

City of Bethlehem, Pennsylvania

Financial Statements and Supplementary Information

Year Ended December 31, 2011 with
Independent Auditor's Report

CITY OF BETHLEHEM, PENNSYLVANIA

YEAR ENDED DECEMBER 31, 2011

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YEAR ENDED DECEMBER 31, 2011

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Independent Auditor's Report

The Honorable John B. Callahan, Mayor, and
Honorable Members of City Council
City of Bethlehem, Pennsylvania

We have audited the accompanying 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 Bethlehem, Pennsylvania (City), as of and for the year ended December 31, 2011, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the Bethlehem Redevelopment Authority, which represent \$8,969,699, \$20,258,152, (\$11,268,453), \$14,478,663, and \$21,438,115, respectively, of the assets, liabilities, net assets, revenues, and expenses of the aggregate discretely presented component units. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Bethlehem Redevelopment Authority, is based on the report of other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The financial statements of the Bethlehem Area Public Library and the Bethlehem Parking Authority were not audited in accordance with *Government Auditing Standards*. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the report of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City as of December 31, 2011, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 29, 2012, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and the required supplementary information listed in the table of contents on pages i through xiv and 71 through 76 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's financial statements as a whole. The combining non-major fund financial statements are presented for purposes of additional analysis and are not a required part of the financial statements. The combining non-major fund financial statements are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Maher Duessel

Harrisburg, Pennsylvania
August 29, 2012

CITY OF BETHLEHEM, PENNSYLVANIA

Management's Discussion and Analysis (Unaudited)

This Management's Discussion and Analysis (MD&A) is intended to provide a narrative overview and analysis of the financial activities of the City of Bethlehem for the years ended December 31, 2011 and 2010. The City's financial performance is discussed and analyzed within the context of the financial statements and the disclosures that follow.

Financial Highlights

The City's total net assets increased by \$4,995,533 in 2011 and decreased by \$8,098,035 in 2010.

In the City's governmental activities, net assets increased by \$5,506,048 in 2011 and decreased by \$6,251,098 in 2010. In 2011, the increase in net assets is the result of increases in revenue from taxes of \$4,562,597 and intergovernmental revenues of \$6,910,436. In 2010, the decrease in net assets is the result of an increase of \$3,130,942 in general expenditures along with decreases in revenue from taxes of \$2,185,840 and departmental earnings of \$1,580,465.

In the City's business-type activities, net assets decreased by \$510,515 in 2011 and decreased by \$1,846,937 in 2010. In 2011, the decrease is the result of a decrease in charges for services of \$1,263,785. On the expenditure side, there was an increase in service charges of \$1,984,141 while interest expense and transfers out reflect decreases of \$1,611,113 and \$1,417,356, respectively. In 2010, the decrease is the result of increasing expenditures including a \$269,522 increase in salaries, wages, and fringe benefits, a \$368,292 increase in utilities, a \$271,048 increase in department contracts, and a \$234,381 increase in service charges.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

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

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

The *statement of activities* presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, *regardless of the timing of related cash flows*. Thus,

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Management's Discussion and Analysis (Unaudited)

revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

Both of the government-wide financial statements distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (*governmental activities*) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*). The governmental activities of the City include general government, parks, public works, community development, fire and police. The business-type activities of the City include the water, sewer and municipal golf operations.

The government-wide financial statements include not only the City itself, but also the legally separate Bethlehem Authority. Financial information for this blended *component unit* is reported as combined with the financial information presented for the primary government itself.

The City's other three component units, the legally separate Bethlehem Parking Authority (Parking Authority), the legally separate Bethlehem Public Library (Library), and the legally separate Bethlehem Redevelopment Authority (Redevelopment Authority), are shown in a separate column as discretely presented component units.

The government-wide financial statements can be found on pages 1-4 of this report.

Fund Financial Statements A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

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

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

The City maintains six individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues,

CITY OF BETHLEHEM, PENNSYLVANIA

Management's Discussion and Analysis (Unaudited)

expenditures, and changes in fund balances for the general fund and the non-utility capital improvement fund, which are considered to be major funds. Data from the other four governmental funds are combined into a single, aggregated presentation captioned "Other Non-Major Governmental Funds". Individual fund data for each of these non-major governmental funds is provided in the form of *combining statements* elsewhere in this report. The City adopts an annual appropriated budget for its general fund. A budgetary comparison statement has been provided for the general fund to demonstrate compliance with this budget.

The basic governmental fund financial statements can be found on pages 5-8 of this report.

Proprietary Funds The City maintains four proprietary funds. *Enterprise funds* are used to report the same functions presented as *business-type activities* in the government-wide financial statements. The City uses enterprise funds to account for its water, sewer, and municipal golf operations. *Internal service funds* are an accounting device used to accumulate and allocate costs internally among the City's various functions. The City uses an internal service fund to account for its medical insurance. Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The internal service fund is presented in the proprietary fund financial statements.

The basic proprietary fund financial statements can be found on pages 9-12 of this report.

Fiduciary Funds

The City's fiduciary fund accounts for the Employee Benefit Trust Fund and Agency Fund and can be found on pages 13-14.

Component Units

The City's component units include the Parking Authority, Library, and Redevelopment Authority. The component unit's financial statements can be found on pages 15-17.

General Fund Budgetary Highlights

The General Fund expenditure budget for fiscal year 2011 was approximately \$64.4 million. This was a decrease of \$6.6 million over the previous year amended budget. There were no material amendments to the 2011 budget. Actual expenditures were approximately \$6.9 million more than budgeted largely due to medical insurance. The City paid \$4.3 million in prior year medical claims with the 2011 Working Capital proceeds which were not budgeted. Also, approximately \$2 million in medical expenses, which were budgeted and paid for out of the Water and Sewer Funds, were presented as expenditures of the General Fund. In addition, the City paid the 2010 municipal minimum obligations for the pension plans in 2011, which were not budgeted for in 2011.

CITY OF BETHLEHEM, PENNSYLVANIA

Management's Discussion and Analysis (Unaudited)

Notes to the Financial Statements The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 18-70 of this report.

Other Information. Required supplementary information can be found on pages 71-76 of this report. The combining statements referred to earlier in connection with governmental fund types are presented immediately following the required supplementary information section. Combining schedules can be found on pages 77-78 of this report.

Government-Wide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the City, liabilities exceeded assets at the close of the end of December 31, 2011 by \$22,400,794 and \$27,396,327 in 2010.

The City's net assets reflects its investment in capital assets (e.g., land, buildings, and equipment), less any related debt used to acquire those assets that is still outstanding. The City uses these capital assets to provide services to citizens; consequently, these assets are *not* available for future spending.

City's Condensed Statement of Net Assets

	Governmental Activities		Business-type Activities		Totals	
	2011	2010	2011	2010	2011	2010
Current assets	\$ 21,349,803	\$ 21,192,267	\$ 5,719,125	\$ 7,910,291	\$ 27,068,928	\$ 29,102,558
Capital assets	57,907,240	55,456,928	98,409,604	100,545,275	156,316,844	156,002,203
Other assets	5,274,289	3,821,910	16,808,069	17,346,731	22,082,358	21,168,641
Total assets	\$ 84,531,332	\$ 80,471,105	\$ 120,936,798	\$ 125,802,297	\$ 205,468,130	\$ 206,273,402
Current liabilities	\$ 19,801,277	\$ 40,177,391	\$ 11,388,312	\$ 9,550,759	\$ 31,189,589	\$ 49,728,150
Noncurrent liabilities	92,392,106	73,461,813	104,287,229	110,479,766	196,679,335	183,941,579
Total liabilities	\$ 112,193,383	\$ 113,639,204	\$ 115,675,541	\$ 120,030,525	\$ 227,868,924	\$ 233,669,729
Net assets:						
Invested in capital assets, net of related debt	\$ 29,407,634	\$ 29,749,300	\$ 2,844,816	\$ 1,719,923	\$ 32,252,450	\$ 31,469,223
Restricted	548,734	423,573	-	-	548,734	423,573
Unrestricted	(57,618,419)	(63,340,972)	2,416,441	4,051,849	(55,201,978)	(59,289,123)
Total net assets (deficit)	\$ (27,662,051)	\$ (33,168,099)	\$ 5,261,257	\$ 5,771,772	\$ (22,400,794)	\$ (27,396,327)

Current liabilities in Governmental Activities decreased approximately \$20.4 million. This was due to workforce and budget cuts along with fee increases and a working capital transaction

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Management's Discussion and Analysis (Unaudited)

which decreased net pooled cash position by \$6.6 million, accounts payable by \$6.5 million, and claims payable by \$4.4 million.

Noncurrent liabilities in Governmental Activities increased approximately \$18.9 million. This was due to the issuance of debt in the amount of \$32.5 million, net of debt principal payments (including refunded debt) of \$16.4 million.

Noncurrent liabilities in Business-type Activities decreased approximately \$6.2 million. This was due to debt issued of \$1.9 million compared to debt principal payments of \$5.7 million in 2011.

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Management's Discussion and Analysis (Unaudited)

City's Condensed Statement of Activities

	Governmental Activities		Business-type Activities		Totals	
	2011	2010	2011	2010	2011	2010
Program revenues:						
Charges for services	\$ 11,949,526	\$ 10,531,890	\$ 30,783,387	\$ 32,047,172	\$ 42,732,913	\$ 42,579,062
Operating grants and contributions	9,878,606	9,598,763	-	-	9,878,606	9,598,763
Capital grants	4,326,673	589,097	1,712,549	313,380	6,039,222	902,477
General revenues:						
Taxes	32,475,537	27,912,940	-	-	32,475,537	27,912,940
Investment earnings	114,897	109,492	481,026	443,383	595,923	552,875
Unrestricted grants	15,446,948	12,553,931	-	-	15,446,948	12,553,931
Total revenues	74,192,187	61,296,113	32,976,962	32,803,935	107,169,149	94,100,048
Expenses:						
General government	722,426	745,701	-	-	722,426	745,701
Administrative	1,131,440	1,636,332	-	-	1,131,440	1,636,332
Community development	5,438,536	6,068,627	-	-	5,438,536	6,068,627
Parks and public property	4,317,501	4,270,200	-	-	4,317,501	4,270,200
Public works	8,035,675	7,956,564	-	-	8,035,675	7,956,564
Police	16,313,591	16,525,305	-	-	16,313,591	16,525,305
Fire	10,858,971	11,126,064	-	-	10,858,971	11,126,064
General expenditures	14,189,563	15,606,883	-	-	14,189,563	15,606,883
Civic	99,863	137,448	-	-	99,863	137,448
Library	1,173,073	925,683	-	-	1,173,073	925,683
Program expenditures	3,720,776	2,672,637	-	-	3,720,776	2,672,637
Interest on long-term debt	4,965,648	3,574,047	-	-	4,965,648	3,574,047
Water fund	-	-	19,347,748	20,095,066	19,347,748	20,095,066
Sewer fund	-	-	10,560,066	9,408,839	10,560,066	9,408,839
Other non-major fund	-	-	1,298,739	1,448,687	1,298,739	1,448,687
Total expenses	70,967,063	71,245,491	31,206,553	30,952,592	102,173,616	102,198,083
Change in net assets before transfers	3,225,124	(9,949,378)	1,770,409	1,851,343	4,995,533	(8,098,035)
Transfers	2,280,924	3,698,280	(2,280,924)	(3,698,280)	-	-
Change in net assets	5,506,048	(6,251,098)	(510,515)	(1,846,937)	4,995,533	(8,098,035)
Net assets:						
Beginning	(33,168,099)	(26,917,001)	5,771,772	7,618,709	(27,396,327)	(19,298,292)
Ending	\$ (27,662,051)	\$ (33,168,099)	\$ 5,261,257	\$ 5,771,772	\$ (22,400,794)	\$ (27,396,327)

Unrestricted grants in Governmental Activities increased approximately \$2.9 million. This was the result of an increase in the State Subsidy for Pension of \$2.1 million, which according to the State was a one-time increase for 2011.

CITY OF BETHLEHEM, PENNSYLVANIA

Management's Discussion and Analysis (Unaudited)

Taxes in Governmental Activities increased approximately \$4.6 million. This was due to an increase in earned income tax of \$3.9 million which was caused by a transfer of EIT collection to a third party per State law. The City then was able to pay out all remaining funds owed the City through internal collection. Current real estate taxes increased by \$1.3 million which was largely due to a millage increase of .75 mills.

Capital grants in Governmental Activities increased approximately \$3.7 million. This was the result of the following grants from the State: \$1.7 million for Broad St. & Pennsylvania Ave., \$670,000 for PennDOT funded infrastructure improvements, and \$602,000 for Phase II of the Greenway.

Capital grants in Business-type Activities increased approximately \$1.4 million. This was due to the increase of approximately \$1 million from two H2O Pennsylvania grants in the water fund.

Governmental activities. Governmental activities increased the City's net assets by \$5,506,048 for the year ended December 31, 2011. Key elements of this increase are as follows:

- The increase in net assets is the result of increases in revenue from taxes of \$4,562,597 and intergovernmental revenues of \$6,910,436.

Business-type activities. Business-type activities decreased the City's net assets by \$510,515 for the year ended December 31, 2011. Key elements of this change are as follows:

- The decrease is the result of a decrease in charges for services of \$1,263,785. On the expenditure side, there was an increase in service charges of \$1,984,141, while interest expense and transfers out reflect decreases of \$1,611,113 and \$1,417,356, respectively.

Financial Analysis of the Major Funds

General Fund

Revenues of the general fund totaled \$62,572,512 for the year ended December 31, 2011. The following represents a summary of general fund revenue, for the years ended December 31, 2011 and 2010 by source, along with changes from 2010:

CITY OF BETHLEHEM, PENNSYLVANIA

Management's Discussion and Analysis (Unaudited)

	2011	2010	Change From 2010 to 2011	Percentage Change
Taxes	\$ 32,273,738	\$ 27,457,670	\$ 4,816,068	17.54%
Licenses and permits	2,228,236	1,803,116	425,120	23.58%
Intergovernmental revenues	8,963,649	7,005,410	1,958,239	27.95%
Fines and forfeitures	547,875	569,920	(22,045)	-3.87%
Departmental earnings	6,956,877	5,744,600	1,212,277	21.10%
Other charges	589,419	657,230	(67,811)	-10.32%
Municipal recreation	378,706	379,298	(592)	-0.16%
Investment income	10,547	2,475	8,072	326.14%
Host fee	9,182,235	8,757,801	424,434	4.85%
Other	1,441,230	1,337,736	103,494	7.74%
Total	\$ 62,572,512	\$ 53,715,256	\$ 8,857,256	16.49%

Taxes increased \$4,816,068 from 2010 to 2011. The increase was due to an increase in earned income tax of \$3.9 million which was caused by a transfer of EIT collection to a third party per State law. The City then was able to pay out all remaining funds owed the City through internal collection. Current real estate taxes increased by \$1.3 million which was largely due to a millage increase of .75 mills.

Intergovernmental revenues increased \$1,958,239 from 2010 to 2011. This was the result of an increase in the State Subsidy for Pension of \$2.1 million, which according to the State was a one-time increase for 2011.

Departmental earnings increased \$1,212,277 from 2010 to 2011. The increase was largely due to an increase in the annual recycling fee as well as an increase in revenues from the sale of recyclable materials. Market prices were up in 2011 from 2010.

Licenses and permits increased \$425,120 from 2010 to 2011. The increase was due to an increase in building and occupancy permits of \$321,085.

Host Fee increased \$424,434 from 2010 to 2011. The increase was due to table games being in operation for a full year in 2011 as table games first became operational in July 2010.

General fund expenditures totaled \$58,582,926, which represents an increase of \$2,173,494, or 3.9% from 2010. The following represents a summary of general fund expenditures for the years ended December 31, 2011 and 2010, by function, along with changes from 2010:

CITY OF BETHLEHEM, PENNSYLVANIA

Management's Discussion and Analysis (Unaudited)

	2011	2010	Change From 2010 to 2011	Percentage Change
General government	\$ 702,484	\$ 686,276	\$ 16,208	2.36%
Administrative	882,207	1,446,173	(563,966)	-39.00%
Community development	5,221,596	5,486,374	(264,778)	-4.83%
Parks and public property	2,873,178	2,971,231	(98,053)	-3.30%
Public works	4,236,235	4,788,843	(552,608)	-11.54%
Police	13,295,034	13,447,266	(152,232)	-1.13%
Fire	10,451,184	10,496,522	(45,338)	-0.43%
General expenditures	18,613,088	15,606,883	3,006,205	19.26%
Civic	99,863	137,448	(37,585)	-27.34%
Library	1,230,000	1,194,000	36,000	3.02%
Debt service - principal	103,386	142,662	(39,276)	-27.53%
Debt service - interest	874,671	5,754	868,917	15101.09%
Total	\$ 58,582,926	\$ 56,409,432	\$ 2,173,494	3.85%

The increase in General fund expenditures is the result of the following:

- General expenditures increased by \$3,006,205 due to the City paying all outstanding claims payable from 2010 in 2011 along with paying all claims as incurred in 2011.
- Debt service interest expense increased by \$868,917 due to bond issuance costs from the 2011 working capital borrowing.
- Administrative expenses decreased by \$563,966 due to the elimination of eleven positions in 2011. Salaries decreased by \$585,725.
- Public works decreased by \$552,608 due to the elimination of seven positions in 2011. Salaries decreased by \$482,826.

Non-Utility Capital Improvements Fund

Cash and cash equivalents decreased by approximately \$5.9 million. This was caused by a reclassification of the 2010 C Note to a due from the General Fund.

Intergovernmental revenues increased by approximately \$3 million from 2010. Capital grants vary from year to year, but some of the larger ones reported for the year ended December 31, 2011 were the Room-to-Grow grant, which was for Library renovations, grants for additional work on the Greenway, and an ARRA grant for Broad Street to Pennsylvania Avenue street projects.

CITY OF BETHLEHEM, PENNSYLVANIA

Management's Discussion and Analysis (Unaudited)

Capital outlays increased by approximately \$3.5 million. This increase is a reflection on the capital grants the City received for the library renovations, Greenway, and street projects mentioned in the preceding paragraph.

Other Non-Major Governmental Funds

The Other Non-Major Governmental Funds revenues are derived from specific sources and are restricted for specific uses. Such funds, primarily Commonwealth of Pennsylvania and federal grants, are restricted by law or other formal action to expenditure for specific purposes.

Pension Trust Fund

At December 31, 2011, the fund balance - reserved for employees' retirement pension benefits was \$113,407,709. In 2004, the City issued a pension bond to fund the unfunded liability as of December 31, 2004. The average interest rate all inclusive with costs of the pension bond is 5.5%. The Fund returned 2.15% in 2011. However, the Fund returned an average of 7.73% annually since its inception in 1987.

Capital Assets

The City's investment in capital assets for its government and business-type activities as of December 31, 2011 amounted to \$57,907,240 and \$98,409,604 (net of accumulated depreciation), respectively. This investment in capital assets includes land and improvements, buildings and improvements, furniture, machinery, equipment, and infrastructure including but not limited to roads, bridges, streetlights, dams, and storm sewer systems.

Major capital asset events during the current year for governmental activities included the following:

- The City spent \$1,787,708 towards improvements at Broad St. and Pennsylvania Ave.
- The City spent \$1,256,258 towards Phase I and II of the Greenway.
- The City spent \$909,684 on street overlays
- The City spent \$729,473 towards improvements to the library building.
- The City spent \$660,249 towards improvements to the City's ice rink.

Major capital asset events during the current year for business-type activities included the following:

- The City spent \$1,558,566 to implement organic capacity improvements at the wastewater treatment plant.
- The City spent \$1,226,727 to replace floating cover on the 12 MG SW reservoir. Also to install sump pumps, electrical work, and construction management.
- The City spent \$262,438 to upgrade Water Treatment Plant and Water Control SCADA systems due to obsolescence of current system.

CITY OF BETHLEHEM, PENNSYLVANIA

Management's Discussion and Analysis (Unaudited)

- The City spent \$212,491 on engineering, maintenance, and retrofit work on the Northeast Standpipe.

Additional information on the City's capital assets can be found at Note 4 on pages 38-41.

Long-Term Debt

As of December 31, 2011, the City's net non-electoral debt of \$56,024,816, (net of deductions of \$27,525,132), is well below the legal limit of \$149,557,575. Additional information on the City's long-term debt can be found at Note 7 on pages 43-54 of this report.

The City's bonds have a rating from Standard and Poor's Rating Group of "BBB" (Stable Outlook).

Economic Outlook

While the national and world economy remain shaky, Bethlehem continues to enjoy steady growth. Liberty Property Trust just completed a 1.5 million square foot (SF) warehouse just off Commerce Center Blvd, which when full could house up to 500 jobs. Additionally, Liberty Property Trust received approval to construct another 800,000 SF warehouse in another portion of LVIP VII. Majestic Realty is presently constructing an 800,000 SF warehouse that will house a Crayola distribution center. Finally, an additional development for the construction of a 200,000 plus SF facility in LVIP VII received approval in the City earlier this year.

The Sands Casino Resort Bethlehem continues to be one of the top performing casinos in the Commonwealth. The opening of the Sands Hotel has only fueled additional growth. This year the Sands completed construction on a 50,000 SF (3,000 seat) flexible multi-purpose event center and 200,000 SF (35-store) retail space; thus, completing Phase One of its development.

The City continues to excel locally as a technology hub. The City opened an 8,000 SF post-incubator technology center, which is full and houses 8 companies and over 40 jobs. The incubators in the City, TechVentures2 and TechVentures, run by the Ben Franklin Technology Partners continue to excel. Recently, TechVentures was named the incubator of the year by the National Business Incubation Association.

The success of Bethlehem as a tourism and entertainment destination extends beyond the Sands Casino Resort. The downtown business districts remain steady. The flagship hotel, the Hotel Bethlehem, enjoyed its best fourth quarter in 2011 and its best December in 2011, which are strong signs of the strength of the City's tourism economy, especially given the instability and limited growth of the national economy.

Overall, the City has continued to see growth in the diversity of its business community. This should lead to the creation of new jobs and new ratables.

CITY OF BETHLEHEM, PENNSYLVANIA

Management's Discussion and Analysis (Unaudited)

The following is a list of other major development projects:

Residential		Status as of August 2012
Cantelmi Condos	3,400,000	Plans Submitted
Central Park West	5,500,000	Under Construction
Cherokee Court Condos	1,800,000	Plans Approved
Clermont Development	500,000	Plans Approved
Elliott Ave. Development	3,600,000	Plans Approved
Evans St. Apartment Building (not townhouse)	3,000,000	Plans Approved
Glenwood Subdivision (Miga-Glenwood)	900,000	Plans Approved
Habitat for Humanity 9th & Williams	1,200,000	Plans Approved
Henn - Kelchner Road Condos	2,100,000	Plans Approved
Kelchner Rd. Condominiums (Rose Hill Condos)	1,820,000	Plans Approved
Lengyel Apartments	1,600,000	Plans Approved
Minsi Ridge	4,050,000	Under Construction/Portions Complete
Mountain Park Condominiums	6,000,000	Under Construction/Portions Complete
Overlook at Saucon Creek	3,000,000	Under Construction/Portions Complete
Park View Commons	3,000,000	Under Construction/Portions Complete
Riverview Heights	5,000,000	Under Construction
Saucon Square Condominiums	3,500,000	Construction Complete
Silk Mill Apartments (Phase 1 & 2)	13,000,000	Portions Complete/Phase II Plans Approved
Stever Mills on Creek Rd.	15,000,000	Under Construction/Portions Complete
Villas at Saucon Valley	12,000,000	Under Construction/Portions Complete
Residential Subtotal	89,970,000	
Residential/Senior		
Cottages @ Monocacy Manor	4,500,000	Under Construction
Moravian Village	12,900,000	Construction Complete
Turnberry Mews	10,000,000	Under Construction/Portions Complete
Residential/Senior Subtotal	27,400,000	

CITY OF BETHLEHEM, PENNSYLVANIA

Management's Discussion and Analysis (Unaudited)

		Status as of August 2012
Institutional		
BASD	729,720	Construction Complete
East Stroudsburg University Extended Learning	400,000	Under Construction
Lehigh University Goodman Campus/Other	2,762,532	Under Construction/Portions Complete
Lehigh Valley Community Health Center	3,000,000	Under Construction
Lehigh Valley Hospital-Mulenburg	5,172,503	Under Construction/Portions Complete
Negrao Preschool	1,294,800	Under Construction
Moravian College	1,144,201	Under Construction
Moravian Village Memory Care Facility	20,000,000	Plans Approved
Moravian Collection Resource Center	2,500,000	Under Construction
Ben Franklin Tech Expansion	17,000,000	Under Construction/Portions Complete
Brookside Drug, Alc & Psych Facility	13,130,000	Plans Submitted
Pi	750,000	Construction Complete
St. Lukes at Northampton Community College	2,630,000	Construction Complete
Performing Arts Charter School	25,000,000	Plans Submitted
Institutional Subtotal	95,513,756	
Mixed-Use		
Conradical Clever Closets	886,400	Plans Approved
Farr Building	5,500,000	Under Construction
Jack Jones Building	3,200,000	Plans Approved
James Best Mixed Commercial/Residential	5,154,200	Under Construction
Plaza on 8th Mixed Use/Commercial	25,000,000	Under Construction/Portions Complete
SteelStacks Campus	57,500,000	Under Construction/Portions Complete
NMIH	26,000,000	Under Construction
Martin Towner	300,000,000	Plans Approved
Taylor Court-Jace Place Development	5,000,000	Under Construction
409-411 Wyandotte Mixed Use	750,000	Plans Approved
Mixed-Use Subtotal	428,990,600	
Industrial		
Gardner Cryogenics	1,980,000	Plans Submitted
Freedom Lawn Care	586,850	Under Construction
Lusitania Bakery	200,000	Under Construction
LVIP VII LBT Warehouse (lots 3,4,5)	44,000,000	Plans Approved
LVIP VII Commerce Ctr Blvd. Warehouse	74,250,000	Under Construction
LVIP VII Lot 13 Warehouse	9,702,000	Planning Commission Approved
Majestic Bethlehem Center	500,000,000	Under Construction
National Magnetic Corporation	250,000	Under Construction
Patriot Distribution	11,770,000	Plans Approved
Triangle Tech	400,000	
Industrial Subtotal	643,138,850	

CITY OF BETHLEHEM, PENNSYLVANIA

Management's Discussion and Analysis (Unaudited)

Commercial		Status as of August 2012
Big Woody's	409,650	Construction Complete
Chevy21	365,000	Under Construction/Portions Complete
Concret Décor	300,000	Construction Complete
Eaton Pointe	5,119,500	Construction Complete
Freedom Lawn Care	533,500	Plans Approved
IQE Expansion	977,000	Construction Complete
Moe's Southwest Grille	250,000	Under Construction
One West Fourth	2,000,000	Under Construction/Portions Complete
Polk St. North Building	18,000,000	Plans Approved
Sands Retail / Event Center	30,000,000	Construction Complete
Steel Pub Ice	600,000	Construction Complete
Stefko Grocery - Bottom Dollar	1,830,000	Construction Complete
TD Bank @ Five-Points	1,100,000	Construction Complete
The Lodge Café	500,000	Construction Complete
Third and Taylor Office Building	9,750,000	Plans Approved
Commercial Subtotal	71,734,650	
Grand Total	\$ 1,356,747,856	

Requests For Information

Questions concerning any of the information provided in this report or requests for additional financial information and complete financial statements for the discretely presented component units should be addressed to the Administration Department, City of Bethlehem, 10 East Church Street, Bethlehem, Pennsylvania 18018.

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CITY OF BETHLEHEM, PENNSYLVANIA

STATEMENT OF NET ASSETS

DECEMBER 31, 2011

Assets	Governmental Activities	Business-Type Activities	Total Primary Government	Component Units	Total Reporting Entity
Current assets:					
Cash and cash equivalents	\$ 7,370,492	\$ 864,950	\$ 8,235,442	\$ 8,250,733	\$ 16,486,175
Investments	101,413	16,289	117,702	1,213	118,915
Receivables (net of allowance for uncollectibles):					
Taxes	3,874,004	-	3,874,004	-	3,874,004
Accounts	826,222	5,502,698	6,328,920	357,145	6,686,065
Grants	-	133,788	133,788	1,022,083	1,155,871
Pledges	-	-	-	31,133	31,133
Other	1,047,103	-	1,047,103	36,600	1,083,703
Accrued interest	-	8,042	8,042	-	8,042
Due from other governments	7,116,817	-	7,116,817	-	7,116,817
Internal balances	1,013,752	(1,013,752)	-	-	-
Inventories	-	207,110	207,110	-	207,110
Prepaid assets	-	-	-	26,015	26,015
Total current assets	21,349,803	5,719,125	27,068,928	9,724,922	36,793,850
Noncurrent assets:					
Loans receivable	2,550,078	-	2,550,078	-	2,550,078
Restricted cash and cash equivalents	-	2,013,754	2,013,754	-	2,013,754
Restricted investments	-	12,623,585	12,623,585	1,322,142	13,945,727
Capital assets, not being depreciated	10,290,485	4,133,603	14,424,088	825,221	15,249,309
Capital assets, net	47,616,755	94,276,001	141,892,756	16,717,545	158,610,301
Other assets	2,724,211	2,170,730	4,894,941	1,684,622	6,579,563
Total noncurrent assets	63,181,529	115,217,673	178,399,202	20,549,530	198,948,732
Total Assets	84,531,332	120,936,798	205,468,130	30,274,452	235,742,582

(Continued)

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

Liabilities	Governmental Activities	Business-Type Activities	Total Primary Government	Component Units	Total Reporting Entity
Current liabilities:					
Accounts payable and other accrued expenses	2,724,821	1,804,248	4,529,069	557,337	5,086,406
Accrued payroll	1,508,448	314,347	1,822,795	121,119	1,943,914
Accrued vacation and other compensated absences	814,018	635,528	1,449,546	364,349	1,813,895
Claims payable	16,029	-	16,029	-	16,029
Interest payable	757,061	387,502	1,144,563	130,166	1,274,729
Escrow liabilities	5,136	-	5,136	-	5,136
Current portion of long-term debt	3,090,000	8,066,318	11,156,318	6,093,557	17,249,875
Current portion of capital lease obligations	162,049	16,095	178,144	52,137	230,281
Due to agency fund	3,315,966	164,274	3,480,240	-	3,480,240
Deferred revenue	7,407,749	-	7,407,749	153,143	7,560,892
Total current liabilities	19,801,277	11,388,312	31,189,589	7,471,808	38,661,397
Noncurrent liabilities:					
Accrued vacation and other compensated absences, net of current portion	2,827,572	-	2,827,572	-	2,827,572
Accrued sick pay	-	127,842	127,842	-	127,842
Long-term debt, net of current portion	86,848,886	103,593,238	190,442,124	26,575,278	217,017,402
Capital lease obligation, net of current portion	160,105	21,202	181,307	227,684	408,991
Other post-employment benefit liability	2,555,543	544,947	3,100,490	-	3,100,490
Deferred revenue	-	-	-	434,450	434,450
Total noncurrent liabilities	92,392,106	104,287,229	196,679,335	27,237,412	223,916,747
Total Liabilities	112,193,383	115,675,541	227,868,924	34,709,220	262,578,144
Net Assets					
Invested in capital assets, net of related debt	29,407,634	2,844,816	32,252,450	3,925,923	36,178,373
Restricted	548,734	-	548,734	1,322,142	1,870,876
Unrestricted	(57,618,419)	2,416,441	(55,201,978)	(9,682,833)	(64,884,811)
Total Net Assets	\$ (27,662,051)	\$ 5,261,257	\$ (22,400,794)	\$ (4,434,768)	\$ (26,835,562)

(Concluded)

CITY OF BETHLEHEM, PENNSYLVANIA

STATEMENT OF ACTIVITIES

YEAR ENDED DECEMBER 31, 2011

<u>Function/Programs:</u>	<u>Expenses</u>	<u>Program Revenues</u>		
		<u>Charges for Services</u>	<u>Operating Grants and Contributions</u>	<u>Capital Grants and Contributions</u>
Primary government:				
Governmental activities:				
General government	\$ 722,426	\$ -	\$ -	\$ -
Administrative	1,131,440	282,958	-	-
Community development	5,438,536	4,142,243	5,417,833	157,883
Parks and public property	4,317,501	536,709	981,624	1,643,604
Public works	8,035,675	1,329,166	1,732,511	1,709,509
Police	16,313,591	2,729,782	1,744,575	131,332
Fire	10,858,971	2,928,668	2,063	205,858
General expenditures	14,189,563	-	-	-
Civic	99,863	-	-	-
Library	1,173,073	-	-	478,487
Program expenditures	3,720,776	-	-	-
Interest on long-term debt	4,965,648	-	-	-
Total governmental activities	70,967,063	11,949,526	9,878,606	4,326,673
Business-type activities:				
Water Fund	19,347,748	17,504,426	-	989,518
Sewer Fund	10,560,066	11,952,682	-	723,031
Other non-major funds	1,298,739	1,326,279	-	-
Total business-type activities	31,206,553	30,783,387	-	1,712,549
Total primary government	\$ 102,173,616	\$ 42,732,913	\$ 9,878,606	\$ 6,039,222
Component units:				
Bethlehem Parking Authority	\$ 4,287,968	\$ 3,852,573	\$ -	\$ 1,022,083
Bethlehem Public Library	3,448,472	262,985	3,186,957	-
Bethlehem Redevelopment Authority	21,438,115	-	-	14,460,220
Total component units	\$ 29,174,555	\$ 4,115,558	\$ 3,186,957	\$ 15,482,303

General Revenues:

Real estate taxes and other taxes

Grants and other charges not restricted
to specific programs

Investment income

Transfers

Total general revenues and transfers

Change in Net Assets

Net Assets:

Beginning of year

End of year

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

Net (Expense) Revenue and
Changes in Net Assets

Primary Government			Component Units	Total Reporting Entity
Governmental Activities	Business-Type Activities	Total		
\$ (722,426)	\$ -	\$ (722,426)	\$ -	\$ (722,426)
(848,482)	-	(848,482)	-	(848,482)
4,279,423	-	4,279,423	-	4,279,423
(1,155,564)	-	(1,155,564)	-	(1,155,564)
(3,264,489)	-	(3,264,489)	-	(3,264,489)
(11,707,902)	-	(11,707,902)	-	(11,707,902)
(7,722,382)	-	(7,722,382)	-	(7,722,382)
(14,189,563)	-	(14,189,563)	-	(14,189,563)
(99,863)	-	(99,863)	-	(99,863)
(694,586)	-	(694,586)	-	(694,586)
(3,720,776)	-	(3,720,776)	-	(3,720,776)
(4,965,648)	-	(4,965,648)	-	(4,965,648)
(44,812,258)	-	(44,812,258)	-	(44,812,258)
-	(853,804)	(853,804)	-	(853,804)
-	2,115,647	2,115,647	-	2,115,647
-	27,540	27,540	-	27,540
-	1,289,383	1,289,383	-	1,289,383
(44,812,258)	1,289,383	(43,522,875)	-	(43,522,875)
-	-	-	586,688	586,688
-	-	-	1,470	1,470
-	-	-	(6,977,895)	(6,977,895)
-	-	-	(6,389,737)	(6,389,737)
32,475,537	-	32,475,537	-	32,475,537
15,446,948	-	15,446,948	-	15,446,948
114,897	481,026	595,923	44,807	640,730
2,280,924	(2,280,924)	-	-	-
50,318,306	(1,799,898)	48,518,408	44,807	48,563,215
5,506,048	(510,515)	4,995,533	(6,344,930)	(1,349,397)
(33,168,099)	5,771,772	(27,396,327)	1,910,162	(25,486,165)
\$ (27,662,051)	\$ 5,261,257	\$ (22,400,794)	\$ (4,434,768)	\$ (26,835,562)

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

CITY OF BETHLEHEM, PENNSYLVANIA

BALANCE SHEET GOVERNMENTAL FUNDS

DECEMBER 31, 2011

	General Fund	Non-Utility Capital Improvements Fund	Other Non-Major Governmental Funds	Total Governmental Funds
Assets				
Cash and cash equivalents	\$ 3,327,568	\$ 1,925,870	\$ 2,093,469	\$ 7,346,907
Investments	-	101,413	-	101,413
Receivables:				
Taxes	3,874,004	-	-	3,874,004
Accounts	661,477	-	-	661,477
Loans	-	-	2,550,078	2,550,078
Other	951,411	10,804	84,888	1,047,103
Due from other funds	1,237,236	2,697,824	549,080	4,484,140
Due from other governments	6,323,977	605,436	187,404	7,116,817
Total Assets	\$ 16,375,673	\$ 5,341,347	\$ 5,464,919	\$ 27,181,939
Liabilities and Fund Balance				
Liabilities:				
Accounts payable and other accrued expenses	\$ 1,521,719	\$ 886,903	\$ 316,199	\$ 2,724,821
Accrued payroll	1,440,311	-	68,137	1,508,448
Accrued vacation and other compensated absences	766,439	-	47,579	814,018
Escrow liabilities	5,136	-	-	5,136
Due to other funds	6,720,963	65,570	-	6,786,533
Deferred revenues	3,018,893	194,644	7,004,250	10,217,787
Total Liabilities	13,473,461	1,147,117	7,436,165	22,056,743
Fund Balances:				
Restricted for:				
Parks and public property	213,336	-	-	213,336
Community development	174,006	-	-	174,006
Capital projects	1,049,265	4,194,230	-	5,243,495
Public works	-	-	161,392	161,392
Unassigned	1,465,605	-	(2,132,638)	(667,033)
Total Fund Balance	2,902,212	4,194,230	(1,971,246)	5,125,196
Total Liabilities and Fund Balance	\$ 16,375,673	\$ 5,341,347	\$ 5,464,919	\$ 27,181,939

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

CITY OF BETHLEHEM, PENNSYLVANIA

RECONCILIATION OF THE BALANCE SHEET OF GOVERNMENTAL FUNDS TO THE STATEMENT OF NET ASSETS

DECEMBER 31, 2011

Total Fund Balance - Governmental Funds	\$ 5,125,196
Amounts reported for governmental activities in the statement of net assets are different because:	
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.	57,907,240
Real estate taxes, earned income taxes, and the stakeholder agreement not collected within a period of time subsequent to year-end are not deferred in the statement of net assets.	2,810,038
Accrued vacation and other compensated absences not due within the next twelve months are recorded on the statement of net assets.	(2,827,572)
Other post-employment benefit liability is recorded on the statement of net assets.	(2,555,543)
Debt issuance costs and loss on refunding are deferred and amortized on the statement of net assets.	2,794,754
Long-term liabilities, including bonds payable and capital lease obligations, are not due and payable in the current period and, therefore, are not reported in the funds:	
Bonds	(90,009,429)
Capital leases	(322,154)
Accrued interest payable included on the statement of net assets.	(757,061)
Assets and liabilities of the internal service fund reported in the statement of net assets are used to charge the costs of insurance to individual funds and are not reported in the governmental funds.	172,480
Net Assets - Governmental Activities	<u>\$ (27,662,051)</u>

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

CITY OF BETHLEHEM, PENNSYLVANIA

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE - GOVERNMENTAL FUNDS

YEAR ENDED DECEMBER 31, 2011

	General Fund	Non-Utility Capital Improvements Fund	Other Nonmajor Governmental Funds	Total Governmental Funds
Revenues:				
Taxes	\$ 32,273,738	\$ -	\$ -	\$ 32,273,738
Licenses and permits	2,228,236	-	-	2,228,236
Intergovernmental revenues	8,963,649	4,730,819	5,965,012	19,659,480
Fines and forfeitures	547,875	-	-	547,875
Departmental earnings	6,956,877	-	-	6,956,877
Other charges	589,419	-	604,038	1,193,457
Municipal recreation	378,706	-	-	378,706
Investment income	10,547	621	103,729	114,897
Host fee	9,182,235	-	-	9,182,235
Other	1,441,230	18,998	56,473	1,516,701
Total revenues	62,572,512	4,750,438	6,729,252	74,052,202
Expenditures:				
Current:				
General government	702,484	-	-	702,484
Administrative	882,207	-	-	882,207
Community development	5,221,596	-	-	5,221,596
Parks and public property	2,873,178	-	-	2,873,178
Public works	4,236,235	-	1,565,072	5,801,307
Police	13,295,034	-	1,683,281	14,978,315
Fire	10,451,184	-	-	10,451,184
General expenditures	18,613,088	-	-	18,613,088
Civic	99,863	-	-	99,863
Library	1,230,000	-	-	1,230,000
Program expenditures	-	-	4,432,868	4,432,868
Capital outlays	-	7,231,683	-	7,231,683
Debt service - principal	103,386	9,709,502	2,952,000	12,764,888
Debt service - interest	874,671	924,815	4,509,838	6,309,324
Total expenditures	58,582,926	17,866,000	15,143,059	91,591,985
Excess (Deficiency) of Revenues Over Expenditures	3,989,586	(13,115,562)	(8,413,807)	(17,539,783)
Other Financing Sources (Uses):				
Transfers in	2,930,189	720,752	8,342,518	11,993,459
Transfers out	(7,431,545)	(1,893,781)	(387,209)	(9,712,535)
Issuance of long-term debt	17,805,000	14,665,000	-	32,470,000
Payment to refunded bond escrow agent	-	(3,953,300)	-	(3,953,300)
Proceeds from capital lease	73,196	149,671	-	222,867
Original issue discount	(234,556)	(136,238)	-	(370,794)
Total other financing sources (uses)	13,142,284	9,552,104	7,955,309	30,649,697
Net Change in Fund Balance	17,131,870	(3,563,458)	(458,498)	13,109,914
Fund Balance:				
Beginning of the year	(14,229,658)	7,757,688	(1,512,748)	(7,984,718)
End of the year	\$ 2,902,212	\$ 4,194,230	\$ (1,971,246)	\$ 5,125,196

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

CITY OF BETHLEHEM, PENNSYLVANIA
RECONCILIATION OF THE STATEMENT OF REVENUES,
EXPENDITURES, AND CHANGES IN FUND BALANCE OF
GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
YEAR ENDED DECEMBER 31, 2011

Net Change in Fund Balance - Governmental Funds	\$ 13,109,914
Amounts reported for governmental activities in the statement of activities are different because:	
Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays (\$8,942,888) exceeded depreciation (\$6,347,545) and loss on disposal (\$145,031) in the current period.	2,450,312
Revenues related to real estate taxes and earned income taxes in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.	139,985
The issuance of long-term debt (e.g., bonds, leases) provides current financial resources to governmental funds, while repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets. This amount is the net effect of those differences in the treatment of long-term debt.	
Issuance of debt	(32,692,867)
Repayment of principal	16,639,888
Accrued interest expense on long-term debt is reported in the statement of activities but does not require the use of current financial resources; therefore, accrued interest expense is not reported as expenditures in governmental funds.	(5,498)
Change in accrued vacation and other compensated absences not due within the next twelve months in the statement of activities.	150,282
Change in other post-employment benefit liability in the statement of activities.	(507,761)
Governmental funds report the effect of issuance costs, premiums, discounts, and similar items when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities.	1,798,268
Activities of the internal service fund are reported as net income within the statement of activities.	4,423,525
Change in Net Assets - Governmental Activities	\$ 5,506,048

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

CITY OF BETHLEHEM, PENNSYLVANIA

BALANCE SHEET - PROPRIETARY FUNDS

DECEMBER 31, 2011

Assets	Enterprise Funds				
	Water Fund	Sewer Fund	Other Enterprise Fund		Internal Service
			Municipal Golf Fund	Total	
Current assets:					
Cash and cash equivalents	\$ 407,644	\$ 420,719	\$ 36,587	\$ 864,950	\$ 23,585
Investments	-	16,289	-	16,289	-
Accounts receivable, net	2,768,986	2,733,712	-	5,502,698	164,745
Grants receivable	133,788	-	-	133,788	-
Accrued interest	8,042	-	-	8,042	-
Due from other funds	188,130	300,000	10,570	498,700	179
Inventories	140,781	16,577	49,752	207,110	-
Total current assets	3,647,371	3,487,297	96,909	7,231,577	188,509
Restricted assets:					
Cash and cash equivalents	2,012,426	-	1,328	2,013,754	-
Investments	12,623,585	-	-	12,623,585	-
Capital assets, not being depreciated	2,582,886	1,375,717	175,000	4,133,603	-
Capital assets, net	85,218,759	8,506,917	550,325	94,276,001	-
Other assets	2,106,602	60,186	3,942	2,170,730	-
Total Assets	\$ 108,191,629	\$ 13,430,117	\$ 827,504	\$ 122,449,250	\$ 188,509
Liabilities and Net Assets					
Liabilities:					
Current liabilities:					
Accounts payable and other accrued expenses	\$ 534,701	\$ 528,406	\$ 69,079	\$ 1,132,186	\$ -
Accrued payroll	181,757	116,342	16,248	314,347	-
Accrued vacation and other compensated absences	355,814	237,720	41,994	635,528	-
Construction accounts payable	672,062	-	-	672,062	-
Claims payable	-	-	-	-	16,029
Interest payable	348,103	33,987	5,412	387,502	-
Current portion of long-term debt	5,741,248	2,265,070	60,000	8,066,318	-
Current portion of capital lease obligation	-	-	16,095	16,095	-
Due to other funds	1,430,496	133,130	113,100	1,676,726	-
Total current liabilities	9,264,181	3,314,655	321,928	12,900,764	16,029
Accrued sick pay	84,959	42,883	-	127,842	-
Long-term debt, net	100,642,005	2,683,233	268,000	103,593,238	-
Capital lease obligation, net	-	-	21,202	21,202	-
Other post-employment benefits liability	327,403	177,933	39,611	544,947	-
Total Liabilities	110,318,548	6,218,704	650,741	117,187,993	16,029
Net Assets:					
Invested in capital assets, net of related debt	(2,511,057)	4,994,517	361,356	2,844,816	-
Unrestricted	384,138	2,216,896	(184,593)	2,416,441	172,480
Total Net Assets	(2,126,919)	7,211,413	176,763	5,261,257	172,480
Total Liabilities and Net Assets	\$ 108,191,629	\$ 13,430,117	\$ 827,504	\$ 122,449,250	\$ 188,509

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

CITY OF BETHLEHEM, PENNSYLVANIA

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN IN NET ASSETS - PROPRIETARY FUNDS

YEAR ENDED DECEMBER 31, 2011

	Enterprise Funds				Internal Service
	Water Fund	Sewer Fund	Other Enterprise Fund		
			Municipal Golf Fund	Total	
Operating Revenues:					
Charges for services	\$ 17,248,546	\$ 11,759,169	\$ 1,317,541	\$ 30,325,256	\$ 12,691,709
Operating Expenses:					
Salaries, wages, and fringe benefits	4,636,162	3,473,339	661,849	8,771,350	-
Professional fees	676,912	195,310	3,088	875,310	-
Utilities	333,655	786,309	50,512	1,170,476	-
Maintenance and repairs	55,862	140,579	52,454	248,895	-
Department contracts	351,343	1,366,882	88,517	1,806,742	-
Supplies	793,336	574,186	144,509	1,512,031	-
Service charges	3,581,187	1,932,076	153,000	5,666,263	-
Depreciation and amortization	4,746,637	1,635,637	87,024	6,469,298	-
Insurance claims	-	-	-	-	8,282,574
Administration	-	-	-	-	79,013
Other	317,859	305,413	40,336	663,608	-
Total operating expenses	15,492,953	10,409,731	1,281,289	27,183,973	8,361,587
Operating Income	1,755,593	1,349,438	36,252	3,141,283	4,330,122
Non-Operating Revenues (Expenses):					
Investment income	480,090	936	-	481,026	24
Interest expense	(3,854,795)	(150,335)	(17,450)	(4,022,580)	-
Grants	989,518	723,031	-	1,712,549	-
Other revenues	255,880	193,513	8,738	458,131	93,379
Total non-operating revenues (expenses)	(2,129,307)	767,145	(8,712)	(1,370,874)	93,403
Change in net assets before transfers	(373,714)	2,116,583	27,540	1,770,409	4,423,525
Transfers out	(300,000)	(1,980,924)	-	(2,280,924)	-
Change in Net Assets	(673,714)	135,659	27,540	(510,515)	4,423,525
Net Assets:					
Beginning of year	(1,453,205)	7,075,754	149,223	5,771,772	(4,251,045)
End of year	<u>\$ (2,126,919)</u>	<u>\$ 7,211,413</u>	<u>\$ 176,763</u>	<u>\$ 5,261,257</u>	<u>\$ 172,480</u>

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

CITY OF BETHLEHEM, PENNSYLVANIA

STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS

YEAR ENDED DECEMBER 31, 2011

	Enterprise Funds				Internal Service
	Water Fund	Sewer Fund	Other	Total	
			Enterprise Fund Municipal Golf Fund		
Cash Flows From Operating Activities:					
Receipts from customers	\$ 18,825,229	\$ 11,581,993	\$ 1,317,541	\$ 31,724,763	\$ 12,526,964
Payments to suppliers for services	(5,566,958)	(5,309,456)	(555,865)	(11,432,279)	(12,741,585)
Payment to employees	(4,581,246)	(3,448,686)	(676,751)	(8,706,683)	-
Net cash provided by (used in) operating activities	8,677,025	2,823,851	84,925	11,585,801	(214,621)
Cash Flows From Noncapital Financing Activities:					
Transfers out	(300,000)	(1,980,924)	-	(2,280,924)	-
Other revenues received	255,880	193,513	8,738	458,131	93,379
Net cash provided by (used in) noncapital financing activities	(44,120)	(1,787,411)	8,738	(1,822,793)	93,379
Cash Flows From Capital and Related Financing Activities:					
Acquisition and construction of capital assets	(2,416,314)	(2,448,777)	-	(4,865,091)	-
Grant proceeds	855,730	723,031	-	1,578,761	-
Principal payments on debt	(5,177,795)	(445,000)	(58,000)	(5,680,795)	-
Interest payments on debt	(3,370,579)	(152,853)	(17,544)	(3,540,976)	-
Principal payments on capital lease obligations	-	-	(38,764)	(38,764)	-
Proceeds from issuance of debt	1,330,812	578,756	-	1,909,568	-
Net cash used in capital and related financing activities	(8,778,146)	(1,744,843)	(114,308)	(10,637,297)	-
Cash Flows From Investing Activities:					
Net sales of investments	250,326	13,980	-	264,306	-
Interest and dividends on investments	480,090	936	-	481,026	24
Net cash provided by investing activities	730,416	14,916	-	745,332	24
Net Increase (Decrease) in Cash and Cash Equivalents	585,175	(693,487)	(20,645)	(128,957)	(121,218)
Cash and Cash Equivalents:					
Beginning of year	1,834,895	1,114,206	58,560	3,007,661	144,803
End of year	\$ 2,420,070	\$ 420,719	\$ 37,915	\$ 2,878,704	\$ 23,585

(Continued)

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

CITY OF BETHLEHEM, PENNSYLVANIA
STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS

YEAR ENDED DECEMBER 31, 2011

(Continued)

	Enterprise Funds				Internal Service
	Water Fund	Sewer Fund	Other Enterprise Fund Municipal Golf Fund	Total	
Reconciliation of Operating Income to Net Cash Provided by (Used in) Operating Activities:					
Operating income	\$ 1,755,593	\$ 1,349,438	\$ 36,252	\$ 3,141,283	\$ 4,330,122
Adjustments to reconcile operating income to net cash provided by (used in) operating activities:					
Depreciation and amortization	4,746,637	1,635,637	87,024	6,469,298	-
Changes in assets and liabilities:					
Accounts receivable	175,277	(31,344)	-	143,933	(164,745)
Due from other funds	9,410	(145,832)	-	(136,422)	-
Inventories	312,715	1,920	(24,677)	289,958	-
Other assets	-	-	2,800	2,800	-
Accrued vacation and other compensated absences	(18,000)	(8,457)	(17,706)	(44,163)	-
Accrued payroll	(3,616)	(5,064)	1,296	(7,384)	-
Accounts payable and other accrued expenses	230,481	(10,621)	(108,312)	111,548	-
Due to other funds	1,391,996	-	106,740	1,498,736	-
Other post-employment benefits liability	76,532	38,174	1,508	116,214	-
Claims payable	-	-	-	-	(4,379,998)
Net cash provided by (used in) operating activities	<u>\$ 8,677,025</u>	<u>\$ 2,823,851</u>	<u>\$ 84,925</u>	<u>\$ 11,585,801</u>	<u>\$ (214,621)</u>

(Concluded)

CITY OF BETHLEHEM, PENNSYLVANIA

STATEMENT OF FIDUCIARY NET ASSETS

DECEMBER 31, 2011

	Employee Benefit Trust Fund	Agency Fund
<hr/> Assets <hr/>		
Cash and cash equivalents	\$ -	\$ 1,234,966
Interest and dividends receivable	366,775	-
Due from the City	-	3,480,240
Investments	113,040,934	-
Total Assets	<u>113,407,709</u>	<u>4,715,206</u>
<hr/> Liabilities <hr/>		
Escrow liabilities	-	4,715,206
Total Liabilities	<u>-</u>	<u>\$ 4,715,206</u>
<hr/> Net Assets <hr/>		
Reserved for employees' retirement benefits	<u>113,407,709</u>	
Total Liabilities and Net Assets	<u>\$ 113,407,709</u>	

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

CITY OF BETHLEHEM, PENNSYLVANIA
STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
YEAR ENDED DECEMBER 31, 2011

	<u>Employee Benefit Trust Fund</u>
Additions:	
<hr/>	
Contributions:	
Employee contributions	\$ 1,395,424
Employer contributions	<u>4,663,325</u>
Total contributions	<u>6,058,749</u>
Investment earnings:	
Investment income	4,231,686
Realized and unrealized losses, net	<u>(1,593,100)</u>
Net investment earnings	<u>2,638,586</u>
Total additions	<u>8,697,335</u>
Deductions:	
<hr/>	
Benefits paid	9,674,174
Administrative costs	<u>671,574</u>
Total deductions	<u>10,345,748</u>
Change in Net Assets	(1,648,413)
Net Assets:	
<hr/>	
Beginning of year	<u>115,056,122</u>
End of year	<u><u>\$ 113,407,709</u></u>

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

CITY OF BETHLEHEM, PENNSYLVANIA

BALANCE SHEET - COMPONENT UNITS

DECEMBER 31, 2011

	Bethlehem Parking Authority	Bethlehem Public Library	Bethlehem Redevelopment Authority	Total
Assets				
Current assets:				
Cash and cash equivalents	\$ 241,911	\$ 627,860	\$ 7,380,962	\$ 8,250,733
Investments	1,213	-	-	1,213
Accounts receivable, net	288,594	10,585	57,966	357,145
Grant receivable	1,022,083	-	-	1,022,083
Pledges receivable	-	31,133	-	31,133
Other receivables	36,600	-	-	36,600
Prepaid expenses	26,015	-	-	26,015
Total current assets	1,616,416	669,578	7,438,928	9,724,922
Restricted investments	-	1,322,142	-	1,322,142
Capital assets, not being depreciated	825,221	-	-	825,221
Capital assets, net	16,569,863	116,387	31,295	16,717,545
Other assets	165,146	-	1,519,476	1,684,622
Total Assets	\$ 19,176,646	\$ 2,108,107	\$ 8,989,699	\$ 30,274,452

(Continued)

CITY OF BETHLEHEM, PENNSYLVANIA

BALANCE SHEET - COMPONENT UNITS

DECEMBER 31, 2011

(Continued)

	Bethlehem Parking Authority	Bethlehem Public Library	Bethlehem Redevelopment Authority	Total
Liabilities and Net Assets				
Liabilities:				
Accounts payable and other accrued expenses	\$ 534,056	\$ -	\$ 23,281	\$ 557,337
Accrued payroll	49,918	71,201	-	121,119
Accrued vacation and other compensated absences	104,108	260,241	-	364,349
Interest payable	130,166	-	-	130,166
Current portion of long-term debt	2,339,081	-	3,754,476	6,093,557
Current portion of capital lease obligation	52,137	-	-	52,137
Deferred revenue	153,143	-	-	153,143
Total current liabilities	3,362,609	331,442	3,777,757	7,471,808
Long-term debt, net	10,094,883	-	16,480,395	26,575,278
Capital lease obligation, net of current portion	227,684	-	-	227,684
Deferred revenue	434,450	-	-	434,450
Total Liabilities	14,119,626	331,442	20,258,152	34,709,220
Net Assets:				
Invested in capital assets, net of related debt	3,778,241	116,387	31,295	3,925,923
Restricted	-	1,322,142	-	1,322,142
Unrestricted	1,278,779	338,136	(11,299,748)	(9,682,833)
Total Net Assets	5,057,020	1,776,665	(11,268,453)	(4,434,768)
Total Liabilities and Net Assets	\$ 19,176,646	\$ 2,108,107	\$ 8,989,699	\$ 30,274,452

(Concluded)

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

CITY OF BETHLEHEM, PENNSYLVANIA

STATEMENT OF ACTIVITIES - COMPONENT UNITS

YEAR ENDED DECEMBER 31, 2011

	Program Revenues			Net (Expense) Revenue and Changes in Net Assets			Total	
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Bethlehem Parking Authority	Bethlehem Public Library		Bethlehem Redevelopment Authority
Bethlehem Parking Authority	\$ 4,287,968	\$ 3,852,573	\$ -	\$ 1,022,083	\$ 586,688	\$ -	\$ -	\$ 586,688
Bethlehem Public Library	3,448,472	262,985	3,186,957	-	-	1,470	-	1,470
Bethlehem Redevelopment Authority	21,438,115	-	-	14,460,220	-	-	(6,977,895)	(6,977,895)
Total Component Units	\$ 29,174,555	\$ 4,115,558	\$ 3,186,957	\$ 15,482,303	586,688	1,470	(6,977,895)	(6,389,737)
General Revenues:								
					5	26,359	18,443	44,807
					5	26,359	18,443	44,807
					586,693	27,829	(6,959,452)	(6,344,930)
Net Assets:								
					4,470,327	1,748,836	(4,309,001)	1,910,162
					\$ 5,057,020	\$ 1,776,665	\$ (11,268,453)	\$ (4,434,768)

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

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

Financial Reporting Entity

The City was incorporated in 1962 under the provisions of the constitution and general statutes of the Commonwealth of Pennsylvania. The City is a third class city, as defined by the state statutes. The City operates under a mayor-council form of government and provides a full range of services, including public safety, roads, sanitation, health, culture and recreation, and general government services.

Basis of Presentation

The government-wide financial statements (i.e., the statement of net assets 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.

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

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.

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

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

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 generally 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, as well as expenditures related to compensated absences, other post-employment benefits, and judgments and claims are recorded only when payment is due.

Property taxes, earned income taxes, telephone fees, licenses, and interest associated with the current fiscal period are all considered to be susceptible to accrual and have been recognized as revenues of the current fiscal period. In determining when to recognize intergovernmental revenues (grants and entitlements), the legal and contractual requirements of the individual programs are used as guidance. All other revenue items are considered to be measurable and available only when cash is received by the government.

The City reports the following major governmental funds:

The General Fund is the government's primary operating fund. It accounts for all financial resources of the general government, except those accounted for in another fund.

The Non-Utility Capital Improvements Fund is the fund used to account for acquisition, construction, and improvement of capital assets.

The City reports the following nonmajor governmental funds: 911 Fund, Community Development Block Grant Fund, Liquid Fuels Fund, and Debt Service Fund.

The City reports the following major proprietary funds:

The Water and Sewer Funds are financed and operated in a manner similar to private business enterprises, where the intent is that costs of providing these services to the general public on a continuing basis be financed or recovered primarily through user charges.

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

The Municipal Golf Fund is the City's nonmajor proprietary fund.

The Internal Service Fund is used to account for the financing of goods or services provided by one department or agency to other departments or agencies of the governmental unit on a cost-reimbursement basis. The Internal Service Fund accounts for the City's externally administered health insurance.

The City's Fiduciary Funds account for the Employee Benefit Trust Fund and Agency Fund. The Employee Benefit Trust Fund is maintained to account for assets held by the City in a trustee capacity for individuals currently or previously employed by the City.

The Agency Fund is used to account for funds held in escrow for other parties. The Agency fund is custodial in nature (assets equal liabilities) and does not involve measurement of results of operations. The Agency Fund accounts for the earned income taxes, payroll withholdings, and tax collections for the surrounding municipalities.

Proprietary funds distinguish *operating* revenues and expenses from *nonoperating* items. Operating revenues and expenses generally result from providing services in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the enterprise fund are charges to citizens for services. Operating expenses for the enterprise fund 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 government's policy to use restricted resources first, then unrestricted resources as they are needed.

Budgetary Accounting Control

Formal budgetary integration is employed as a management control device during the year for all funds of the City. Annual operating budgets are legally adopted for the General Fund, Water Fund, Sewer Fund, Municipal Golf Fund, all Capital Projects Funds, 911 Fund, Community Development Block Grant Fund, and Liquid Fuels Fund.

Upon enactment of the budgets by City Council, any amendments are developed by individual City departments and presented to the Finance Committee of City Council. Amendments as approved by the Finance Committee are submitted to the City Council to be read in a public hearing and ratified. A ratified budget amendment becomes effective ten days after being enacted. The Office of Budget and Finance can make intrafund budget transfers of up to five percent provided they do not alter total revenues or expenditures of such fund. Appropriations not reserved for encumbrances lapse at year-end.

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Derivative Financial Instrument

The City has entered into an interest rate swap agreement, which is considered a derivative financial instrument, to manage interest rate exposure in certain long-term debt. For the year ended December 31, 2010, the City was required to implement Governmental Accounting Standards Board (GASB) Statement No. 53, "*Accounting and Financial Reporting for Derivative Instruments*." However, the City considers the value of the swap to be immaterial. The swap agreement terminates in 2012. Therefore, other than the net interest expenditures resulting from this agreement, no amounts are recorded in the financial statements.

Cash, Cash Equivalents, and Investments

For purposes of the statement of cash flows, the Proprietary Funds consider all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased and all certificates of deposit to be cash equivalents.

Investments of the City are stated at fair value. Fair value is determined based on the last reported sales price on the last business day of the year; securities for which no sale was reported on that date are valued at the last reported bid price.

Internal Balances

Internal balances arise from interfund transactions and are recorded by all funds affected in the period in which transactions are executed.

Receivables

All receivables are reported at their gross value and, where appropriate, are reduced by the estimated portion that is expected to be uncollectible. Estimated unbilled revenues from the Water and Sewer Funds are recognized at the end of each fiscal year on a pro rata basis. The estimated amount is based on billings during the months following the close of the calendar year.

Stakeholder Agreement Receivable

In December 2007, the City entered into an agreement with certain parties to allow excess sewer capacity to be available to Bethlehem Township, in the event such parties develop within the Township. The transaction has been included in the financial statements as a voluntary non-exchange transaction. As of December 31, 2011, a receivable of \$294,668 and deferred revenue of \$294,668 still remained in the General Fund. Since the full \$5 million was recognized as revenue in the Governmental Activities statement of activities as of

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

December 31, 2007, no revenue is shown for the years ended December 31, 2008, 2009, 2010, or 2011. Per the agreement, the entire balance should have been received on or before December 31, 2009. One developer owes the remaining balance and the City has extended the due date of that payment to December 31, 2012. No allowance for uncollectible accounts has been established, as the City is confident payment will be made by December 31, 2012.

Property Taxes

Based upon assessed valuations provided by Lehigh and Northampton Counties, the City bills and collects its own property taxes. Delinquent taxes are turned over to an outside agency, which collects the taxes on behalf of the City. The schedule for property taxes levied for 2011 is as follows:

January 1, 2011	original levy date
January 1, 2011 - April 1, 2011	2% discount period
April 2, 2011 - May 27, 2011	face payment period
May 28, 2011 - December 30, 2011	10% penalty period

In addition, City taxes may be paid in four installments due approximately February 7, April 4, June 6, and August 1 of the tax year with no discount period allowed. Any delinquent installment is subject to a penalty of 10%.

The City is permitted by the Third Class City Code to levy real estate taxes up to 25 mills on every dollar of assessed valuation for general City purposes. The City's 2011 millage was 8.42 for general purposes, 0.75 for the construction of an EMS facility and acquisition of a fire pumper, 0.91 for recreation, 3.00 for debt service, 0.4 for landfill debt, 0.5 for Hirko settlement debt, and 0.87 for library.

Inventories

Inventories are valued at the lower of cost (first-in, first-out) or market. The costs of governmental fund-type inventories are recorded as expenditures when consumed rather than when purchased.

Interfund Transactions

As a result of its operations, the City affects a variety of transactions between funds to finance operations. Accordingly, to the extent that certain interfund transactions have not been paid or received as of December 31, 2011, appropriate interfund receivables or payables have been established.

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Capital Assets

All capital assets are valued at historical cost or estimated historical cost if actual historical cost is not available. Donated fixed assets are valued at their estimated fair value on the date donated. The City maintains a capitalization threshold of \$5,000 for all capital assets.

General infrastructure assets acquired prior to December 31, 2002 consist of streets and street lights, storm sewers, and bridges and are reported at estimated historical cost using deflated replacement cost. The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized.

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

<u>Asset Class</u>	<u>Estimated Useful Lives</u>
Infrastructure	25-50 years
Land improvements	20 years
Buildings and improvements	45 years.
Equipment	5-20 years

Amortization of assets purchased under capital leases is included in depreciation expense.

Restricted Investments

Restricted investments represent resources set aside for the liquidation of specific obligations and capital acquisitions.

Bond Discounts and Issuance Costs

Bond discounts and issuance costs are deferred and amortized over the term of the bonds using the straight-line method, which approximates the interest method.

Compensated Absences

The City's vacation policy provides that employees are to take unused vacation within a year following the year it was earned or the vacation time is lost to the employee, except that with

CITY OF BETHLEHEM, PENNSYLVANIA

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YEAR ENDED DECEMBER 31, 2011

the approval of the department head and the business administrator, employees may carry up to 30 days of vacation leave. In accordance with accounting principles generally accepted in the United States of America, the City accrues such benefits as they are earned. Employees, with the exception of police officers and firefighters, are permitted, under the City's present sick leave policy, to accumulate an unlimited number of days of sick leave to be paid to the employee when proper proof of illness is demonstrated. Police officers may accumulate up to 260 days of sick leave. Firefighters may accumulate up to 170 days of sick leave. Accumulated sick leave is not paid to an employee upon termination, except upon retirement. At that time, police and fire employees receive \$25 per day for accumulated sick leave, while all other employees receive \$15 per day for the first 170 days and \$20 per day for each day over 170 days. Employees that have up to twelve years of experience and voluntarily resign receive \$10 per day for accumulated sick leave up to a maximum of 50 days.

Deferred Revenues

Deferred revenues are those where asset recognition criteria have been met, but revenue recognition criteria have not been met. Such amounts are measurable but are not available. Deferred revenue may also result from revenues being collected in advance of the fiscal year to which they apply or in advance of their legal due date.

Net Assets

In the government-wide financial statements and the proprietary funds, net assets are classified in the following categories:

Invested in Capital Assets, Net of Related Debt – This category groups all capital assets, including infrastructure, into one component of net assets. Accumulated depreciation and the outstanding balances of debt that are attributable to the acquisition, construction, or improvement of these assets reduce this category.

Restricted Net Assets – This category presents external restrictions imposed by creditors, grantors, contributors, or laws or regulations of other governments and restrictions imposed by law through constitutional provisions or enabling legislation.

Unrestricted Net Assets – This category represents the net assets of the City, which are not restricted for any project or other purpose.

Fund Balance

In the fund financial statements, governmental funds report fund balance in categories based on the level of constraint placed upon the funds. These levels are as follows:

CITY OF BETHLEHEM, PENNSYLVANIA

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Restricted Fund Balance – This category represents funds that are limited in use due to constraints on purpose and circumstances of spending that are legally enforceable by outside parties.

Unassigned Fund Balance – This category represents all other funds not otherwise defined.

The City's policy is to use funds in the order of the most restrictive to the least restrictive.

Accounting Standards

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the GASB. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The City has elected not to follow subsequent private-sector guidance.

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 at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Adoption of Governmental Accounting Standards Board Statement

The City has adopted GASB Statement No. 54, "*Fund Balance Reporting and Governmental Fund Type Definitions*." This Statement's objective is to clarify fund definitions and to enhance the usefulness of fund balance information. As a result of this Statement, the titles and definitions of governmental fund balances have changed.

Pending Changes in Accounting Principles

In November of 2010, the GASB issued Statement No. 61, "*The Financial Reporting Entity: Omnibus*." Statement No. 61 modifies certain requirements for inclusion of component units in the financial reporting entity. The provisions of this Statement are effective for the City's December 31, 2013 financial statements.

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In June of 2011, the GASB issued Statement No. 63, "*Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position.*" Statement No. 63 provides guidance on reporting deferred inflows and outflows of resources, which are distinctly different from assets and liabilities. As a result of reporting these additional elements, the residual balances will be considered as net position, rather than net assets. The provisions of this Statement are effective for the City's December 31, 2012 financial statements.

In April of 2012, the GASB issued Statement No. 65, "*Items Previously Reported as Assets and Liabilities.*" Statement No. 65 reclassifies certain items currently being reported as assets and liabilities as deferred outflows of resources and deferred inflows of resources. The provisions of this Statement are effective for the City's December 31, 2013 financial statements.

In June of 2012, the GASB issued Statements No. 67 and 68, "*Financial Reporting for Pension Plans*" and "*Accounting and Financial Reporting for Pensions.*" These Statements revise and establish reporting requirements for most governments that provide their employees with pension benefits. The provisions of these Statements are effective for the City's December 31, 2014 and 2015 financial statements.

The effect of implementation of these statements has not yet been determined.

2. REPORTING ENTITY

As required by GASB, the City has evaluated all related entities for the possible inclusion in the financial reporting entity.

The following component unit has been included in the financial reporting entity as a blended component unit:

Bethlehem Authority

The Bethlehem Authority owns the water supply and distribution systems that service the City and nearby communities while serving as a financing authority for these systems. The City operates these systems. The Bethlehem Authority is governed by five board members who are appointed by the Mayor and approved by City Council. The water supply and distribution systems were acquired through the proceeds of water revenue bonds which are guaranteed by the City. Operations are financed through user-based charges. Repayment of the bonds is financed through a lease between the City and the Bethlehem Authority. The City leases the systems for a fixed rental fee. The Bethlehem

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

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Authority does not issue separate audited financial statements.

The following component units have been included in the financial reporting entity as discretely-presented component units:

Bethlehem Area Public Library

The Bethlehem Area Public Library (Library) provides library services to the City and nearby communities. The Library is governed by thirteen directors, seven of whom are appointed by City Council on the recommendation of the President of City Council. The remaining members are appointed by the governing boards of the municipalities of Fountain Hill, Hanover Township (Northampton County), Lower Saucon Township, Borough of Freemansburg, and Bethlehem Township. The City supports the Library. The City's 2011 appropriation to the Library represented 38% of the Library's General Fund revenue. Title to the assets of the Library rests with the City directly or indirectly through the Board of Directors. Separate financial statements were issued by the Library and can be obtained by contacting the Library.

Bethlehem Parking Authority

The Bethlehem Parking Authority (Parking Authority) acquires, constructs, and equips parking facilities in the City. The Parking Authority is governed by five board members, all appointed by the Mayor and approved by City Council. Also, the City may require the Parking Authority to transfer surpluses to the City. Separate financial statements were issued by the Parking Authority and can be obtained by contacting the Authority.

Bethlehem Redevelopment Authority

The Bethlehem Redevelopment Authority (Redevelopment Authority) provides community development services on behalf of the City. The largest project is among the City, the Redevelopment Authority, and the Department of Housing and Urban Development (HUD) for Section 108 Loan Guarantee Assistance to finance the Bethlehem Works Project. The Redevelopment Authority is governed by five board members who are appointed by the Mayor and approved by City Council. Operations are financed through the appropriations from the City and tax incremental financing from the City, the County of Northampton, and the Bethlehem Area School District. Repayment of the HUD Loan Guarantee Assistance is guaranteed by the City. Separate financial statements were issued by the Redevelopment Authority and can be obtained by contacting the Redevelopment Authority.

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

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3. DEPOSITS AND INVESTMENTS

The City follows the third class city code for investment of City funds. Authorized types of investments for City funds shall be:

- a. United States Treasury bills.
 - b. Short-term obligations of the United States government or its agencies or instrumentalities.
 - c. Deposits in savings accounts or time deposits, other than certificates of deposit, or share accounts of institutions insured by the Federal Deposit Insurance Corporation or the Federal Savings and Loan Insurance Corporation or the National Credit Union Share Insurance Fund or the Pennsylvania Deposit Insurance Corporation or the Pennsylvania Savings Association Insurance Corporation to the extent that such accounts are so insured, and, for any amounts above the insured maximum, provided that approved collateral as provided by law therefore shall be pledged by the depository.
 - d. Obligations of the United States of America or any of its agencies or instrumentalities backed by the full faith and credit of the United States of America, the Commonwealth of Pennsylvania or any of its agencies or instrumentalities backed by the full faith and credit of the Commonwealth, or of any political subdivision of the Commonwealth of Pennsylvania or any of its agencies or instrumentalities backed by the full faith and credit of the political subdivision.
 - e. Shares of an investment company registered under the Investment Company Act of 1940, whose shares are registered under the Securities Act of 1933, provided that the only investments of that company are in the authorized investments for city funds listed.
 - f. Certificates of deposit purchased from institutions insured by the Federal Deposit Insurance Corporation or the Federal Savings and Loan Insurance Corporation or the National Credit Union Share Insurance Fund or the Pennsylvania Deposit Insurance Corporation or the Pennsylvania Savings Association Insurance Corporation to the extent that such accounts are so insured, however, for any amounts above the insured maximum, such certificates of deposit shall be collateralized by a pledge or assignment of assets of the institution, and such collateral may include loans (including interest in pools of loans) secured by first mortgage liens on real property. Certificates of deposit purchased from
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CITY OF BETHLEHEM, PENNSYLVANIA

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commercial banks shall be limited to an amount equal to twenty percent of a bank's total capital and surplus. Certificates of deposit purchased from savings and loan associations or savings banks shall be limited to an amount equal to twenty percent of an institution's assets minus liabilities.

- g. Any investment authorized by 20 Pa. C.S. Ch. 73 (relating to fiduciaries' investments) shall be an authorized investment for any pension or retirement fund.

In making investment of City funds, the Council shall have authority to permit assets pledged as collateral under subsection (d)(3), to be pooled in accordance with the Act of August 6, 1971 (P.L. 281, No. 72), relating to pledges of assets to secure deposits of public funds.

Investments of the Proprietary and Internal Service Funds primarily represent debt sinking funds, escrow deposits, and other accounts required to be maintained under bond or trust indentures. These investments are held by fiscal agents and managed in accordance with the terms of the respective indentures. Other unrestricted investments of the Proprietary Funds are held by fiscal agents and are managed under the direction of City management. Investments of the Employee Benefit Trust Fund are held by a fiscal agent under trust agreements that authorize the trustee to invest in any form of property, at its discretion, without restriction to investments authorized for fiduciaries, provided that the investments of the trust shall be kept separate and apart from other City funds. Investments of the Library are managed by the board and management of the Library, without restriction as to type of investment.

A. Deposits

Custodial Credit Risk. Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. The City does not have a deposit policy for custodial credit risk. As of December 31, 2011, the City's book balance was \$11,484,162 and the bank balance was \$15,471,098. Of the bank balance, \$2,332,490 was covered by federal depository insurance and \$13,138,608 was collateralized under Act No. 72 of the 1971 Session of the Pennsylvania General Assembly (Act), in which financial institutions were granted the authority to secure deposits of public bodies by pledging a pool of assets, as defined in the Act, to cover all public funds deposited in excess of federal depository insurance limits.

CITY OF BETHLEHEM, PENNSYLVANIA

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Reconciliation to total cash and cash equivalents:	
<u>Governmental activities:</u>	
Unrestricted	\$ 7,370,492
<u>Business-type activities:</u>	
Unrestricted	864,950
Restricted	2,013,754
<u>Fiduciary funds:</u>	
Agency fund	1,234,966
Total cash and cash equivalents	<u>\$ 11,484,162</u>

B. Investments

The fair value of the investments of the City at December 31, 2011 was as follows:

<u>Investments</u>	<u>Fair Value</u>
Money market funds	\$ 10,130,455
External investment pool	3,613,369
U.S. Government obligations	15,411,538
U.S. Government agency obligations	5,610,738
Municipal bonds	557,071
Corporate bonds and notes	17,480,016
Equities	44,194,284
Real estate equity fund	4,090,722
Collective investment trust - fixed income	5,926,762
Collective investment trust - equity	10,208,640
Other investments	8,558,626
Total investments	<u>\$ 125,782,221</u>

CITY OF BETHLEHEM, PENNSYLVANIA

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<u>Reconciliation to total investments</u>	
Governmental activities:	
Unrestricted	\$ 101,413
Business-type activities:	
Unrestricted	16,289
Restricted	12,623,585
Fiduciary funds:	
Employee benefit trust fund	<u>113,040,934</u>
Total investments	<u>\$ 125,782,221</u>

The City uses an external investment pool to ensure safety and maximize efficiency, liquidity, and yield for City funds. These funds are invested in the Pennsylvania Local Government Investment Trust (PLGIT), which separately issues audited financial statements that are available to the public. The fair value of the City's position in the external investment pool is equivalent to the value of the pool shares. The Commonwealth of Pennsylvania provides external regulatory oversight for the external investment pool.

Custodial credit risk. Custodial credit risk is the risk that the counterparty to an investment transaction will fail and the government will not recover the value of the investment or collateral securities that are in possession of an outside party. The City does not have an investment policy for custodial credit risk. Of the City's investments, \$84,250,392 are held by the counterparty's trust department or agent in the City's name, \$8,477,457 are held by the counterparty's trust department or agent not in the name of the city, and the remaining balance of \$33,054,372 is not exposed to custodial credit risk because the investments are not evidenced by securities in book entry or paper form.

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

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Credit risk. The City's money market and fixed income investments had the following level of exposure to credit risk as of December 31, 2011:

	<u>Fair Value</u>	<u>Rating</u>
Money market funds	\$ 10,130,455	AAA
External investment pool	3,613,369	AAA
U.S. Government agency obligations	2,542,822	AAA
U.S. Government agency obligations	3,016,027	AA+
U.S. Government agency obligations	51,889	Unrated
Municipal bonds	346,201	AA+
Municipal bonds	210,870	AA-
Corporate bonds and notes	503,938	AAA
Corporate bonds and notes	400,082	AA+
Corporate bonds and notes	377,471	AA
Corporate bonds and notes	824,203	AA-
Corporate bonds and notes	1,277,001	A+
Corporate bonds and notes	2,565,134	A
Corporate bonds and notes	4,558,174	A-
Corporate bonds and notes	2,938,217	BBB+
Corporate bonds and notes	2,587,604	BBB
Corporate bonds and notes	776,562	BBB-
Corporate bonds and notes	119,518	BB+
Corporate bonds and notes	256,878	BB
Corporate bonds and notes	16,909	B
Corporate bonds and notes	278,325	B-
Collective investment trust - fixed income	5,926,762	B

Concentration of credit risk. The City does have a formal policy that limits the amount the City may invest in any one issuer to five percent for the Employee Benefit Trust Fund, but not for the City's general investments. At December 31, 2011, the City does not hold more than five percent of the City's investments in any one issuer.

CITY OF BETHLEHEM, PENNSYLVANIA

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Interest rate risk. The City does not have a formal policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. The following is a list of the City's money market and fixed income investments and their related average maturities:

	Fair Value	Investment Maturities			
		2012	2013-2017	2018-2022	2023 and beyond
Money market funds	\$10,130,455	\$10,130,455	\$ -	\$ -	\$ -
External investment pool	3,613,369	3,613,369	-	-	-
U.S. Government obligations	15,411,538	5,934,635	7,678,233	1,798,670	-
U.S. Government agency obligations	5,610,738	2,940,178	2,245,303	311,318	113,939
Municipal bonds	557,071	-	557,071	-	-
Corporate bonds and notes	17,480,016	436,010	10,945,793	5,312,285	785,928
Collective investment trust - fixed income	5,926,762	-	5,926,762	-	-
	<u>\$58,729,949</u>	<u>\$23,054,647</u>	<u>\$27,353,162</u>	<u>\$ 7,422,273</u>	<u>\$ 899,867</u>

Other Investments

At December 31, 2011, the City's Employee Benefit Trust Fund was invested in the Graham Global Investment Fund II, Ltd. in the amount of \$3,082,575. This fund was organized to invest directly in the Graham Global Investment Fund (GGIF). GGIF enables investors to invest in various master trading entities through eight different share classes. The objective of each portfolio of the fund is to achieve long-term capital appreciation through professionally managed trading in global fixed income, foreign exchange, and other financial instruments. The City's investment is in the Graham Global Investment Fund II, K4D portfolio, which utilizes multiple computerized trading models that trade in approximately 100 global markets, including interest rates, foreign exchange, global stock indices, and agricultural, metals and energy futures. It has complete flexibility in the instruments and markets in which it invests. The carrying amount of the fund's assets and liabilities approximate their fair value. The shares reported by the City are proportionate to the City's capital contribution.

At December 31, 2011, the City's Employee Benefit Trust Fund was invested in CCA Green, LP Partner's Capital, a limited partnership, in the amount of \$5,476,051. The partnership's primary investments consist of in-force, non-variable universal life insurance policies

CITY OF BETHLEHEM, PENNSYLVANIA

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insuring the lives of individuals who have life expectancy as of the date of purchase of between three and fifteen years at a price greater than the cash surrender value offered by the life insurance companies, but less than the face amount of or the death benefit payable under such policies. The partnership uses a probabilistic method to value life insurance policies. The probabilistic method takes into consideration the mortality curve of the insured, rather than assuming mortality will occur at life expectancy. Utilizing the inputs of age, gender, smoking status, and a mortality table, the probabilistic method uses the insured's life expectancy to determine a mortality curve for the insured. Under the probabilistic method, the sum of the estimated discounted cash flows is the estimated fair market value of the policy. The City's share of the partnership is based on the size of the capital contribution. All income and expenses are allocated based on each Limited Partner's capital balance.

C. Restricted Cash, Cash Equivalents, and Investments

Business-Type Activities

The City has restricted assets for the purpose of retiring long-term debt and related interest payments, and funding for certain capital and other projects.

Component Units

Bethlehem Parking Authority

As a component unit of the City, the Parking Authority follows the third class city code for investment of Parking Authority funds.

Authorized investments for Parking Authority funds are deposits in savings accounts or time deposits, other than certificates of deposit, or share accounts of institutions insured by the Federal Deposit Insurance Corporation or the Federal Savings and Loan Insurance Corporation or the National Credit Union Share Insurance Fund or the Pennsylvania Deposit Insurance Corporation or the Pennsylvania Savings Association Insurance Corporation to the extent that such accounts are so insured, and, for any amounts above the insured maximum, provided that approved collateral as provided by law therefore shall be pledged by the depository.

A. Deposits

Custodial Credit Risk – Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. The Parking Authority does not have a deposit policy for custodial credit risk. As of December 31, 2011, the Parking Authority's book balance was \$241,911 and the bank balance was \$259,006. Of the bank balance at December 31, 2011, \$253,519 was covered by federal depository insurance and \$5,487 was collateralized under the

CITY OF BETHLEHEM, PENNSYLVANIA

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Act, in which financial institutions were granted the authority to secure deposits of public bodies by pledging a pool of assets, as defined in the Act, to cover all public funds deposited in excess of federal depository insurance limits.

B. Investments

The Parking Authority uses an external investment pool to ensure safety and maximize efficiency, liquidity, and yield for Parking Authority funds. These funds are invested in the Pennsylvania Treasurer's INVEST Program for Local Governments and Nonprofits (INVEST), which separately issues audited financial statements that are available to the public.

At December 31, 2011, the Parking Authority's investments in the external investment pool were \$1,213.

The fair value of the Parking Authority's position in the external investment pool is equivalent to the value of the pool shares. The Commonwealth of Pennsylvania provides external regulatory oversight of the pool.

Credit risk – The Parking Authority does not have a formal policy that would limit its investment choices with regard to credit risk. At December 31, 2011, the external investment pool is rated AAAm by Standard & Poor's.

Interest rate risk – The Parking Authority does not have a formal policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. At December 31, 2011, the investments of the Parking Authority have an average weighted maturity of less than one year.

Bethlehem Area Public Library

The deposit and investment policy of the Library adheres to prudent business practice.

A. Deposits

Custodial Credit Risk - Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. The Library does not have a deposit policy for custodial credit risk. As of December 31, 2011, the Library's book balance was \$627,860 and the bank balance was \$799,598. Of the bank balance, \$250,000 was covered by federal depository insurance and \$549,598 was collateralized under the Act, in which financial institutions were granted the authority to secure deposits of public bodies by pledging a pool of assets, as defined in the Act, to cover all public funds deposited in excess of federal depository insurance limits.

CITY OF BETHLEHEM, PENNSYLVANIA

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B. Investments

The fair value of the investments of the Library at December 31, 2011 was as follows:

<u>Investments</u>	<u>Fair Value</u>
Money market funds	\$ 52,689
U.S. Government agency obligations	86,923
Municipal bonds	26,359
Corporate bonds	219,588
Equities	936,583
Total investments	<u>\$ 1,322,142</u>

Custodial credit risk – Custodial credit risk is the risk that the counterparty to an investment transaction will fail and the government will not recover the value of the investment or collateral securities that are in possession of an outside party. The Library does not have an investment policy for custodial credit risk. The Library's investment in U.S. Government agency obligations, municipal bonds, corporate bonds, and equities are held by the financial institution, not in the Library's name. The Library's remaining investment in money market funds is not exposed to custodial credit risk because they are not evidenced by securities in book entry or paper form.

Credit risk – The Library does not have a formal policy that would limit its investment choices with regard to credit risk. The Library's investments had the following level of exposure to credit risk as of December 31, 2011:

	<u>Fair Value</u>	<u>Rating</u>
Money market funds	\$ 52,689	AAA
Municipal bonds	26,359	AA-
Corporate bonds	30,938	AAA
Corporate bonds	15,597	AA-
Corporate bonds	56,833	A+
Corporate bonds	35,143	A
Corporate bonds	28,679	A-
Corporate bonds	52,398	BBB+

CITY OF BETHLEHEM, PENNSYLVANIA

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Concentration of credit risk – The Library places no limit on the amount the Library may invest in any one issuer. At December 31, 2011, no investments were held that were more than five percent of the Library's investments.

Interest rate risk – The Library does not have a formal policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. The Library's money market funds had a weighted average maturity of less than one year. The following is a list of the Library's fixed income investments and their related average maturities:

	Fair Value	Investment Maturities 2013-2017
U.S. Government agency obligations	\$ 86,923	\$ 86,923
Municipal bonds	26,359	26,359
Corporate bonds	219,588	219,588
Total	<u>\$ 332,870</u>	<u>\$ 332,870</u>

Redevelopment Authority

A. Deposits

Bank of America secures the deposits of public funds under the Act.

Under this system, it is the Bank's legal responsibility to provide collateral to secure public fund deposits against the claims of any third party. All collateral is pooled and held with the Bank of New York.

CITY OF BETHLEHEM, PENNSYLVANIA

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4. CAPITAL ASSETS

A summary of changes in capital assets follows:

	January 1, 2011	Additions and Transfers In	Disposals and Transfers Out	December 31, 2011
Governmental activities:				
Capital assets not being depreciated:				
Land	\$ 6,757,780	\$ -	\$ -	\$ 6,757,780
Construction in progress	3,459,536	1,657,212	(1,584,043)	3,532,705
Total capital assets not being depreciated	10,217,316	1,657,212	(1,584,043)	10,290,485
Capital assets being depreciated:				
Buildings and related improvements	24,547,575	2,165,958	(2,898)	26,710,635
Improvements other than buildings	39,653,629	1,436,728	-	41,090,357
Furniture, machinery, and equipment	38,617,799	1,330,652	(3,704,302)	36,244,149
Infrastructure	20,312,501	3,936,381	-	24,248,882
Total capital assets being depreciated	123,131,504	8,869,719	(3,707,200)	128,294,023
Less accumulated depreciation for:				
Buildings and related improvements	(20,687,338)	(745,953)	2,898	(21,430,393)
Improvements other than buildings	(23,672,758)	(1,783,045)	-	(25,455,803)
Furniture, machinery, and equipment	(26,576,899)	(2,429,714)	3,559,271	(25,447,342)
Infrastructure	(6,954,897)	(1,388,833)	-	(8,343,730)
Total accumulated depreciation	(77,891,892)	(6,347,545)	3,562,169	(80,677,268)
Total capital assets being depreciated, net	45,239,612	2,522,174	(145,031)	47,616,755
Governmental activities capital assets, net	\$ 55,456,928	\$ 4,179,386	\$ (1,729,074)	\$ 57,907,240

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	January 1, 2011	Additions and Transfers In	Disposals and Transfers Out	December 31, 2011
Business-type activities:				
Capital assets not being depreciated:				
Land	\$ 1,980,542	\$ -	\$ -	\$ 1,980,542
Construction in progress	2,290,619	1,790,701	(1,928,259)	2,153,061
Total capital assets not being depreciated	4,271,161	1,790,701	(1,928,259)	4,133,603
Capital assets being depreciated:				
Land improvements	1,100,349	-	-	1,100,349
Building and fixtures	13,382,452	35,558	-	13,418,010
Improvements other than buildings	188,077,689	4,043,069	(4,977)	192,115,781
Furniture, machinery, and equipment	4,843,699	220,741	(12,039)	5,052,401
Vehicles	4,003,277	128,912	(17,379)	4,114,810
Office equipment	759,915	-	(417,329)	342,586
Total capital assets being depreciated	212,167,381	4,428,280	(451,724)	216,143,937
Less accumulated depreciation for:				
Land improvements	(876,454)	(29,863)	-	(906,317)
Building and fixtures	(11,770,614)	(217,298)	-	(11,987,912)
Improvements other than buildings	(94,845,532)	(5,789,506)	-	(100,635,038)
Furniture, machinery, and equipment	(4,375,819)	(179,622)	-	(4,555,441)
Vehicles	(3,294,992)	(187,062)	17,381	(3,464,673)
Office equipment	(729,856)	(8,900)	420,201	(318,555)
Total accumulated depreciation	(115,893,267)	(6,412,251)	437,582	(121,867,936)
Total capital assets being depreciated, net	96,274,114	(1,983,971)	(14,142)	94,276,001
Business-type activities capital assets, net	\$ 100,545,275	\$ (193,270)	\$ (1,942,401)	\$ 98,409,604

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Depreciation expense was charged to governmental activities as follows:

General government	\$ 4,867
Administration	117,440
Community development	311,579
Parks and public property	1,083,578
Public works	3,095,062
Police	1,206,848
Fire	462,898
Library	65,273
	<u>65,273</u>
	<u>\$ 6,347,545</u>

Depreciation expense was charged to business-type activities as follows:

Water Fund	\$ 4,701,835
Sewer Fund	1,623,392
Municipal Golf Fund	87,024
	<u>87,024</u>
	<u>\$ 6,412,251</u>

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

	January 1, 2011	Additions and Transfers In	Deletions and Transfers Out	December 31, 2011
Parking Authority:				
Capital assets, not being depreciated:				
Land	\$ 554,380	\$ -	\$ -	\$ 554,380
Construction in progress	3,914,583	270,841	(3,914,583)	270,841
Total capital assets, not being depreciated	4,468,963	270,841	(3,914,583)	825,221
Capital assets, being depreciated:				
Parking garages	22,697,721	3,916,333	-	26,614,054
Furniture and fixtures	542,303	29,430	(11,441)	560,292
Automobiles	269,593	-	-	269,593
Leasehold and parking lot improvements	21,860	-	-	21,860
Total capital assets, being depreciated	23,531,477	3,945,763	(11,441)	27,465,799
Less accumulated depreciation	(9,995,536)	(911,841)	11,441	(10,895,936)
Total capital assets, being depreciated, net	13,535,941	3,033,922	-	16,569,863
Total capital assets, net	<u>\$ 18,004,904</u>	<u>\$ 3,304,763</u>	<u>\$ (3,914,583)</u>	<u>\$ 17,395,084</u>
	January 1, 2011	Additions and Transfers In	Deletions and Transfers Out	December 31, 2011
Library:				
Capital assets, being depreciated:				
Furniture, machinery, and equipment	\$ 1,425,710	\$ 71,994	\$ -	\$ 1,497,704
Less accumulated depreciation	(1,331,149)	(50,168)	-	(1,381,317)
Total capital assets being depreciated, net	<u>\$ 94,561</u>	<u>\$ 21,826</u>	<u>\$ -</u>	<u>\$ 116,387</u>

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

5. INTERFUND RECEIVABLE AND PAYABLES BALANCES

A summary of the total amounts due from and due to other funds, by fund, at December 31, 2011 is as follows:

	<u>Due From Other Funds</u>	<u>Due To Other Funds</u>
Governmental funds:		
General Fund	\$ 1,237,236	\$ 6,720,963
Non-Utility Capital Improvements Fund	2,697,824	65,570
Other Non-Major Governmental Funds	549,080	-
Proprietary funds:		
Water Fund	188,130	1,430,496
Sewer Fund	300,000	133,130
Other Non-Major Enterprise Fund	10,570	113,100
Internal Service Fund	179	-
Agency funds	<u>3,480,240</u>	<u>-</u>
Total	<u>\$ 8,463,259</u>	<u>\$ 8,463,259</u>

Interfund balances are primarily for reimbursement of expenditures paid on behalf of another fund and interfund loans for cash flow purposes.

6. INTERFUND TRANSFERS

Interfund transfers for the year ended December 31, 2011 are as follows:

	<u>Transfers In</u>	<u>Transfers Out</u>
Governmental funds:		
General Fund	\$ 2,930,189	\$ 7,431,545
Non-Utility Capital Improvements Fund	720,752	1,893,781
Other Non-Major Governmental Funds	8,342,518	387,209
Proprietary funds:		
Water Fund	-	300,000
Sewer Fund	-	1,980,924
Total	<u>\$ 11,993,459</u>	<u>\$ 11,993,459</u>

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Transfers are used to (1) reimburse funds for expenses incurred on behalf of other funds, and (2) move receipts restricted to debt service from the funds collecting the receipts as debt service payments become due.

7. LONG-TERM OBLIGATIONS

Bonds and Notes Payable

A summary of long-term bonds payable of the City at December 31, 2011 and principal and interest maturities through the next five years and thereafter, respectively, are as follows:

	Governmental Activities	Business-type Activities			Total
		Water Fund	Sewer Fund	Municipal Golf Fund	
Outstanding at beginning of year	\$ 74,271,000	\$ 109,197,303	\$ 4,901,314	\$ 386,000	\$ 188,755,617
Issuance of debt	32,470,000	1,330,812	578,756	-	34,379,568
Repayment of debt	(16,380,000)	(5,177,795)	(445,000)	(58,000)	(22,060,795)
	90,361,000	105,350,320	5,035,070	328,000	201,074,390
Plus unamortized bond premium	50,915	1,467,200	16,078	-	1,534,193
Less unamortized bond discount	(351,571)	(77,353)	-	-	(428,924)
Less unamortized deferred costs of refunding	(121,458)	(356,914)	(102,845)	-	(581,217)
Outstanding at end of year	<u>\$ 89,938,886</u>	<u>\$ 106,383,253</u>	<u>\$ 4,948,303</u>	<u>\$ 328,000</u>	<u>\$ 201,598,442</u>

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

	Discretely Presented Component Units	
	Parking Authority	Redevelopment Authority
	Outstanding at beginning of year	\$ 13,329,125
Issuance of new debt	370,053	18,715,395
Repayment of debt	(554,269)	(4,676,622)
	13,144,909	20,234,871
Less unamortized deferred costs of refunding	(710,945)	-
Outstanding at end of year	\$ 12,433,964	\$ 20,234,871

Year	Governmental Activities			Water Fund		
	Principal	Interest	Total	Principal	Interest	Total
2012	\$ 3,090,000	\$ 4,851,832	\$ 7,941,832	\$ 5,741,248	\$ 3,335,303	\$ 9,076,551
2013	4,143,000	4,718,400	8,861,400	6,014,872	2,925,901	8,940,773
2014	4,328,000	4,535,026	8,863,026	7,658,142	2,679,256	10,337,398
2015	4,519,000	4,342,995	8,861,995	6,597,827	2,367,537	8,965,364
2016	4,470,000	4,137,917	8,607,917	6,911,238	2,096,250	9,007,488
2017-2021	19,590,000	17,946,136	37,536,136	37,046,952	7,995,684	45,042,636
2022-2026	19,846,000	12,896,474	32,742,474	26,929,442	19,968,843	46,898,285
2027-2031	22,750,000	6,626,961	29,376,961	8,450,599	8,124,426	16,575,025
2032-2034	7,625,000	747,495	8,372,495	-	-	-
Totals	\$ 90,361,000	\$ 60,803,236	\$ 151,164,236	\$ 105,350,320	\$ 49,493,200	\$ 154,843,520

Year	Sewer Fund			Municipal Golf Fund		
	Principal	Interest	Total	Principal	Interest	Total
2012	\$ 2,265,070	\$ 159,338	\$ 2,424,408	\$ 60,000	\$ 12,988	\$ 72,988
2013	460,000	78,022	538,022	63,000	10,613	73,613
2014	480,000	67,398	547,398	66,000	8,118	74,118
2015	485,000	56,197	541,197	68,000	5,505	73,505
2016	495,000	43,835	538,835	71,000	2,812	73,812
2017-2020	850,000	63,555	913,555	-	-	-
Totals	\$ 5,035,070	\$ 468,345	\$ 5,503,415	\$ 328,000	\$ 40,036	\$ 368,036

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Year	Parking Authority			Year	Redevelopment Authority
	Principal	Interest	Total		Principal
2012	\$ 2,339,081	\$ 691,659	\$ 3,030,740	2012	\$ 3,754,476
2013	563,274	487,652	1,050,926	2013	2,235,000
2014	586,474	464,847	1,051,321	2014	2,310,000
2015	599,683	434,341	1,034,024	2015	2,390,000
2016	623,397	409,492	1,032,889	2016	2,475,000
2017-2021	3,192,000	1,627,726	4,819,726	2017-2018	7,070,395
2022-2026	2,704,000	985,211	3,689,211		
2027-2030	2,537,000	295,628	2,832,628		
Totals	<u>\$ 13,144,909</u>	<u>\$ 5,396,556</u>	<u>\$ 18,541,465</u>		<u>\$ 20,234,871</u>

Total principal and interest for the primary government due through maturity is \$311,879,207.

Under the terms of its respective debt agreements, the City is required to maintain certain balances in restricted trust accounts, to make timely payments to the trustee or to a sinking fund for principal and interest, and to insure and maintain assets acquired with the proceeds of the debt.

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Long-term obligations payable at December 31, 2011 are as follows:

Governmental Activities:	Current Portion	Balance at December 31, 2011
Bethlehem Authority Federally Taxable Lease Revenue Bonds, Series of 2001, due in annual installments of \$345,000 to \$825,000 through December 1, 2026; interest rates vary from 5.85% to 6.60%.	\$ 345,000	\$ 8,255,000
General Obligation Bonds, Series B of 2004, due in annual installments of \$1,390,000 to \$1,735,000 through November 1, 2034; interest rates vary from 4.10% to 5.70%.	1,390,000	28,050,000
Bethlehem Authority Guaranteed Lease Revenue Bonds, Series of 2004, due in annual installments of \$745,000 to \$840,000 through October 1, 2015; interest rates vary from 4.00% to 4.40%.	745,000	3,165,000
General Obligation Bonds, Series A of 2005, due in annual installments of \$15,000 to \$285,000 through October 2020; interest rates vary from 3.25% to 4.00%.	15,000	1,815,000
General Obligation Bonds, Series B of 2005, due in one installment \$395,000 in October 2016; interest rates vary from 3.40% to 3.80%.	-	395,000
General Obligation Notes, Series of 2007, due in annual installments of \$245,000 to \$356,000 through August 2022; interest rates fixed at 3.65% through August 2017.	245,000	4,498,000
General Obligation Notes, Series of 2008, due in annual installments of \$705,000 to \$382,000 through August 2016; interest rates of 3.96%.	-	1,798,000

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

	<u>Current Portion</u>	<u>Balance at December 31, 2011</u>
General Obligation Bonds, Series of 2010, due in annual installments of \$335,000 to \$360,000 through August 2024; interest rates vary from 1.50% to 4.00%.	335,000	3,875,000
General Obligation Bonds, Series C of 2010, due in annual installments of \$5,000 to \$825,000 through August 2020; interest rate of 3.55%.	5,000	6,040,000
Bethlehem Authority Guaranteed Lease Revenue Bonds, Series A of 2011, due in annual installments of \$5,000 to \$1,135,000 through December 1, 2028; interest rates vary from 5.125% to 6.125%.	5,000	17,805,000
General Obligation Refunding Bonds, Series A of 2011, due in annual installments of \$1,035,000 to \$1,505,000 through December 2032; interest rate of 6.50%.	-	7,860,000
General Obligation Refunding Notes, Series B of 2011, due in annual installments of \$5,000 to \$1,195,000 through December 2032; interest rate of 6.50%.	5,000	6,805,000
Total Governmental Activities	<u>\$ 3,090,000</u>	<u>\$ 90,361,000</u>

Governmental activities debt is expected to be liquidated by the General Fund.

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Business-Type Activities: Water Fund:	Current Portion	Balance at December 31, 2011
Bethlehem Authority Guaranteed Water Revenue Note, Series of 1997, due in annual installments of \$620,000 to \$1,260,000 through August 1, 2027; interest rates are variable. The interest rate at December 31, 2011 was 1.94% (see Note 12).	\$ 620,000	\$ 14,470,000
Bethlehem Authority Capital Appreciation Bonds, Series of 1998, due in annual installments of \$425,000 to \$6,050,000 from 2018 to 2028. The interest rates vary from 5.25% to 5.35%.	-	25,741,011
Bethlehem Authority Guaranteed Water Revenue Bonds, Series of 2004, due in annual installments of \$3,530,000 to \$5,410,000 through November 15, 2021; interest rates vary from 3.00% to 4.60%	3,530,000	44,265,000
1998 Pennvest loan payable in monthly installments of \$116,147, including interest at 3.20% through 2018.	1,158,248	7,885,886
General Obligation Note, Series of 2007, due in annual installments of \$48,000 to \$69,000 through August 2022; interest rates fixed at 3.65% through August 2017.	48,000	641,000
Bethlehem Authority Guaranteed Water Revenue Bonds, Series of 2010, due in annual installments of \$385,000 to \$940,000 through November 15, 2028; interest rates vary from 2.00% to 4.25%.	385,000	10,985,000

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Business-Type Activities:	Current	Balance at
Water Fund:	<u>Portion</u>	<u>December 31, 2011</u>
<p>General Obligation Note, Series A of 2010, is a draw down construction loan. The outstanding principal is due in full on or before December 15, 2014. Interest on the outstanding principal is due quarterly at 3.92%. At December 31, 2011, the City had drawn down \$1,362,423 of the \$8,100,000 available under the note.</p>	-	1,362,423
<p style="padding-left: 40px;">Total Water Fund</p>	<u>5,741,248</u>	<u>105,350,320</u>
Sewer Fund:		
<p>General Obligation Bonds, Series A of 2005, due in annual installments of \$90,000 to \$125,000 through October 2020; interest rates vary from 3.25% to 4.00%.</p>	\$ 90,000	\$ 960,000
<p>General Obligation Bonds, Series of 2010, due in annual installments of \$365,000 to \$140,000 through August 1, 2018; interest rates vary from 1.50% to 3.50%.</p>	365,000	2,265,000
<p>General Obligation Note, Series B of 2010, is a draw down construction loan. The outstanding principal is due in full on or before December 15, 2012. Interest on the outstanding principal is due quarterly at 3.92%. At December 31, 2011, the City had drawn down \$1,810,070 of the \$2,600,000 available under the note.</p>	<u>1,810,070</u>	<u>1,810,070</u>
<p style="padding-left: 40px;">Total Sewer Fund</p>	<u>2,265,070</u>	<u>5,035,070</u>

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

	<u>Current Portion</u>	<u>Balance at December 31, 2011</u>
Municipal Golf Fund:		
General Obligation Note, Series of 2008, due in annual installments of \$60,000 to \$71,000 through August 2016; interest rate of 3.96%.	60,000	328,000
Total Business-Type Activities	<u>\$ 8,066,318</u>	<u>\$ 110,713,390</u>

Component Units:

Parking Authority:

	<u>Current Portion</u>	<u>Balance at December 31, 2011</u>
General Obligation Bond Series C of 2003, due in annual installments of \$265,000 in October 2012 to \$575,000 in October 2030, interest rates range from 3.30% to 4.75%.	\$ 265,000	\$ 7,520,000
Parking Revenue Note Series of 2004, due in annual installments of \$205,000 to \$280,000, maturing in August 2020. Interest-only payments due semiannually through February 2008 at a rate of 3.5%, increasing to 4.41% beginning August 2011; secured by future revenues of the Authority.	205,000	2,160,000
Term Note of 2009, due in annual installments of \$64,000 in December 2012 to \$136,000 in December 2029, interest rates are fixed at 4.8% for a period of sixty months; thereafter, the interest rate is at a floating rate equal to 65% of the Wall Street Journal Prime Rate plus 225 basis points, but in no event will the interest rate be more than 6%, secured by real property and future revenues of the Authority.	64,000	1,638,000

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

	<u>Current Portion</u>	<u>Balance at December 31, 2011</u>
Promissory Note of 2009. The interest rate on the note is fixed at 4.8%. Beginning on June 1, 2010, the Authority is to make semi-annual payments of interest only on June 1 and December 1 or each calendar year throughout the term of the loan. One final payment of all outstanding principal, accrued interest, and costs is due on or before December 1, 2012. Within thirty days of receipt by the Authority of any Redevelopment Assistance Capital Program grant proceeds from the Commonwealth of Pennsylvania pursuant to Contract No. ME 300-742 that reimburses the Authority for project costs, the Authority will pay to the lender (of this note) the grant proceeds.	1,550,000	1,550,000
Loan payable, \$500 per month, including interest at 3.74%, through December 2016, unsecured loan.	5,081	26,909
\$250,000 line-of-credit, expires April 30, 2012, annually renewable, interest floats at the financial institution's prime rate but not less than 4% and not more than 9%, secured by the Authority's business assets.	<u>250,000</u>	<u>250,000</u>
Total Parking Authority	<u>\$ 2,339,081</u>	<u>\$ 13,144,909</u>

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Redevelopment Authority:	<u>Current Portion</u>	<u>Balance at June 30, 2011</u>
Note Payable, due in monthly installments through 2012; interest rate is variable.	\$ 1,519,476	\$ 1,519,476
TIF Bonds, Series of 2010, due in annual installments of \$2,235,000 to \$1,870,395 through December 2018; interest rates fixed at 3.42% through December 2017. The Redevelopment Authority has drawn down \$18,715,395 of the available \$27,600,000 under the bonds.	<u>2,235,000</u>	<u>18,715,395</u>
Total Redevelopment Authority	<u>\$ 3,754,476</u>	<u>\$ 20,234,871</u>

Defeased Debt

On March 31, 2011, the City advance refunded \$3,875,000 aggregate principal amount of a portion of the General Obligation Bonds, Series of 2010. The advance refunding increased the City's total debt service payments by \$5,704,588 through the year 2032 and resulted in an economic loss (difference between the present values of the old and new debt service payments) in the amount of \$447,086.

The City has invested monies in escrow with the Trustee sufficient to pay the outstanding defeased portion of the Series of 2010 to maturity. As of December 31, 2011, \$3,875,000 of Series of 2010 is outstanding.

Swap Payments and Associated Debt

As of December 31, 2011, debt service requirements of the variable-rate debt and net interest rate swap payments (Note 12), assuming current interest rates remain the same for their term, were as follows. As rates vary, variable-rate bond interest payments and net swap payments will vary.

<u>Year</u>	<u>Variable-Rate Bonds</u>		<u>Interest Rate</u>	<u>Total</u>
	<u>Principal</u>	<u>Interest</u>	<u>Swaps, Net</u>	
2012	<u>\$ 4,590,000</u>	<u>\$ 89,046</u>	<u>\$ 173,798</u>	<u>\$ 4,852,844</u>

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Other Changes in Long-Term Debt

The following represents changes in long-term liabilities, other than bond and note issues:

	Balance January 1, 2011	Additions	Reductions	Balance December 31, 2011
Governmental activities:				
Accrued vacation and other compensated absences	\$ 3,939,654	\$ -	\$ (298,064)	\$ 3,641,590
Capital leases	359,175	222,867	(259,888)	322,154
	<u>\$ 4,298,829</u>	<u>\$ 222,867</u>	<u>\$ (557,952)</u>	<u>\$ 3,963,744</u>
Business-type activities:				
Accrued vacation and other compensated absences	\$ 807,533	\$ -	\$ (44,163)	\$ 763,370
Capital leases	82,098	-	(44,801)	37,297
	<u>\$ 889,631</u>	<u>\$ -</u>	<u>\$ (88,964)</u>	<u>\$ 800,667</u>

Capitalized Lease Obligations Payable

The City has agreements for the lease of lighting equipment, other equipment, and vehicles, which are classified as capital leases. As of December 31, 2011, the net book value of the equipment and vehicles held under capital leases and included in capital assets was \$426,758 for governmental activities and \$128,136 for business-type activities.

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

As of December 31, 2011, future minimum payments were as follows:

Year	Governmental Activities	Business-Type Activities
2012	\$ 172,061	\$ 17,653
2013	126,199	15,033
2014	40,389	6,982
Total commitment under capital leases	338,649	39,668
Less amount representing interest	16,495	2,371
Present value of future minimum lease payments	322,154	37,297
Less current portion	162,049	16,095
Long-term portion	\$ 160,105	\$ 21,202

Parking Authority

During December 2011, the Parking Authority entered into a lease agreement that meets the requirements of a capital lease for garage automation equipment. The total cost of the equipment was \$282,856, of which \$14,015 represented equipment purchased from the Authority by a third party. The cost and accumulated depreciation of the lease equipment recorded by the Authority were \$268,841 and \$0, respectively, at December 31, 2011. Amortization of the lease equipment is included in depreciation expense. The future minimum lease payments required are as follows:

Year	Amount
2012	\$ 63,379
2013	63,379
2014	63,379
2015	63,379
2016	58,097
Total minimum lease payments	311,613
Less amount representing interest at 4.39%	31,792
Present value of minimum lease payments	279,821
Less current portion	52,137
Long-term portion	\$ 227,684

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

8. PENSION PLANS

PLAN DESCRIPTIONS

The City has three single-employer defined benefit plans covering Police, Firemen, and certain non-uniformed employees (Officers' and Employees' Plan). The plans provide for retirement, disability, and death benefits to plan members and their beneficiaries. Cost of living adjustments are provided at the discretion of the Police, Firemen, and Officers' and Employees' Retirement Boards. These plans do not issue separate reports. The City also participates in a pension plan administered by the Pennsylvania Municipal Retirement System (PMRS) covering the remainder, and larger group, of non-uniformed employees, and all full-time Library and Parking Authority employees. PMRS is an agent multiple-employer public employee retirement system that acts as a common investment and administrative agent for participating municipal pension plans. PMRS issues a separate Comprehensive Annual Financial Report (CAFR) which may be obtained by writing to Pennsylvania Municipal Retirement System, P. O. Box 1165, Harrisburg, PA 17108-1165 or by calling 1-800-622-7968. The combining information for the plans is as follows:

	Firemen Pension Fund	Police Pension Fund	Officers' and Employees' Pension Fund	Employee Benefit Trust Fund Total
Assets				
Interest and dividends receivable	\$ 149,644	\$ 197,178	\$ 19,953	\$ 366,775
Investments	46,121,319	60,770,667	6,148,948	113,040,934
Total Assets	\$ 46,270,963	\$ 60,967,845	\$ 6,168,901	\$ 113,407,709
Net Assets				
Reserved for employees' retirement benefits	\$ 46,270,963	\$ 60,967,845	\$ 6,168,901	\$ 113,407,709
Total Net Assets	\$ 46,270,963	\$ 60,967,845	\$ 6,168,901	\$ 113,407,709

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

	Firemen Pension Fund	Police Pension Fund	Officers' and Employees' Pension Fund	Employee Benefit Trust Fund Total
Additions:				
Employee contributions	\$ 587,410	\$ 802,032	\$ 5,982	\$ 1,395,424
Employer contributions	1,672,843	2,534,484	455,998	4,663,325
Investment income	1,729,667	2,269,356	232,663	4,231,686
Realized and unrealized losses, net	(652,487)	(862,861)	(77,752)	(1,593,100)
Total additions	3,337,433	4,743,011	616,891	8,697,335
Deductions:				
Benefits paid	3,738,701	4,813,061	1,122,412	9,674,174
Administrative costs	275,107	358,678	37,789	671,574
Total deductions	4,013,808	5,171,739	1,160,201	10,345,748
Change in Net Assets	(676,375)	(428,728)	(543,310)	(1,648,413)
Net Assets:				
Beginning of year	46,947,338	61,396,573	6,712,211	115,056,122
End of year	\$ 46,270,963	\$ 60,967,845	\$ 6,168,901	\$ 113,407,709

The Officers' and Employees' Pension Plan (O&E) was closed for eligibility as of January 1, 1964 and was replaced by the PMRS plan. The O&E plan is still active for those employees and retirees who were participants prior to January 1, 1964 and elected not to transfer to PMRS.

Benefit provisions and their amendments are authorized by the separate Pension Boards for the Police, Firemen, and O&E plans and by Pennsylvania State Act 15 for the PMRS plan. The following table provides information concerning types of covered employees and benefit provision for each of the Plans as of their latest actuarial valuation date, January 1, 2011:

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

	Police	Firemen	Officers' and Employees'	PMRS
	All Full-time Members of the Police Force	All Full-time Members of the Fire Department	Closed 01/01/64	All Full-time Employees Not Previously Covered
Covered Employees				
Active plan members	159	110	2	398
Numbers of retirees and beneficiaries receiving benefits	155	83	57	235
Terminated employees entitled to deferred benefits	-	-	-	10

Contributions

Pennsylvania Act 205 of 1984, the Municipal Pension Plan Funding Standard and Recovery Act of the Commonwealth of Pennsylvania (as amended) (Act 205) requires that annual contributions be based upon the Minimum Municipal Obligation (MMO), which is based on the plans' biennial actuarial valuation. According to Act 205, actuarial valuations may be made biennially and the most recent valuation for all of the City's plans was completed as of January 1, 2011. The MMO includes the normal cost, estimated administrative expenses and an amortization of the unfunded actuarial accrued liability, less estimated member contributions, and a credit equal to 10 percent of the excess (if any) of the actuarial value of assets over the actuarial accrued liability. The state provides an allocation of funds that must be used for pension funding. Any financial requirements established by the MMO which exceeds state and member contributions must be funded by the employer.

Police and firemen are required to contribute 7% and 8% of covered payroll, respectively, plus \$1 per month to their respective pension plans. The O&E plan requires contributions of 3% of covered payroll for single coverage, 3½% for joint coverage, and 5% for dual coverage from participants. These contributions are governed by the Plans' governing ordinances and collective bargaining agreements. 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 investment earnings.

Annual Pension Cost and Net Pension (Asset) Obligation – For the year ended December 31, 2011, the City made its annual required contribution of \$2,534,484, \$1,672,843, and \$455,998 for the City's Police, Firemen, and O&E Defined Benefit Pension Plans,

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

respectively. The City's net pension (asset) obligation for the City's Police, Firemen, and O&E Defined Benefit Pension Plans at December 31, 2011 is not significant.

The pension expenditures/expense are allocated between governmental and business-type activities based on the proportion of employees, active and retired, representing participants in each of these Plans.

The January 1, 2011 actuarial valuations utilized the entry age normal cost method. The actuarial assumptions included (a) investment rate of return of 7.5% for the three City Plans, and (b) projected salary increases of 4.5% per year, including an inflation component of 3.5%, for the City Plans. The actuarial value of assets was based on the investment gain or loss being recognized over a five-year period. In no event is the actuarial value of assets allowed to be greater than 120% or less than 80% of market value. The Police and Firemen unfunded actuarial accrued liabilities (UAAL) are being amortized over 18 and 16 years, respectively, utilizing the level dollar closed method and the O&E's UAAL is being amortized over two years utilizing the level dollar closed method.

The PMRS plan requires contributions of 7.5% from plan participants. The January 1, 2011 actuarial valuation utilized the entry age normal cost method. The actuarial assumptions included (a) investment rate of return of 6.0%, and (b) projected salary increases are based on a salary range of 3.7% - 6.4%. The actuarial value of assets was based on market value as determined by the trustee. The PMRS unfunded actuarial accrued liability is being amortized over nine years, utilizing the annual funding adjustment equal to 10% of negative UAAL. For the year ended December 31, 2011, the City made the \$3,040,895 annual required contribution for the PMRS plan.

Funded Status and Schedule of Funding Progress (in thousands):

The schedules of funding progress, presented as required supplementary information following the notes to financial statements, present multi-year trend information about whether the actuarial value of plan assets are increasing or decreasing over time relative to the actuarial accrued liability for benefits.

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

(in thousands)							UAAL as a
Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	Percentage of Covered Payroll (b-a/c)	
Police:							
1/1/2011	\$ 63,718	\$ 83,930	\$ 20,212	76%	\$ 11,565	175%	
Firemen:							
1/1/2011	\$ 48,627	\$ 62,441	\$ 13,814	78%	\$ 7,318	189%	
Officers and Employees:							
1/1/2011	\$ 7,121	\$ 8,531	\$ 1,410	83%	\$ 120	1175%	
PMRS:							
1/1/2011	\$ 88,255	\$ 111,163	\$ 22,908	79%	\$ 22,034	104%	

Investments That Represent Five Percent or More of Plan Net Assets

The City does have a formal policy that limits the amount the City may invest in any one issuer to five percent for the Plan. At December 31, 2011, the City does not hold more than five percent of the Plan's investments in any one issuer.

The negative events in the credit market, as well as the general economic conditions in the United States and worldwide have caused a significant decrease in investment values, either directly invested or tied to the equity markets. These declines, at present, are expected to be temporary and not permanent declines; however, equity market recovery, if it occurs, may take some time. The major resulting impact of the equity markets' decline on the City will be in the form of increased annual required contributions and increased pension expense with respect to its pension plans.

9. POST-EMPLOYMENT BENEFITS OTHER THAN PENSIONS

Plan Descriptions

In addition to pension benefits described in Note 8, the City provides certain post-retirement healthcare benefits to its retirees through one single-employer, defined benefit other post-retirement benefit (OPEB) plan. However, within this one plan, there are three groups of employees with different types of benefits. The plan does not issue a separate report.

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Police:

Article XI of the Collective Bargaining Agreement between the City and the Fraternal Order of Police, Star Lodge #20, effective January 1, 2011, establishes retirees' eligibility for post-retirement medical benefits. Article VII Section D. of the personnel manual establishes retirees' eligibility for post-retirement life-insurance benefits.

Eligibility: Any police officer who retires after completion of 20 years of service. Any employee who retires under the disability provision may begin coverage no earlier than age 41, regardless of service.

Any employee hired on or after January 1, 2012 shall not be entitled to any City-funded retiree healthcare upon retirement.

Benefits: The City will provide medical and prescription drug coverage for the retiree and spouse until Medicare eligibility. The City's maximum monthly contribution for health insurance coverage for each retiree is \$340 in 2011. If the retiree dies, his or her spouse will be covered and the City will contribute to coverage for the spouse until Medicare eligibility, unless the spouse remarries or has a job in which health insurance coverage is normally granted. If the retiree reaches Medicare eligibility prior to his or her spouse, the spouse may continue coverage and the City will contribute to coverage for the spouse until Medicare eligibility.

The City will provide each retiree \$1,500 of post-retirement life insurance coverage. The City will also make available an additional \$1,000 of coverage at the employee's expense, if the employee paid for an additional \$30,000 of life insurance coverage while an active employee.

Firefighters:

Article X of the Collective Bargaining Agreement between the City and the Local 735 of the International Association of Firefighters (AFL-CIO), effective January 1, 2011, establishes retirees' eligibility for post-retirement medical benefits. Article VII Section 4 of the personnel manual establishes retirees' eligibility for post-retirement life-insurance benefits.

Eligibility: Any firefighter who retires after completion of 20 years of service and after attainment of age 38. Any employee who retires under the disability provision may begin coverage no earlier than age 38, regardless of service.

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Any firefighter hired on or after January 1, 2012 shall not be entitled to any City-funded retiree healthcare upon retirement.

Benefits: The City will provide medical and prescription drug coverage for the retiree and spouse until Medicare eligibility. The City's maximum monthly contribution for health insurance coverage for each retiree is \$340 in 2011. If the retiree dies, his or her spouse will be covered and the City will contribute to coverage for the spouse until Medicare eligibility, unless the spouse remarries or has a job in which health insurance coverage is normally granted. If the retiree reaches Medicare eligibility prior to his or her spouse, the spouse may continue coverage and the City will contribute to coverage for the spouse until Medicare eligibility. An employee who retires prior to age 38 shall be eligible to enter the plan at the contribution rate equal to the negotiated rate for contributions.

The City will provide each retiree \$1,500 of post-retirement life insurance coverage. The City will also make available an additional \$1,000 of coverage at the employee's expense, if the employee paid for an additional \$30,000 of life insurance coverage while an active employee.

Non-uniformed union and non-union employees:

Article X of the Collective Bargaining Agreement between the City and the Service Employees International Union, Local 32BJ, Mid-Atlantic District, effective January 1, 2010, establishes retirees' eligibility for post-retirement medical benefits. Article VII Section D. of the personnel manual establishes retirees' eligibility for post-retirement life-insurance benefits.

Eligibility: Any non-uniformed union or non-union employee who retires after completion of 20 years of service and after attainment of age 55. Any employee who retires under the disability provision may begin coverage after 20 years of service.

Benefits: The City will provide medical and prescription drug coverage for the retiree and spouse until Medicare eligibility. The City's maximum monthly contribution for health insurance coverage for each retiree is \$280. If the retiree dies, his or her spouse will be covered and the City will contribute to coverage for the spouse until Medicare eligibility, unless the spouse remarries or has a job in which health insurance coverage is normally granted. If the retiree reaches Medicare eligibility prior to his or her spouse, the spouse may continue coverage and the City will contribute to coverage for the spouse until Medicare eligibility.

The City will provide each retiree \$1,500 of post-retirement life insurance coverage. The City will also make available an additional \$1,000 of coverage at the employee's

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

expense, if the employee paid for an additional \$30,000 of life insurance coverage while an active employee.

Funding Policy and Annual OPEB Costs

The City's contribution is based on projected pay-as-you-go financing requirements. For the year ended December 31, 2011, the City contributed \$747,970 to the OPEB plan.

Police:

Police would pay any additional premiums above the City's contribution of \$340. For the year ended December 31, 2011, police retirees contributed \$116,490 toward the cost of their plans.

Firefighters:

Firefighters would pay any additional premiums above the City's contribution of \$340. For the year ended December 31, 2011, firefighter retirees contributed \$97,725 toward the cost of their plans.

Non-uniformed union and non-union employees:

Non-uniformed union and non-union retirees would pay any additional premiums above the City's contribution of \$280. For the year ended December 31, 2011, non-uniformed union and non-union retirees contributed \$194,152 toward the cost of their plans.

The City's annual OPEB cost (expense) for the plan is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years.

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. Examples include assumptions about future employment, mortality and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the ARC are subject to continual revision, as actual results are compared to past expectations and new estimates are made about the future. The schedule of funding progress presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan and include the types of benefits provided at the time of the valuation and on the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities consistent with the long-term perspective of the calculation. The projections of benefits for financial reporting purposes do not explicitly incorporate the potential effects of legal or contractual funding limitations on the pattern of cost sharing between the employer and plan members in the future.

Information as of the latest actuarial valuation follows:

Valuation date	1/1/2010
Actuarial cost method	Entry age normal
Actuarial assumptions:	
Interest rate	4.5%
Salary increases	5.0%
Medical inflation:	
2010	7.5%
2011	7.0%
2012	6.5%
2013	6.0%
2014	5.5%
2015 and later	5.3% - 4.2%
Amortization method	Level dollar, open period
Amortization period	30 year

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Annual OPEB Cost and Net OPEB Obligation

The City's annual OPEB costs and net OPEB obligations to the Plan for the year ended December 31, 2011 were as follows:

	Governmental Activities	Business-type Activities	Total
Annual required contribution	\$ 1,177,882	\$ 234,658	\$ 1,412,540
Interest on net OPEB obligation	92,172	19,270	111,442
Adjustment to ARC	(125,215)	(26,822)	(152,037)
Annual OPEB cost	1,144,839	227,106	1,371,945
Contribution made	(637,078)	(110,892)	(747,970)
Change in Net OPEB obligation	507,761	116,214	623,975
Net OPEB obligation, beginning	2,047,782	428,733	2,476,515
Net OPEB obligation, ending	<u>\$ 2,555,543</u>	<u>\$ 544,947</u>	<u>\$ 3,100,490</u>

Three-Year Trend Information

Year	Annual OPEB Cost (AOC)	Percentage of AOC Contributed	Net OPEB Obligation (Asset)
2011	\$ 1,371,945	54.5%	\$ 3,100,490
2010	1,383,435	49.3%	2,476,515
2009	1,530,248	67.9%	1,775,607

Funded Status and Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll (b-a/c)
1/1/2010	\$ -	\$ 13,369,049	\$ 13,369,049	0.00%	\$ 36,902,714	36.23%

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

The schedule of funding progress, presented as required supplementary information following the notes to financial statements, presents multi-year trend information about whether the actuarial value of plan assets are increasing or decreasing over time relative to the actuarial accrued liability for benefits.

10. DEFERRED COMPENSATION PLAN

The City offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all full-time City employees at their option, permits participants to defer a portion of their salary until future years. The City provides a 1% matching contribution to the plan up to 4% contributed by the participants. The City contributed \$215,194 to the plan during 2011. The deferred compensation is not available to participants until termination, retirement, death, or unforeseeable emergency.

11. COMMITMENT AND CONTINGENCIES

Federal and State Grants

Under the terms of federal and state grants, periodic audits are required and certain costs may be disallowed as not being appropriate expenditures under the terms of the grants. Such audits could lead to reimbursement to the grantor agencies. City management believes disallowances, if any, will be immaterial.

Litigation

The City is defending a number of lawsuits, the outcome of which, in the opinion of management, will not materially affect the financial position of the City.

Risk Management

The City is exposed to various risks of loss related to torts: theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. Significant losses are covered by commercial insurance. There were no significant reductions in insurance coverages in 2011. Settlement amounts have not exceeded insurance coverages for the current year or three prior years.

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Construction

The City is committed in various construction contracts in the total amount of \$2,011,378 at December 31, 2011.

The Parking Authority has agreed to terms with a construction company related to services provided for the construction of the South Main Street Garage. Under the agreement, the Authority is to make monthly payments of principal and interest of \$46,616 beginning in January 2012 through October 2012 on the outstanding construction payables of \$454,156, which includes interest on the outstanding payables calculated at 6% of \$31,510.

Line of Credit

Beginning on September 8, 2009, the Library established a line of credit in the amount of \$200,000. The interest rate established by the lender is equal to the prime rate plus .75%, except that the interest rate will be no less than 5.00%. In October of 2011, the line of credit was renewed, and if no demand is made, will expire on June 30, 2012. At December 31, 2011, there were no amounts borrowed under the line of credit.

Early Retirement Benefits

At December 31, 2010, the Library offered an Early Retirement Incentive Program to its qualifying employees. The Program stipulated that any full-time employee, 55 years of age or older by December 31, 2010, choosing to retire would receive \$1,000 for every year of service at the Library, up to \$20,000; any part-time employee, whose average work week was no less than 20 hours over the past five years, choosing to retire would receive \$500 for every year of service to the Library, up to \$10,000; and any part-time employee, whose average work week was under 20 hours over the past five years, choosing to retire would receive \$250 for every year of service to the Library, up to \$5,000. The employee could choose to receive this amount in two equal lump sum payments in 2011 and 2012 or choose to designate the money for health insurance for 2011 and 2012. If choosing the health insurance option, the employee would only receive benefits up to the amount they earned based on tenure. If there are monies left over, the employee will receive this as a lump sum. At December 30, 2011, 15 employees retired as a part of this program and the total amount committed to these employees is approximately \$127,000.

Violations of Finance-Related Legal and Contractual Provisions

During the year ended December 31, 2011, the City's pooled cash accounts included restricted and unrestricted funds. Therefore, the City could be using restricted money for expenditures in the unrestricted funds. The City agrees and Bond Counsel did review applicable bond

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

documents and the City is in compliance with applicable terms and conditions.

During the year ended December 31, 2011, the City did not comply with certain regulations related to Act 78 and Act 56 for landline and wireless 911 revenues. The City used Act 78 money to pay for unallowable expenses. The City also used Act 56 money to pay for Act 78 expenditures. The City intends to return the excess costs, in the amount of \$549,080, to the Act 78 account from the General Fund and excess costs, in the amount of \$2,499,633, to the Act 56 account from the Act 78 account and/or General Fund. The City intends to work with the 911 Fund manager to ensure that the payments remain in allowable limits.

During the year ended December 31, 2011, the General Fund borrowed restricted funds from the Community Development Block Grant Fund to pay for unallowable expenses. The City reimbursed the funds during the year ended December 31, 2011.

During the year ended December 31, 2011, the City advanced itself earned income tax (EIT) receipts that were being held on behalf of other governments and owed approximately \$3.4 million back to the EIT account at December 31, 2011. Beginning January 1, 2011, Keystone Collections Group is collecting the City's EIT funds; therefore, the City can no longer advance or borrow EIT. Also, as of August 3, 2012, the City has \$1,415,300 in outstanding claims to other municipalities. The City is awaiting payment and/or responses which can be used towards the shortfall. There are additional claims that still need to be processed, both from the City to other municipalities and from other municipalities to the City.

12. DERIVATIVE FINANCIAL INSTRUMENT

Objective of the Interest Rate Swap

As a means to manage interest rate exposure, the City entered into an interest rate swap in connection with its Bethlehem Authority, Guaranteed Water Revenue Note, Series of 1997 (see Note 7). The intention of the swap was to effectively change the City's variable interest rate on this long-term debt to a synthetic fixed rate of 3.9%.

Terms

The interest rate swap agreement was effective January 1, 2003. The long-term debt and related swap agreement mature on August 1, 2012 and the swap's notional amount of \$5,595,000 matches the principal amount of the hedged debt. Beginning in 2003, the notional amount of the swap and the principal amount of the debt decline at an equal rate. Under the swap, the City pays the counterparty a fixed payment of 3.9% and receives a variable payment computed as Securities Industry and Financial Markets Association

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

Municipal Swap Index (SIFMA), one week (weighted weekly average). Conversely, the variable rate debt is based on a weekly remarketed rate plus 1.8%.

Fair Value

The swap had a negative fair value of \$105,000 as of December 31, 2011. Because the coupon on the City's variable-rate notes adjusts to changing interest rates, the notes do not have a corresponding fair value increase. The fair value was calculated by the financial advisor to the Bethlehem Authority and reflects the fact that taxable interest rates were lower at December 31, 2011.

Credit Risk

As of December 31, 2011, the swap had a negative fair value. However, should interest rates increase and the fair value of the swap becomes positive, the City would be exposed to credit risk in the amount of the derivative's fair value. The Counterparty, Lehman Brothers Special Financing, Inc., has filed for bankruptcy protection in the United States Bankruptcy Court.

Basis Risk

The swap exposes the City to basis risk should the relationship between the weekly remarketed rate (which has to be paid by the Bethlehem Authority) and SIFMA (which is the amount paid by the counterparty to the Bethlehem Authority) diverge, changing the synthetic rate on the bonds. The effect of this basis differential has generally been an increase in interest costs. As of December 31, 2011, the weekly remarketed rate was .14%, whereas SIFMA was .11355%.

Liquidity Facility Risk

During the past several years, obtaining liquidity facilities has become increasingly difficult and expensive. Many issuers are unable to access this market at a price that is as economical as it once was. Indeed, the Bethlehem Authority has experienced a significant increase in the "gross up rate" of the financing due in large part to costs associated with liquidity and credit enhancement. This has resulted in a significant increase in the synthetic fixed rate on the loan.

Termination Risk

The derivative contract uses the International Swap Dealers Association Master Agreement, which includes standard termination events, such as failure to pay and bankruptcy. The City or the counterparty may terminate the swap if the other party fails to perform under the terms

CITY OF BETHLEHEM, PENNSYLVANIA

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YEAR ENDED DECEMBER 31, 2011

of the contract. If the swap is terminated, the variable-rate loan would no longer carry a synthetic fixed interest rate and the City would be exposed to interest rate risk. Also, if at the time of termination the swap has a negative fair value, the City would be liable to the counterparty for a payment equal to the swap's fair value. If at the time of termination the swap has a positive fair value but the counterparty is unable for any reason, including its insolvency, to pay such amount, the City might not receive amounts due it under the contract.

13. CREDIT RISK AND MARKET RISK

The City uses its authority to levy certain general purpose taxes. Major taxing revenue sources include real estate, earned income, mercantile, and business privilege taxes. These taxes account for approximately 93% of the total taxes collected by the City in 2011. Although the City has a diversified taxing base, its citizens' ability to honor their taxing obligations is substantially dependent upon the general economic condition of the region.

The market value of the City's investments is subject to fluctuations in the prevailing market prices of those investments.

14. RELATED PARTY TRANSACTIONS

The City provided services to a company in which a Council member is an officer and, as of December 31, 2011, the company owes the City approximately \$127,000.

The City provided enterprise zone loans to a company in which several high level City employees are members of the company's Board of Directors and, as of December 31, 2011, the company owes the City approximately \$642,000.

15. NEGATIVE FUND BALANCE AND NET ASSETS OF ENTERPRISE FUNDS

911 Fund

The 911 Fund had a deficit balance of \$2,132,638 at December 31, 2011. In 2011, the City transferred approximately \$1 million from the General Fund to the 911 Fund as a way to begin addressing the deficit balance. This deficit will continue to be addressed as part of the 2013 budget.

Water Fund

The Water Fund had a deficit balance of \$2,126,919 at December 31, 2011. The negative net

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO FINANCIAL STATEMENTS

YEAR ENDED DECEMBER 31, 2011

assets in the water fund is largely due to the depreciation of assets outpacing new capital investment in the water system, and the austerity that this requires, the City and the Bethlehem Authority are working on a long-term restructuring to deal with this issue.

Additionally, the City obtained approval from the Pennsylvania Public Utility Commission for a rate increase in early 2012. The rate increase was 10.7%, retroactive back to December 16, 2011.

16. SUBSEQUENT EVENTS

In March 2012, the City issued Guaranteed Revenue Note, Series of 2012, in the amount of \$9,429,730 for the design and construction project of the City's digester system and waste activated sludge thickening improvements project.

In March 2012, the Parking Authority entered into a capital lease for 400 smart parking meters. The total cost of the equipment is \$208,236 and is payable in 60 monthly installments of \$3,857 beginning in April 2012.

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**Required Supplementary
Information**

CITY OF BETHLEHEM, PENNSYLVANIA

BUDGETARY COMPARISON SCHEDULE - BUDGET AND ACTUAL (BUDGETARY BASIS) GENERAL FUND

YEAR ENDED DECEMBER 31, 2011

	Budgeted Amounts		Actual Amounts	Variance with Final Budget- Positive (Negative)
	Original	Final		
Revenues:				
Taxes	\$ 31,969,152	\$ 31,969,152	\$ 32,446,033	\$ 476,881
Licenses and permits	2,050,000	2,050,000	2,201,332	151,332
Intergovernmental	7,217,908	7,539,092	8,902,920	1,363,828
Departmental earnings	6,542,533	6,542,533	7,159,317	616,784
Fines and forfeitures	560,000	560,000	547,875	(12,125)
Investment income	-	-	67,958	67,958
Municipal recreation	542,800	542,800	378,706	(164,094)
Host fees	8,750,000	8,750,000	9,225,404	475,404
Other operating revenues	587,362	587,362	360,429	(226,933)
Miscellaneous	2,166,607	2,166,607	3,930,558	1,763,951
Total revenues	<u>60,386,362</u>	<u>60,707,546</u>	<u>65,220,532</u>	<u>4,512,986</u>
Expenditures:				
Current:				
General government	887,740	1,927,740	869,519	1,058,221
Administration	1,808,255	1,801,126	1,674,943	126,183
Community development	5,321,027	5,556,306	5,316,204	240,102
Parks and public property	3,676,040	3,722,410	3,615,734	106,676
Public works	5,750,659	5,808,729	5,401,655	407,074
Police	12,473,310	13,016,410	12,359,664	656,746
Fire	10,000,437	10,506,942	10,373,976	132,966
General	17,118,401	16,066,655	25,345,715	(9,279,060)
Civic	108,420	108,420	104,150	4,270
Library	1,230,000	1,230,000	1,230,000	-
Debt service:				
Principal	2,329,645	2,329,645	2,581,645	(252,000)
Interest	2,367,996	2,367,996	2,492,243	(124,247)
Total expenditures	<u>63,071,930</u>	<u>64,442,379</u>	<u>71,365,448</u>	<u>(6,923,069)</u>
Excess (Deficiency) of Revenues Over Expenditures	<u>(2,685,568)</u>	<u>(3,734,833)</u>	<u>(6,144,916)</u>	<u>(2,410,083)</u>
Other Financing Sources (Uses):				
Transfers in	3,317,638	3,317,638	2,854,622	(463,016)
Transfers out	(1,832,070)	(782,805)	(782,805)	-
Issuance of long-term debt	1,200,000	1,200,000	12,700,000	11,500,000
Total other financing sources (uses)	<u>2,685,568</u>	<u>3,734,833</u>	<u>14,771,817</u>	<u>11,036,984</u>
Net Change in Fund Balance	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 8,626,901</u>	<u>\$ 8,626,901</u>

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

CITY OF BETHLEHEM, PENNSYLVANIA

NOTES TO BUDGETARY COMPARISON SCHEDULE

YEAR ENDED DECEMBER 31, 2011

1. ADJUSTMENT TO CONVERT FROM BUDGETARY BASIS TO GAAP – GENERAL FUND

Adjustments necessary to convert the results of operations and fund balances on the budgetary basis to the GAAP basis are as follows:

	Revenues and Other Financing Sources	Expenditures and Other Financing Uses
Budgetary basis	\$ 80,775,154	\$ 72,148,253
Agency fund borrowings	6,256	(1,739,355)
Other fund borrowings	(92,288)	(1,866,009)
Accrual adjustments:		
Receivables:		
Beginning of year	(10,671,380)	(17,600)
End of year	11,811,075	206
Due from/to:		
Beginning of year	7,623,872	-
End of year	(11,241,750)	(1,505,921)
Accrued liabilities:		
Beginning of year	-	(9,887,385)
End of year	106,107	3,839,712
Deferred revenues:		
Beginning of year	2,805,618	-
End of year	(3,018,893)	-
Reclassifications	5,277,126	5,277,126
GAAP basis	\$ 83,380,897	\$ 66,249,027

2. STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

Excess of Expenditures over Appropriations:

	Appropriation	Expenditure
Current:		
General	\$ 16,066,655	\$ 25,345,715
Debt service:		
Principal	2,329,645	2,581,645
Interest	2,367,996	492,243

Appropriations sufficient to provide for the excess expenditures were made available from issuance of debt.

CITY OF BETHLEHEM, PENNSYLVANIA

SCHEDULES OF FUNDING PROGRESS - PENSIONS

(in thousands)

	Actuarial Valuation Date	Actuarial Value of Assets	Actuarial Accrued Liability (AAL) Entry Age		Excess of Assets Over (Under) AAL	Funded Ratio	Covered Payroll	Excess (Deficiency) as a Percentage of Covered Payroll
Police:								
	1/1/2007	\$ 64,234	\$ 67,123		\$ (2,889)	96%	\$ 8,604	-34%
	1/1/2009	64,399	74,424		(10,025)	87%	10,058	-100%
	1/1/2011	63,718	83,930 *		(20,212)	76%	11,565	-175%
Firemen:								
	1/1/2007	48,461	49,969		(1,508)	97%	5,994	-25%
	1/1/2009	48,780	55,305		(6,525)	88%	6,544	-100%
	1/1/2011	48,627	62,441 **		(13,814)	78%	7,318	-189%
Officers and Employees:								
	1/1/2007	9,001	10,178		(1,177)	88%	321	-367%
	1/1/2009	7,943	8,984		(1,041)	88%	241	-432%
	1/1/2011	7,121	8,531		(1,410)	83%	120	-1175%
PMRS:								
	1/1/2007	64,898	85,564 ***		(20,666)	76%	20,225	-102%
	1/1/2009	77,370	97,712 ****		(20,342)	79%	23,164	-88%
	1/1/2011	88,255	111,163 *****		(22,908)	79%	22,034	-104%

Source: Actuarial Reports. Valuations performed on a biennial basis.

Note: State law requires biennial valuations on the odd-numbered years.

* - Actuarial losses and actuarial assumption modifications for the 1/1/2011 valuation resulted in increases to the AAL of \$10.7 million.

** - Actuarial losses and actuarial assumption modifications for the 1/1/2011 valuation resulted in increases to the AAL of \$6.5 million.

*** - Significant plan changes for the 1/1/2007 valuation resulted in increases to the AAL of \$4.2 million.

**** - Significant plan changes for the 1/1/2009 valuation resulted in increases to the AAL of \$2.1 million.

***** - Actuarial losses and actuarial assumption modifications for the 1/1/2011 valuation resulted in increases to the AAL of \$5.5 million.

See accompanying note to required supplementary information.

CITY OF BETHLEHEM, PENNSYLVANIA

SCHEDULES OF CONTRIBUTIONS FROM EMPLOYER AND OTHER CONTRIBUTING ENTITIES - PENSIONS

(in thousands)

Calendar Year	Police		Firemen		Officers and Employees		PMRS	
	Annual Required Contributions	Percentage Contributed	Annual Required Contributions	Percentage Contributed	Annual Required Contributions	Percentage Contributed	Annual Required Contributions	Percentage Contributed
2006	\$ 1,572	100%+	\$ 987	100%+	\$ 381	100%+	\$ 916	100%+
2007	1,692	100%	1,045	100%	381	100%+	3,168	100%+
2008	1,713	100%	1,019	100%	379	98%	3,264	100%+
2009	1,870	100%	1,174	100%	623	100%	3,350	100%
2010	1,921	100%	1,137	100%	468	100%	2,861	100%
2011	2,534	100%	1,673	100%	456	100%	3,041	100%

Note: Contributions include state pension aid.

See accompanying note to required supplementary information.

CITY OF BETHLEHEM, PENNSYLVANIA

NOTE TO REQUIRED SUPPLEMENTARY PENSION INFORMATION

YEAR ENDED DECEMBER 31, 2011

The information presented in the required supplementary schedules of trend information was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest available actuarial valuation follows:

	<u>Police</u>	<u>Firemen</u>	<u>Officers and Employees</u>	<u>PMRS</u>
Actuarial valuation date	1/1/2011	1/1/2011	1/1/2011	1/1/2011
Actuarial cost method	Entry Age Normal	Entry Age Normal	Entry Age Normal	Entry Age Normal
Amortization method	Level Dollar Closed	Level Dollar Closed	Level Dollar Closed	Level Dollar Adjustment Equal to 10% of Negative Unfunded AAL
Amortization period	18 years	16 years	2 years	9 years
Asset valuation method	5 year smoothed value with a maximum of 120% market value	5 year smoothed value with a maximum of 120% market value	5 year smoothed value with a maximum of 120% market value	Market Value as determined by Trustee
Actuarial assumptions:				
Investment rate of return	7.5%	7.5%	7.5%	6.0%
Projected salary increases	4.5%	4.5%	4.5%	3.7%-6.4%

CITY OF BETHLEHEM, PENNSYLVANIA
POST-EMPLOYMENT BENEFITS OTHER THAN PENSIONS

YEAR ENDED DECEMBER 31, 2011

SCHEDULE OF FUNDING PROGRESS

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll (b-a/c)
1/1/2008	\$ -	\$ 14,256,169	\$ 14,256,169	0.0%	\$ 32,868,661	43.4%
1/1/2010	-	13,369,049	13,369,049	0.0%	36,902,714	36.2%

Note: Valuation as of 1/1/2008 represents the initial valuation for the Plan as required under GASB Statement No. 45

SCHEDULE OF EMPLOYER CONTRIBUTIONS

Year Ended December 31,	Annual Required Contributions	Percentage Contributed
2009	\$ 1,545,919	67.3%
2010	1,412,540	48.3%
2011	1,412,540	53.0%

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION

Valuation Date	January 1, 2010
Actuarial Cost Method	Entry Age Normal
Actuarial Assumptions:	
Investment Rate of Return	4.5%
Projected Salary Increases	5%
Medical inflation:	
2010	7.5%
2011	7.0%
2012	6.5%
2013	6.0%
2014	5.5%
2015 and later	5.3% - 4.2%
Amortization Method	Level Dollar, Open Period
Amortization Period	30 Years

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Supplementary Information

CITY OF BETHLEHEM, PENNSYLVANIA

COMBINING BALANCE SHEET - OTHER NON-MAJOR GOVERNMENTAL FUNDS

DECEMBER 31, 2011

	911 Fund	Community Development Block Grant Fund	Liquid Fuels Fund	Debt Service Fund	Total
Assets					
Cash and cash equivalents	\$ 4,745	\$1,895,642	\$ 193,082	\$ -	\$ 2,093,469
Receivables:					
Loans	-	2,550,078	-	-	2,550,078
Other	84,888	-	-	-	84,888
Due from other funds	549,080	-	-	-	549,080
Due from other governments	-	187,404	-	-	187,404
Total Assets	\$ 638,713	\$4,633,124	\$ 193,082	\$ -	\$ 5,464,919
Liabilities and Fund Balance					
Liabilities:					
Accounts payable and other accrued expenses	\$ 38,839	\$ 245,670	\$ 31,690	\$ -	\$ 316,199
Accrued payroll	56,080	12,057	-	-	68,137
Accrued vacation and other compensated absences	24,042	23,537	-	-	47,579
Deferred revenues	2,652,390	4,351,860	-	-	7,004,250
Total Liabilities	2,771,351	4,633,124	31,690	-	7,436,165
Fund Balance:					
Restricted for:					
Public works	-	-	161,392	-	161,392
Unassigned	(2,132,638)	-	-	-	(2,132,638)
Total Fund Balance	(2,132,638)	-	161,392	-	(1,971,246)
Total Liabilities and Fund Balance	\$ 638,713	\$4,633,124	\$ 193,082	\$ -	\$ 5,464,919

CITY OF BETHLEHEM, PENNSYLVANIA

COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE - OTHER NON-MAJOR GOVERNMENTAL FUNDS

YEAR ENDED DECEMBER 31, 2011

	911 Fund	Community Development Block Grant Fund	Liquid Fuels Fund	Debt Service Fund	Total
Revenues:					
Intergovernmental revenues	\$ 1,210,354	\$3,392,277	\$1,362,381	\$ -	\$ 5,965,012
Other charges	604,038	-	-	-	604,038
Investment income	14	103,438	277	-	103,729
Other	-	56,473	-	-	56,473
Total revenues	1,814,406	3,552,188	1,362,658	-	6,729,252
Expenditures:					
Current:					
Public works	-	-	1,565,072	-	1,565,072
Police	1,683,281	-	-	-	1,683,281
Program expenditures	-	4,432,868	-	-	4,432,868
Debt service - principal	-	-	-	2,952,000	2,952,000
Debt service - interest	-	-	-	4,509,838	4,509,838
Total expenditures	1,683,281	4,432,868	1,565,072	7,461,838	15,143,059
Excess (Deficiency) of Revenues Over Expenditures	131,125	(880,680)	(202,414)	(7,461,838)	(8,413,807)
Other Financing Sources (Uses):					
Transfers in	-	880,680	-	7,461,838	8,342,518
Transfers out	(387,209)	-	-	-	(387,209)
Total other financing sources (uses)	(387,209)	880,680	-	7,461,838	7,955,309
Net Change in Fund Balance	(256,084)	-	(202,414)	-	(458,498)
Fund Balance:					
Beginning of year	(1,876,554)	-	363,806	-	(1,512,748)
End of year	<u><u>\$(2,132,638)</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 161,392</u></u>	<u><u>\$ -</u></u>	<u><u>\$(1,971,246)</u></u>