Lock Haven, Pennsylvania

Notes to Financial Statements
December 31, 2012

6. Capital Assets

The City's capital asset activity as of and for the year ended December 31, 2012 is as follows:

	Balance January 1, 2012	Acquisitions	Disposals	Transfers	Balance December 31, 2012
Governmental activities:					
Capital assets, not being depreciated,					
Land	\$ 3,411,307	\$ -	\$ -	\$ -	\$ 3,411,307
Construction in progress	923,498	270,700	-	(1,194,198)	-
Total capital assets, not being depreciated	<u>4,334,805</u>	<u>270,700</u>	<u>-</u>	<u>(1,194,198)</u>	<u>3,411,307</u>
Capital assets, being depreciated:					
Land improvements	1,609,806	-	-	-	1,609,806
Buildings and improvements	3,925,614	-	-	-	3,925,614
Furniture and equipment	2,249,514	32,752	-	-	2,282,266
Transportation	766,480	45,924	-	-	812,404
Infrastructure	2,607,234	10,115	-	1,194,198	3,811,547
Total capital assets, being depreciated	<u>11,158,648</u>	<u>88,791</u>	<u>-</u>	<u>1,194,198</u>	<u>12,441,637</u>
Less accumulated depreciation:					
Land improvements	(1,212,465)	(62,660)	-	-	(1,275,125)
Buildings and improvements	(2,133,145)	(110,463)	-	-	(2,243,608)
Furniture and equipment	(1,469,391)	(103,722)	-	-	(1,573,113)
Transportation	(611,423)	(33,071)	-	-	(644,494)
Infrastructure	(560,001)	(191,819)	-	-	(751,820)
Total accumulated depreciation	<u>(5,986,425)</u>	<u>(501,735)</u>	<u>-</u>	<u>-</u>	<u>(6,488,160)</u>
Total capital assets, being depreciated	<u>5,172,223</u>	<u>(412,944)</u>	<u>-</u>	<u>1,194,198</u>	<u>5,953,477</u>
Governmental activities, net	<u>\$ 9,507,028</u>	<u>\$ (142,244)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 9,364,784</u>

City of Lock Haven, Pennsylvania

Notes to Financial Statements

December 31, 2012

	Balance January 1, 2012	Acquisitions	Disposals	Transfers	Balance December 31, 2012
Business-type activities:					
Capital assets, not being depreciated					
Land	\$ 669,000	\$ -	\$ -	\$ -	\$ 669,000
Construction in process	2,091,144	11,142,023	-	-	13,233,167
Total capital assets not being depreciated	2,760,144	11,142,023	-	-	13,902,167
Capital assets, being depreciated:					
Utility system	16,151,234	98,514	-	-	16,249,748
Land improvements	1,236,975	715,888	-	-	1,952,863
Equipment and vehicles	621,859	119,236	-	-	741,095
Total capital assets, being depreciated	18,010,068	933,638	-	-	18,943,706
Less accumulated depreciation:					
Utility system	(8,119,433)	(543,384)	-	-	(8,662,817)
Land improvements	(355,373)	(97,643)	-	-	(453,016)
Equipment and vehicles	(345,896)	(52,012)	-	-	(397,908)
Total accumulated depreciation	(8,820,702)	(693,039)	-	-	(9,513,741)
Business-type activities capital assets, net	<u>\$ 11,949,510</u>	<u>\$ 11,382,622</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 23,332,132</u>
	Balance January 1, 2012	Additions	Disposals		Balance December 31, 2012
Component – Unit Flood Protection Authority:					
Land improvements	\$ 84,590,355	\$ -	\$ -	\$ -	\$ 84,590,355
Accumulated depreciation	(10,996,741)	(845,903)	-	-	(11,842,644)
Component unit capital asset, net	<u>\$ 73,593,614</u>	<u>\$ (845,903)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 72,747,711</u>

City of Lock Haven, Pennsylvania

Notes to Financial Statements

December 31, 2012

Governmental activity depreciation expense, which amounted to \$501,735 for the year ended December 31, 2012 was not allocated to functional expense categories in the accompanying financial statements. Business-type activities depreciation expense, which amounted to \$277,327, \$273,026, and \$142,686 for the year ended December 31, 2012 was charged to the Water, Sewer, and Airport Funds in the accompanying financial statements, respectively.

7. Interfund Balances and Activity

Balances Due To/From Other Funds

Balances due to/from other funds are primarily the result of inter-fund borrowings necessitated by cash flow needs, or, in certain situations, a particular City program may involve a number of operating funds, wherein a periodic "settling up" has yet to take place and is reflected by a due to/from other funds.

Individual fund receivable and payable amounts at December 31, 2012 were as follows:

	<u>Interfund Receivable</u>	<u>Interfund Payable</u>
General Fund	\$ 110,542	\$ 191,623
Capital Projects Fund	81,952	-
Non-major Funds	338,412	829
Enterprise Funds	198,062	526,499
Internal Service Fund	-	10,017
	<u>\$ 728,968</u>	<u>\$ 728,968</u>

Transfers To/From Other Funds

Interfund transfers for the year ended December 31, 2012 were as follows:

	<u>In</u>	<u>Out</u>
General Fund	\$ 40,000	\$ 81,411
Capital Projects Fund	46,572	40,000
Non-major Funds	28,429	-
Enterprise Funds	6,410	-
	<u>\$ 121,411</u>	<u>\$ 121,411</u>

City of Lock Haven, Pennsylvania

Notes to Financial Statements
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During the year ended December 31, 2012, the City made a transfer from its General Fund for the purposes of funding an annual allocation to its Interchange Fund \$(2,500). In addition, the General Fund made transfers to its off-street parking fund (a nonmajor governmental fund) (\$23,289) to fund parking meter replacements during the year, its rehab/sidewalk fund (a nonmajor governmental fund) (\$2,640) to fund loans for rehabilitation of city sidewalks, its capital projects fund (a major fund) (\$46,572) to fund certain capital asset projects and its Airport Fund (a major proprietary fund) (\$6,410) to fund asset additions. The Capital Projects Fund transfer represents an annually budgeted transfer of \$40,000 from the Capital Projects Fund to the General Fund (pursuant to an agreement between the City and International Paper).

8. Long-Term Debt

As of December 31, 2012, the City's long-term debt consisted of the following:

Description	Interest Rate	Amount of Original Issue	Balance at 1/1/12	Additions	Retirements	Balance at 12/31/12	Current Portion
PennVEST Note Payable - Sewer Fund	1.156 %	\$ 2,638,730	\$ 1,623,312	\$ 85,043	\$ 124,243	\$ 1,584,113	\$ 130,721
DCED Note Payable - Sewer Fund	2.00 %	25,000	7,764	-	5,150	2,614	2,614
PennVEST Note Payable - Water Fund	1.00 %	6,122,000	3,428,880	-	142,598	3,286,281	204,967
2009 General Obligation Bond, Series A	2.00 - 3.50 %	3,715,000	2,965,000	-	400,000	2,565,000	450,186
2010 General Obligation Note	2.39 - 5.00 %	1,200,000	809,429	1,996	673,000	138,426	138,426
2011 General Obligation Bond - Sewer Fund	1.97 %	8,600,000	3,219,617	2,096,730	-	5,316,346	-
PennVEST Note Payable - Sewer Fund	1.00 %	18,074,732	-	3,398,968	-	3,398,968	-
Total, net			<u>\$ 12,054,002</u>	<u>\$ 5,582,737</u>	<u>\$ 1,344,991</u>	<u>\$ 16,291,748</u>	<u>\$ 926,914</u>

City of Lock Haven, Pennsylvania

Notes to Financial Statements
December 31, 2012

Amounts are reported in the accompanying financial statements as follows:

	<u>Current Portion</u>	<u>Long-Term Portion</u>	<u>Total</u>
Governmental Activities Bonds & Notes Payable	\$ 333,136	\$ 805,137	\$ 1,138,273
Business-Type Activities Bonds & Notes Payable	593,778	14,559,697	15,153,475
Total	<u>\$ 926,914</u>	<u>\$ 15,364,834</u>	<u>\$ 16,291,748</u>

PennVEST - Note Payable - Sewer Fund

In 2004, the City entered into a loan agreement with the Pennsylvania Infrastructure Investment Authority ("PennVEST") with an original balance of \$2,638,730, due in monthly installments of \$12,275 including principal and interest at 1.156% per annum through maturity during November 2024. The proceeds of the note were used to finance a portion of the cost of renovations to the sewage treatment facility. The note is secured by the City's pledge of all gross receipts and revenues of the system and a lien position thereto. Beginning in March 2012, the City's monthly payment installment changed to \$11,864, including principal and interest based on final amortization.

General Obligation Note – DCED – Sewer Fund

In April 2006, the City entered into a \$25,000 note payable arrangement with the Commonwealth of Pennsylvania, Department of Community and Economic Development ("DCED"), bearing interest at 2%, payable quarterly, maturing in May 2013. The City received the proceeds from this note in April 2008; the proceeds were used toward the purchase of a Flusher Truck.

PennVEST - Note Payable - Water Fund

In 2008, the City entered into a loan agreement with the Pennsylvania Infrastructure Investment Authority ("PennVEST") with a maximum balance of \$6,122,000 (only \$4,140,427 was drawn as of 12/31/12), due in monthly installments of \$19,691, including principal and interest at 1% per annum through maturity in July 2027. The proceeds drawn on the note to date were used to finance the City's Ohl Dam Grouting Project. The note is secured by the City's pledge of all gross receipts and revenues of the water system and a lien position thereto. Beginning in May 2012, the City's monthly payment installment changed to \$12,171, including principal and interest based on final amortization.

General Obligation Bond, Series A of 2009

In 2009, the City issued a \$3,715,000 General Obligation Bond, Series A of 2009, bearing interest at rates ranging from 1.00% to 3.50% per annum, maturing on dates ranging from November 1, 2013 to November 1, 2019. The proceeds from the bonds were used to (1) currently refund the City's General Obligation Bonds, Series of 2002, General Obligation Note, Series B of 2007 and a portion of the General Obligation Note, Series A of 2007; (2) to finance various capital projects of the City; and (3) to pay the costs of issuing the bonds. Of the \$3,715,000, \$1,475,632 was allocated to governmental activities and \$2,239,368 was allocated to proprietary funds. At December 31, 2012, the City had \$999,848 and \$1,565,152 outstanding within its governmental activities and proprietary funds, respectively.

General Obligation Note, Series of 2010

In 2011, the City issued a \$1,200,000 General Obligation Note, Series of 2010, bearing interest at 67% of 1 month LIBOR plus 2.39% (not to exceed 5%), maturing June 1, 2013 (only \$811,426 was drawn as of 12/31/12). For 2012, the interest rate equated to approximately 2.39%. The proceeds from the issuance of the note were used to (1) finance the planning, development, design, purchase, acquisition and construction of a Pedestrian Mall Walkway; and (2) to pay the costs of issuing the notes.

General Obligation Bond, Series of 2011 - Sewer Fund

In 2011, the City issued, as interim financing, a \$8,600,000 General Obligation Bond, Series of 2011, bearing interest at 1.97% per annum, maturing December 15, 2014 (only \$5,316,346 was drawn as of 12/31/12). The proceeds from the issuance of the bond were used to (1) currently refund all of the City's General Obligation Note, Series A of 2010; (2) to finance the sewer system capital improvement project; and (3) to pay the costs of issuing the bond.

PennVEST - Note Payable - Sewer Fund

In 2012, the City entered into a loan agreement with the Pennsylvania Infrastructure Investment Authority ("PennVEST") with a maximum balance of \$18,074,732 (only \$3,398,968 was drawn as of 12/31/12), due in monthly installments of \$58,135, including principal and interest at 1% per annum through maturity in July 2044. (If the City does not draw any further funds on this loan, final maturity would be during 2022.) The proceeds drawn on the note to date were used to finance the City's sewer system capital improvement project. The note is secured by the City's pledge of all gross receipts and revenues of the sewer system and a lien position thereto.

Interest paid on these bonds and notes during the year ended December 31, 2012 amounted to \$229,593. Of the interest paid, \$93,251 was capitalized for the year ended December 31, 2012 within the City's Sewer Fund..

The following is a schedule, by year, of the future minimum principal and interest payments required under the bond and note payable obligations as of December 31, 2012:

<u>Years Ending December 31</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2013	\$ 926,914	\$ 224,085	\$ 1,150,999
2014	6,056,345	200,476	6,256,821
2015	1,198,010	120,386	1,318,396
2016	1,381,683	103,608	1,485,291
2017	1,332,834	83,499	1,416,333
2018-2022	4,048,156	161,836	4,209,992
2023-2027	1,347,806	26,563	1,374,369
Total	\$ 16,291,748	\$ 920,453	\$ 17,212,201

City of Lock Haven, Pennsylvania

Notes to Financial Statements
December 31, 2012

9. Compensated Absences

The changes in the City's compensated absences in 2012 are summarized as follows:

Governmental Activities	
Balance, January 1, 2012	\$ 154,928
Increase	26,670
Decrease	<u>(22,295)</u>
Balance, December 31, 2012	<u>\$ 159,303</u>
Business Type Activities	
Balance, January 1, 2012	\$ 70,689
Increase	4,052
Decrease	<u>(15,326)</u>
Balance, December 31, 2012	<u>\$ 59,415</u>

10. Water and Sewer Fund Leases

On January 1, 1995, the City of Lock Haven and the Lock Haven City Authority entered into operating lease agreements wherein the Authority agreed to lease its sewer and water systems to the City.

Under the terms of these agreements, the City is required to transfer to the Authority on an annual basis, amounts equal to five (5) percent of the respective operating costs of these systems for the purpose of establishing capital reserve accounts. These transfers are required until each respective capital reserve account reaches an amount sufficient to pay operating expenses for a six-month period, as estimated by the consulting engineer, plus the next succeeding semi-annual total amount of debt service on the respective system.

During the year ended December 31, 2012, the City transferred \$29,527 to the Authority pursuant to the water system lease. In doing so, the City substantially met the funding requirement of this agreement. No such transfer was made to the Authority pursuant to the sewer system lease, because the sewer capital reserve account had reached the required amount during 2002.

11. Employee Pension Funds

Plan Descriptions

The Lock Haven City Employees Retirement Pension Fund ("CERF"), and the Lock Haven Police Pension Fund ("Police"), (collectively, the "Plans") are single-employer defined benefit pension plans administered by the City. The CERF Plan was established effective February 1, 1966 and the Police Plan was established effective March 26, 1963. The City is the only participating employer in the plans. Stand-alone financial statements are not issued for the Plans, nor are the Plans included in the report of any public employee retirement system or other entity.

	Combining Statement of Fiduciary Net Position				
	Police Pension	City Employees Retirement Fund	Total Pension	OPEB Police Death Benefit *	Total Pension/OPEB
Assets:					
Cash and cash equivalents	\$ 101,838	\$ 116,972	\$ 218,810	\$ 1,257	\$ 220,067
Contributions receivable	694	6,358	7,052	-	7,052
Total	102,532	123,330	225,862	1,257	227,119
Investments:					
Fixed income securities	1,427,887	1,627,222	3,055,109	68,584	3,123,693
Equity securities	2,698,812	2,667,714	5,366,526	62,487	5,429,013
Mutual funds	447,402	462,164	909,566	14,185	923,751
Total investments	4,574,101	4,757,100	9,331,201	145,256	9,476,457
Total	\$ 4,676,633	\$ 4,880,430	\$ 9,557,063	\$ 146,513	\$ 9,703,576
Net position, Held in trust for benefits	\$ 4,676,633	\$ 4,880,430	\$ 9,557,063	\$ 146,513	\$ 9,703,576

City of Lock Haven, Pennsylvania

Notes to Financial Statements
December 31, 2012

Combining Statement of Changes in Fiduciary Net Position

	Police Pension	City Employees Retirement Fund	Total Pension	OPEB Police Death Benefit *	Total Pension/OPEB
Additions:					
Contributions:					
Commonwealth of Pennsylvania	\$ 156,821	\$ 90,757	\$ 247,578	\$ -	\$ 247,578
Employees	10,171	81,732	91,903	-	91,903
Total contributions	166,992	172,489	339,481	-	339,481
Investment earnings:					
Net increase in fair value of investments	359,810	341,767	701,577	8,550	710,127
Interest and dividends	99,528	102,750	202,278	6,370	208,648
Total investment earnings	459,338	444,517	903,855	14,920	918,775
Total additions	626,330	617,006	1,243,336	14,920	1,258,256
Deductions:					
Benefits	294,940	178,118	473,058	-	473,058
Other	18,763	19,399	38,162	580	38,742
Total deductions	313,703	197,517	511,220	580	511,800
Change in net position	312,627	419,489	732,116	14,340	746,456
Net position, beginning	4,364,006	4,460,941	8,824,947	132,173	8,957,120
Net position, beginning	<u>\$ 4,676,633</u>	<u>\$ 4,880,430</u>	<u>\$ 9,557,063</u>	<u>\$ 146,513</u>	<u>\$ 9,703,576</u>

* - See Note 12

City of Lock Haven, Pennsylvania

Notes to Financial Statements

December 31, 2012

Additional information related to each of the pension plans, as of January 1, 2011 (the date of the most recent actuarial valuation), is as follows:

	CERF	Police
Employee groups covered	All non-uniformed employees, also, elected officials and City police officers hired prior to 1/1/1978	All City police officers
Legislative body governing plan and responsible for management of plan assets	Council of the City of Lock Haven	Council of the City of Lock Haven
Normal retirement age	65	50
Years of service requirement prior to retirement	10	20 (Vested at 12 years)
Monthly retirement benefits	Will receive monthly benefit based on the following: (1) Elected officials received \$7 times years of service as an elected official; (2) City employees receive 1.8% of average monthly earnings in the highest 5 consecutive of the last 10 years of services times years of service; and(3) Police officers hired prior to 1/1/1978, will receive monthly benefit equal to \$3 times years of service	Will receive annual benefit equal to 50% of the highest one years' W-2 earnings during the last 3 years of service preceding retirement
Monthly service increment benefit	None	Equal to one-fortieth of the pension benefit for each completed year of service in excess of twenty years, up to a maximum of \$100
Disability benefits: Eligibility	None	Service related injury or illness

City of Lock Haven, Pennsylvania

Notes to Financial Statements
December 31, 2012

	CERF	Police
Monthly disability benefits	None	2.5% of final monthly compensation times years of completed service, not to exceed 50%
Death benefits - Spouse: Before retirement	Refund of employee contributions without interest	Monthly benefit equal to years of service times 1.25%, up to a maximum of 25% times last salary prior to death, if death was duty related.
After retirement	In accordance with option selected	Monthly benefit equal to 50% of the pension participant was receiving on the day of participant's death is payable to legal spouse or minor children under age 18 if no eligible spouse of retired member.

Membership of the Pension Plans consisted of the following at January 1, 2011, the date of the latest actuarial valuation:

	CERF	Police
Retirees and beneficiaries receiving benefits	25	12
Terminated members entitled to but not yet receiving benefits	1	-
Active plan members	<u>45</u>	<u>11</u>
Total	<u>71</u>	<u>23</u>
Number of participating employers	<u>1</u>	<u>1</u>

City of Lock Haven, Pennsylvania

Notes to Financial Statements

December 31, 2012

Funding Policy

The contribution requirements of plan members are established and may be amended by the respective legislative bodies governing each of the plans (see Plan Descriptions). Employees are required to make the following contributions:

Employee Groups Covered	CERF	Police
Elected officials	\$8 per month	n/a
City employees	6% of pay	n/a
Police officers	\$3 per month	0.5% of compensation plus an additional \$12 per year for service increment

The contribution requirements of the City are determined in accordance with the Commonwealth of Pennsylvania's Municipal Pension Plan Funding and Recovery Act (Act 205 of 1984, [the "Act"]). The Act requires that annual contributions be based on a Minimum Municipal Obligation ("MMO"), as determined in connection with the Plans' biennial actuarial valuation. The MMO includes the normal cost, estimated administrative expenses and an amortization contribution of the unfunded actuarial accrued liability, less estimated member contributions and a credit equal to ten percent of the excess (if any) of the actuarial present value of assets over the actuarial accrued liability.

The Commonwealth of Pennsylvania provides an allocation of funds that must be used for pension funding. The City must fund any financial requirement established by the MMO that exceeds state/member contributions.

	CERF	Police
Annual required contribution	\$ 85,437	\$ 156,821
Interest on net pension asset	(25,591)	(8,537)
Adjustment to annual required contribution	-	-
Annual pension cost	59,846	148,284
Contributions made	90,757	156,821
Increase in net pension asset	30,912	8,537
Net pension asset, beginning of year	365,590	121,959
Net pension asset, end of year	\$ 396,502	\$ 130,496

City of Lock Haven, Pennsylvania

Notes to Financial Statements
December 31, 2012

The annual required contribution ("ARC") for the current year was determined as part of the January 1, 2011 actuarial valuation, which used the following assumptions:

Actuarial Assumptions	CERF	Police
Actuarial cost method	Entry age normal cost method	Entry age normal cost method
Amortization method	Level percentage of projected payroll, closed	Level percentage of projected payroll, closed
Investment rate of return	7.0%	7.0%
Projected salary increase	4.0%	5.0%
Inflation rate	3.0%	3.0%
Asset valuation method	4-Year Smoothing	4-Year Smoothing
Remaining amortization period	N/A	N/A

Trend Information

Plan and Year Ending	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation (Asset)
City Employees Retirement Pension Fund			
12/31/12	\$ 59,846	>100 %	\$ (396,502)
12/31/11	116,894	>100	(365,590)
12/31/10	(1,309)	>100	(335,105)
Police Pension Fund			
12/31/12	\$ 148,284	>100 %	\$ (130,496)
12/31/11	79,487	>100	(121,959)
12/31/10	45,615	>100	(109,960)

Funded Status and Funding Progress

The funded status of the plan as of January 1, 2011, the most recent actuarial valuation date, was as follows:

	Actuarial Value of Plan Assets (a)	Actuarial Accrued Liability (b)	Total Unfunded Actuarial Liability (Asset) (c)	Funded Ratio (a)/(b)	Annual Covered Payroll (c)	Ratio Of Unfunded Liability To Annual Covered Payroll ((b-a)/c)
Police Pension Fund	\$ 4,549,639	\$ 4,417,256	\$ (132,383)	103.0 %	\$ 647,361	N/A %
City Employees Retirement Pension Fund	4,476,383	4,500,489	24,106	99.5 %	1,544,320	1.6 %

The schedules of funding progress, presented as required supplementary information (RSI) following the notes to the financial statements, presents multiyear trend information about whether the actuarial values of plan assets are increasing or decreasing over time relative to the Actuarial Accrued Liability for benefits.

Summary of Significant Accounting Policies

Basis of Accounting

The Plans' financial statements are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which contributions are made. Employer contributions to each Plan are recognized when made. 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.

Contributions

Employee contributions are governed by the Plans' respective governing ordinances and collective bargaining. (See "Funding Policy" above).

Employer contributions are determined pursuant to the Commonwealth of Pennsylvania's Municipal Pension Funding and Recovery Act (Act 205 of 1984, [see "Funding Policy" above]).

Administrative costs, which may include but are not limited to investment management fees and actuarial services, are charged to the Plans and funded through the MMO and/or Plan earnings.

Concentrations

At December 31, 2012 the individual Plans held no investments (other than U.S. Government and U.S. Government guaranteed obligations) in any one organization that represents five percent or more of individual Plan net position.

12. Postemployment Benefits

Plan Description

The City provides and administers other postretirement benefits, consisting of health-care benefits for retired employees who are participants in the City's Police pension plan. Currently, 10 retirees meet those eligibility requirements. Such benefits are provided in accordance with the police union contract. The costs of such insurance coverage for retirees are primarily funded through annual appropriations from the City's General Fund. These benefits are accounted for in accordance with GASB Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions. Retired employees who are ineligible under the above requirements and choose to participate in the medical plan must pay 100% of the composite rate cost of such coverage. While no formal plan document currently exists, GASB No. 45 requires the valuation to consider the "substantive plan," meaning the plan terms as understood by the City and plan members, as described in various current and historical employment and union contracts, including any plan changes that have been made and communicated to employees. The plan is an unfunded single employer plan and no financial report is prepared. Stand-alone financial statements are not issued for the plan.

Funding Policy

The contribution requirements of plan members and the City are established and may be amended through negotiations between the City and the respective unions. The plan is funded on a pay-as-you-go basis, i.e., premiums are paid annually to fund the health care benefits provided to current retirees. Retirees are currently not required to contribute to the plan. The City paid premiums of approximately \$156,000 for the year ended December 31, 2012.

Annual OPEB Cost and Net OPEB Obligation

The City's annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution of the employer (ARC); an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years. The following show the components of the City's annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the City's net OPEB obligation:

Annual required contribution	\$ 817,930
Interest on net OPEB obligation	48,734
Adjustment to annual required contribution	<u>(105,364)</u>
Annual OPEB cost (expense)	761,300
Contributions made	<u>155,896</u>
Increase in net OPEB obligation	605,404
Net OPEB obligation at January 1, 2012	<u>1,218,342</u>
Net OPEB obligation at December 31, 2012	<u>\$ 1,823,746</u>

City of Lock Haven, Pennsylvania

Notes to Financial Statements
December 31, 2012

The net OPEB obligation is recorded as a benefit expense within the accompanying schedule of activities, within the Public Safety function.

The City's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for the years ended December 31, 2012, 2011 and 2010 were as follows:

Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
December 31, 2012	\$ 761,300	20.5 %	\$ 1,823,746
December 31, 2011	438,092	18.2 %	1,218,342
December 31, 2010	495,156	12.6 %	860,041

Funded Status and Funding Progress

The funded status of the plan as of December 31, 2012, the most recent actuarial valuation date, was as follows:

Actuarial accrued liability	\$ 6,564,915
Actuarial value of plan assets	<u>146,916</u>
Unfunded actuarial accrued liability (UAAL)	<u>\$ 6,417,999</u>
Funded ratio (actuarial value of plan assets/UAAL)	2.2%
Estimated annual covered payroll	730,000
UAAL as a percentage of covered payroll	879.2%

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the health care cost trend. Actuarial amounts determined regarding the funded status of the plan and the annual required contributions of the City are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

Actuarial Methods and Assumptions

The calculations are based on the types of benefits provided at the time of the valuation based upon the substantive plan (the plan as understood by the employer and the plan members). The projection of benefits for financial reporting purposes does not explicitly incorporate the potential effects of legal or contractual funding limitations in the future. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

City of Lock Haven, Pennsylvania

Notes to Financial Statements
December 31, 2012

In the December 31, 2012, actuarial valuation, the Entry Age Normal Method was used. Under the Entry Age Normal Cost Method, the Normal Cost is the present value of benefits allocated to the year following the valuation date. Benefits are allocated on a level basis over the earnings of an individual between the date of hire and the assumed retirement age. The Accrued Liability as of the valuation date is the excess of the present value of future benefits over the present value of future Normal Cost. The Unfunded Accrued Liability is the excess of the Accrued Liability over the Actuarial Value of Assets. Actuarial gains and losses serve to reduce or increase the Unfunded Accrued Liability.

The actuarial assumptions included a 4% investment rate of return, which is the expected rate to be earned on the City's deposits and investments, an annual healthcare cost trend rate of 9.0% for 2012, with the rate decreasing by decrements to an ultimate rate of 4.0% in 2084 and later, and a constant 5% increase per year for Medicare Part B and 4% increase in dental premiums. The UAAL is being amortized as a level dollar over a fifteen year open period. Twelve years remain at December 31, 2012.

13. Fund Balance Classification

The City presents its governmental fund balances by Level of constraint in the aggregate on its balance sheet – governmental funds. The individual specific purposes of each constraint are presented below:

	<u>General Fund</u>	<u>Capital Projects</u>	<u>Other Nonmajor Governmental Funds</u>	<u>Total</u>
Restricted for:				
Capital Projects	\$ -	\$ 574,790	\$ -	\$ 574,790
Street Programs	-	-	358,004	358,004
Recreation	-	-	49,530	49,530
Economic Development	-	-	132,451	132,451
Total	<u>\$ -</u>	<u>\$ 574,790</u>	<u>\$ 539,985</u>	<u>\$ 1,114,775</u>
Assigned for,				
Flood Protection	<u>\$ 65,283</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 65,283</u>

14. Jointly Governed Organization

The City is a participant in a jointly governed organization, the Central Clinton County Water Filtration Authority (the "Water Filtration Authority"). The Water Filtration Authority was formed by the City, which appoints five members to the Water Filtration Authority's board of directors, and the Borough of Flemington, the Borough of Mill Hall, and Woodward Township, each of which appoints two members to the Water Filtration Authority's board.

During the year ended December 31, 2012, the City purchased \$948,030 in water filtration services from the Water Filtration Authority.

15. Related Organizations

The Redevelopment Authority of the City of Lock Haven, PA (the "Redevelopment Authority") was established by the City pursuant to the provisions of the Pennsylvania Urban Redevelopment Law, Act of 1945. The City's accountability for the Redevelopment Authority does not extend beyond making appointments to the board and as such is not considered a component unit of the City.

16. Contingent Liabilities

Grant Programs

The City participates in federal and state assisted grant programs. These programs are subject to program compliance audits by the grantors or their representatives. The City is potentially liable for any expenditure which may be disallowed pursuant to the terms of these grant programs.

Environmental

The City maintains sewer and water treatment and fuel storage facilities. The City is potentially liable for any expenditure associated with compliance to mandated regulations and any assessments by regulatory authorities related to this facility or other similarly situated facilities.

Contingencies

In the normal course of business, the City may be subject to pending and threatened lawsuits in which claims for monetary damage could be asserted. In management's opinion, the City's financial position and results of operations would not be materially affected by the outcome of such legal proceedings.

18. Pending Changes in Accounting Principles

In December 2010, the GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus*. This statement addresses certain issues with distinguishing a government's control over another government in the reporting of component units. The City is required to adopt Statement No. 61 for its calendar year 2013 financial statements.

In March 2012, the GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. The City is required to adopt Statement No. 65 for its calendar year 2013 financial statements.

In March 2012, the GASB issued Statement No. 66, *Technical Corrections – 2012, an amendment of GASB Statements No. 10 and No. 62*. This statement addresses certain technical corrections to resolve conflicting guidance related to accounting for risk financing activities and the treatment of leases with scheduled rent increases. To the extent applicable, the City is required to adopt Statement No. 66 for its calendar year 2013 financial statements.

In June 2012, the GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27*. This statement is intended to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. This Statement replaces the requirements of *Statement No. 27, Accounting for Pensions by State and Local Governmental Employers*, as well as the requirements of Statement No. 50, *Pension Disclosures*, as they relate to pensions that are provided through pension plans administered as trusts or equivalent arrangements (hereafter jointly referred to as trusts) that meet certain criteria. The requirements of Statements 27 and 50 remain applicable for pensions that are not covered by the scope of this Statement. To the extent applicable, the City is required to adopt Statement No. 68 for its calendar year 2014 financial statements.

City management is in the process of analyzing these pending changes in accounting principles and the impact they will have on the financial reporting process.

19. Subsequent Events

In April 2013, the City approved an ordinance to issue debt through a local financial institution, in the principal amount of \$2,118,000, with a twenty year term, bearing interest at 2.46% for the first ten years and then at a variable rate of 4.25%, not to exceed 5.50% for ten years. This General Obligation Bond will be used for various capital projects, currently refunding the City's outstanding General Obligation Note, Series of 2010, payment of capitalized interest on the Bond and paying the costs of issuance.

City of Lock Haven, Pennsylvania

Required Supplementary Information
 Schedule of Funding Progress - Pension Trust Funds
 Year Ended December 31, 2012
 (Unaudited)

Actuarial Valuation Date	Actuarial Value of Plan Assets (a)	Actuarial Accrued Liability (b)	Total Unfunded Actuarial Liability (Asset)	Funded Ratio (a)/(b)	Annual Covered Payroll	Ratio of Unfunded Liability to Annual Covered Payroll
City Employees Retirement Fund						
January 1, 2011	\$ 4,476,383	\$ 4,500,489	\$ 24,106	99.5%	\$ 1,544,320	1.6%
January 1, 2009	3,790,120	3,800,602	10,482	99.7%	1,395,136	0.8%
January 1, 2007	4,011,159	3,404,242	(606,917)	117.8%	1,426,255	N/A
Police Pension Fund						
January 1, 2011	\$ 4,549,639	\$ 4,417,256	\$ (132,383)	103.0%	\$ 647,361	N/A
January 1, 2009	4,139,188	3,866,755	(272,433)	107.0%	631,043	N/A
January 1, 2007	4,595,664	3,565,871	(1,029,793)	128.9%	616,735	N/A

Note: As permitted by GASB No. 25, the City has elected to value these plans on a biennial basis.

City of Lock Haven, Pennsylvania

Required Supplementary Information

Schedule of Employer Contributions - Pension Trust Funds

Year Ended December 31, 2012

(Unaudited)

Year Ended December 31,	Police Pension Fund		City Employees Retirement Pension Fund	
	Annual Required Contribution	Percentage Contributed	Annual Required Contribution	Percentage Contributed
2012	\$ 156,821	100 %	\$ 85,437	106 %
2011	87,184	105 %	140,351	105 %
2010	50,572	168 %	12,320	1,129 %
2009	37,722	100 %	7,926	100 %
2008	40,011	103 %	10,313	103 %
2007	64,540	100 %	42,987	100 %
2006	56,187	100 %	37,529	100 %
2005	122,539	100 %	95,812	100 %
2004	110,428	102 %	88,807	102 %
2003	23,690	100 %	80,447 (1)	100 %

(1) - An additional \$9,704 was paid in 2005 for 2003 as a result of a state audit.

See note to required supplementary information

City of Lock Haven, Pennsylvania

Note to Required Supplementary Information – Pension Trust Funds

December 31, 2012

(Unaudited)

Actuarial Assumptions

The following actuarial assumptions were used in the January 1, 2011 actuarial valuation, the most recent actuarial valuation:

<u>Actuarial Assumption</u>	<u>City Employees Retirement Fund</u>	<u>Police Pension Fund</u>
Actuarial cost method	Entry age normal cost method	Entry age normal cost method
Amortization method	Level percentage of projected payroll, closed	Level percentage of projected payroll, closed
Investment rate of return	7.0%	7.0%
Projected salary increase	4.0%	5.0%
Consumer Price Index	3.0%	3.0%
Asset valuation method	4-Year Smoothing	4-Year Smoothing
Remaining amortization period	N/A	N/A

City of Lock Haven, Pennsylvania

Schedule of Expenditures of Federal Awards
Year Ended December 31, 2012

Federal Grantor/Pass-Through Grantor/Program Title	Pass-Through Entity Identification Number	Federal CFDA Number	Program Amount	Total Received for the Year	Accrued (Deferred) Revenue January 1, 2012	Revenue Recognized	Expenditures	Accrued (Deferred) Revenue December 31, 2012
U.S. Department of Housing and Urban Development, Passed through Pennsylvania Department of Community and Economic Development: CDBG - State - Administered Small Cities Program Cluster:								
Community Development Block Grant State's Program (2010 Allotment)	C000049876	14.228	\$ 370,457	\$ 223,781	\$ 2,500	\$ 227,894	\$ 227,894	\$ 6,613
Community Development Block Grant State's Program (2011 Allotment)	C000052228	14.228	316,864	71,799	-	71,799	71,799	-
Community Development Block Grant Revolving Loan Program Income	(N/A)	14.228	(N/A)	18,960	10,245	40,603	40,603	31,888
Total CDBG - State Administered Small Cities Program Cluster				314,540	12,745	340,296	340,296	38,501
HOME Program - Home Investment Partnerships Program	C000051595	14.239	500,000	122,408	872	128,096	128,096	6,550
Total U.S. Department of Housing and Urban Development				436,948	13,617	468,382	468,382	45,051
U.S. General Services Administration, Passed through Pennsylvania Department of General Services, Federal Surplus Program	(N/A)	39.003	(N/A)	23,914	-	23,914	23,914	-
U.S. Department of Transportation, Passed through Pennsylvania Department of Transportation:					(a)	-	-	-
Airport Action Plan - Update Airport Layout Plan	7880131084	20.106	249,635	-	-	-	-	-
Replace Airport Beacon	7880131091	20.106	77,349	-	-	-	-	-
Acquire Snow Removal Equipment	7880131100	20.106	115,168	115,168	2,367	112,801	112,801	476
Rehab RW 9/27, Phase I Design	7880131110	20.106	80,684	80,449	3,974	76,951	76,951	12,127
Rehab RW 9/27, Phase II Construction	7880131121	20.106	888,500	548,564	-	560,691	560,691	-
Total U.S. Department of Transportation				744,181	6,341	750,443	750,443	12,603

City of Lock Haven, Pennsylvania

Schedule of Expenditures of Federal Awards
Year Ended December 31, 2012

Federal Grantor/Pass-Through Grantor/Program Title	Pass Through Entity Identification Number	Federal CFDA Number	Program Amount	Total Received for the Year	Accrued (Deferred) Revenue January 1, 2012	Revenue Recognized	Expenditures	Accrued (Deferred) Revenue December 31, 2012
Environmental Protection Agency, Passed through the Pennsylvania Infrastructure Investment Authority, Capitalization Grants for Clean Water State Revolving Funds	ME #71259	66.458	2,190,146	85,043	-	85,043	85,043	-
U.S. Department of Justice, JAG Program Cluster								
ARRA/Byrne Justice Assistance Program - Police Hiring	2009-AJ-01-20862	16.803	100,000	52,817	13,689	52,832	52,832	13,704
ARRA/Byrne Justice Assistance Program - Law Enforcement Interoperability and Communication (pass thru to County)	2009-JG-0621472	16.738	398,200	386,034	-	386,034	386,034	-
Total U.S. Department of Justice, JAG Program Cluster				438,851	13,689	438,866	438,866	13,704
Total Federal Financial Assistance				\$ 1,728,937	\$ 33,647	\$ 1,766,648	\$ 1,766,648	\$ 71,358

(a) - Adjustments due to over accrued expenditures.

Notes:

This schedule includes the federal award activity of the City of Lock Haven, Pennsylvania, and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of the financial statements.

Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With Government Auditing Standards

Honorable Members of City Council
City of Lock Haven, Pennsylvania

We have audited, in accordance with the 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, the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Lock Haven, Pennsylvania (the "City"), as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated September 3, 2013. Our report includes a reference to other auditors who audited the financial statements of the Lock Haven Area Flood Protection Authority (the "Flood Protection Authority"), as described in our report on the City's financial statements. This report includes our consideration of the results of the other auditor's testing of internal control over financial reporting and compliance and other matters that are reported on separately by those other auditors. However, this report, insofar as it relates to the results of the other auditors, is based solely on the report of the other auditors. Our report also disclosed that the City has not presented a Management's Discussion and Analysis, which accounting principles generally accepted in the United States of America have determined is necessary to supplement, although not required to be part of, the basic financial statements.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we and the other auditors did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We and the other auditors did identify certain deficiencies in internal control, described in the accompanying schedule of findings and questioned costs as items 2012-01, 2012-02 and 2012-03, that we consider to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests and those of the other auditors disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

City's Response to Findings

The City's response to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. The City's response was not subjected to the auditing procedures applied on the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the City's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

ParenteBeard LLC

Williamsport, Pennsylvania
September 3, 2013

**Independent Auditors' Report on Compliance for
Each Major Federal Program and on Internal Control
Over Compliance in Accordance With
OMB Circular A-133**

Honorable Members of City Council
City of Lock Haven, Pennsylvania

Report on Compliance for Each Major Federal Program

We have audited the City of Lock Haven, Pennsylvania's (the "City") compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the City's major federal programs for the year ended December 31, 2012. The City's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the City's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the City's compliance.

Opinion on Each Major Federal Program

In our opinion, the City complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2012.

Internal Control over Compliance

Management of the City is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the City's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

ParenteBeard LLC

Williamsport, Pennsylvania
September 3, 2013

City of Lock Haven, Pennsylvania

Schedule of Findings and Questioned Costs
Year Ended December 31, 2012

Section I - Summary of Auditors' Results

Financial Statements

Type of auditors' report issued:

UNQUALIFIED

Internal control over financial reporting:

Material weakness(es) identified?

_____ yes X no

Significant deficiency(ies) identified?

 X yes _____ none reported

Noncompliance material to financial statements noted?

_____ yes X no

Federal Awards

Internal control over major programs:

Material weakness(es) identified?

_____ yes X no

Significant deficiency(ies) identified?

_____ yes X none reported

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

UNQUALIFIED

Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133?

_____ yes X no

Identification of major programs:

CFDA Number(s)

Name of Federal Program or Cluster

16.738

JAG Program Cluster:
Edward Byrne Memorial Justice Assistance Grant Program

16.803

Edward Byrne Memorial Justice Assistance Grant Program

20.106

Airport Improvement Program

Dollar threshold used to distinguish Between Type A and Type B programs:

\$300,000

Auditee qualified as low-risk auditee?

_____ yes X no

City of Lock Haven, Pennsylvania

Schedule of Findings and Questioned Costs
Year Ended December 31, 2012

Section II - Financial Statement Findings

Finding No.

Finding/Noncompliance

2012-01

**Internal Control Over Financial Reporting –
Segregation Of Duties Over Cash Receipts – Significant Deficiency**

Criteria: Adequate segregation of duties between accounting functions is essential to good internal control.

Condition/Context: The responsibility for the performance of accounting duties related to the cash receipts cycle is vested in a limited number of employees. In certain instances one individual has the ability to collect payments, post the payments to the general ledger, reconcile the payments to system generated reports, count and reconcile the cash drawer, and make the deposit at the bank.

Effect: Without proper segregation of accounting functions, errors or fraud could occur and go undetected.

Cause: The City employs a limited number of accounting personnel.

Recommendation: While it is advisable to have adequate segregation of duties among employees, the cost of such implementation must be weighed against the benefits to be derived. The cost which would result from increasing the number of employees to more fully segregate duties in your organization may exceed any internal control benefits to be derived. We feel that this internal control weakness is somewhat mitigated by the active involvement of the City Manager and City Council in the City's operational activities. You must, however, be aware of the possible impact of the internal control weaknesses which exist and continue to involve these individuals in financial accounting matters.

**Views of
Responsible
Officials and
Planned Corrective**

Actions: See corrective action plan.

City of Lock Haven, Pennsylvania

Schedule of Findings and Questioned Costs
Year Ended December 31, 2012

Finding No.

Finding/Noncompliance

2012-02

**Internal Control over Financial Reporting –
Non-attest Services – Significant Deficiency**

Criteria: In connection with our audit of your financial statements, you have also engaged us to perform certain non-attest services, subject to City review and approval, which included assistance with adjusting:

- Various receivable/payable accounts;
- Proprietary Fund capital assets;
- Conversion of financial statements from fund basis to government wide basis and from cash to accrual basis; and,
- Beginning fund balances for prior year activity.

Condition/Context: Internal control is a process which captures and records transactions, safeguards your assets and assures compliance with laws and regulations. As part of the audit, there were certain adjustments required, which might not have been made had the audit not been performed.

Effect: The fact that you have requested our technical assistance with the above-mentioned tasks, which are a normal and required component of internal control over financial reporting, constitutes a significant deficiency in internal control over financial reporting.

Cause: You have asked us to provide these accounting services because, like many smaller local governments, you have determined that your internal accounting personnel may not be sufficiently experienced to handle these areas, and you have determined it is cost beneficial for you to utilize our services to supplement your internal capabilities.

Recommendation: We recommend that management give consideration to performing the above tasks internally.

**Views of
Responsible
Officials and
Planned Corrective**

Actions: See corrective action plan.

City of Lock Haven, Pennsylvania

Schedule of Findings and Questioned Costs
Year Ended December 31, 2012

Finding No.

Finding/Noncompliance

2012-03

Internal Control Over Financial Reporting – City Pension Funds – Significant Deficiency

Criteria: The City provides separate defined benefit pension plans for general employees and police department personnel (the “Pension Funds”).

Condition/Context: The City does not maintain the activity relating to its cash and investment of Pension Funds within its general ledger system, nor is the activity within these funds reconciled on a monthly basis by an appropriate individual within the City. As such, existing internal control is limited with regard to these funds.

Effect: City management cannot be assured that its Pension Funds have been properly valued, credited for investment earnings, and that Pension Fund disbursements are limited to authorized benefit payments and administrative charges.

Cause: Lack of oversight.

Recommendation: City management should establish monthly reconciliation procedures whereby investment activity is tracked, recorded and reconciled by an appropriate individual.

Views of Responsible Officials and Planned Corrective

Actions: See corrective action plan.

Section III – Federal Award Findings and Questioned Costs

None.

Section IV – Summary Schedule of Prior Year Audit Findings

Prior year findings 2011-01, 2011-02 and 2011-03, which related to internal control over financial reporting, are repeated as current year findings 2012-01, 2012-02 and 2012-02, respectively.