

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the City of Great Falls, we offer readers of the City of Great Falls' financial statements this narrative overview and analysis of the financial activities of the City of Great Falls for the fiscal year ended June 30, 2005. We encourage readers to consider the information presented here in combination with additional information that we have furnished in the accompanying letter of transmittal found on pages 1-2 and the City's financial statements, which begin on page 7.

FINANCIAL HIGHLIGHTS

- The assets of the City of Great Falls exceeded its liabilities at the close of the most recent fiscal year by \$151,228,173. Of this amount, \$18,876,581 may be used to meet the government's ongoing obligations to citizens and creditors.
- The government's total net assets increased by \$3,941,733 in comparison with the prior year. Approximately three fourths of this increase is attributable to an issuance of debt for the sewer fund.
- As of the close of the most recent fiscal year, the City of Great Falls's governmental funds reported combined ending fund balances of \$12,468,873, a decrease of \$3,246,626 in comparison with the prior year. Approximately three fourths of this total amount, \$8,943,679, is available for spending at the government's discretion.
- At the close of the most recent fiscal year, unreserved fund balance for the general fund was \$3,280,357, or 22 percent of total general fund expenditures.
- The City of Great Falls's bonded debt increased by \$4,420,269 (11 percent) during the most recent fiscal year. The key factor in this increase was the issuance of \$5,005,000 in revenue bonds for the sewer fund.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the City of Great Falls' basic financial statements which are comprised of four components: 1) government-wide financial statements, 2) fund financial statements, 3) notes to the financial statements, and 4) other required supplementary information in addition to the basic financial statements themselves.

GOVERNMENT-WIDE FINANCIAL STATEMENTS. The government-wide financial statements, presented on pages 19-21, are designed to provide readers with a broad overview of the City' finances, in a manner similar to a private-sector business.

The statement of net assets presents information on all of the City of Great Falls' 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 of Great Falls 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, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., delinquent taxes and earned but unused compensated absences).

The government-wide financial statements distinguish functions of the City of Great Falls that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the City of Great Falls include general government, public safety, public works, culture and recreation, housing and development, and interest and fees. The business-type activities of the City of Great Falls include activities such as water, sanitary sewer, storm drain, sanitation, and golf courses operations.

The government-wide financial statements include not only the primary government of the City of Great Falls but also two component units, the Great Falls Business Improvement District and the Great Falls Library Foundation. The exclusion of the component units would cause the City of Great Falls' financial statements to be misleading or incomplete and should, therefore, be included in the City of Great Falls' financial reports. Consolidated financial information for these component units is reported separately from the financial information presented for the primary government itself. Requests for additional information for the component units should be addressed to Greg Madson, Ph.D., Executive Director, Great Falls

Business Improvement District, 417 Central Avenue, Suite 320, Great Falls, MT 59401 or DeeAnn Andre, Executive Director, Great Falls Public Library Foundation, PO Box 742, Great Falls, MT 59403.

FUND FINANCIAL STATEMENTS. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City of Great Falls, 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 of Great Falls 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.

Because 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 of Great Falls maintains thirty-six individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the General fund, the Street District fund, and the Community Development Block Grant fund, all of which are considered to be major funds. Data for the basic governmental fund financial statements is presented on pages 24-27. Data from the other thirty-three governmental funds are combined into a single, aggregated presentation, on pages 80-114.

The City of Great Falls adopts an annual appropriated budget. A budgetary comparison schedule has been provided for the General Fund and the major special revenue funds to demonstrate compliance with this budget. In addition, the City has provided budgetary comparison schedules for non-major governmental funds.

Proprietary Funds. The City of Great Falls maintains two different types of proprietary funds. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The City of Great Falls uses enterprise funds to account for its water, sewer, storm drain, electric utility, sanitation, safety services, parking, golf courses, swim pools, recreation, fairgrounds, and civic center events operations. Internal service funds are an accounting device to accumulate and allocate costs internally among the City of Great Falls' various functions. The City of Great Falls uses internal service funds to account for administrative services, central communications, health and benefits, insurance and safety, fiscal services, information technology, central garage, craft services, engineering, public works administration, park and recreation administration, and facility services. Because these services predominantly benefit governmental rather than business-type functions, they have been included within governmental activities in the government-wide financial statements.

Proprietary fund financial statements provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statements provide separate information for the Water, Sewer, Storm Drain, Sanitation, and Golf Courses operations funds, all of which are considered to be major funds of the City of Great Falls. Data for these major funds is presented on pages 28-35. The other eight proprietary funds are combined into a single, aggregated presentation, presented on pages 115-123. Conversely, the internal service funds are combined into a single, aggregated presentation in the proprietary fund financial statements, presented on pages 125-139.

Fiduciary funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statement because the resources of those funds are not available to support the City of Great Falls' own programs. The accounting used for fiduciary funds is much like that used for proprietary funds. Combined data for the fiduciary funds is presented on pages 36-37 with detail data presented on pages 143-145.

NOTES TO THE FINANCIAL STATEMENTS. The notes, presented on pages 39-72, provide additional narrative and tabular information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

OTHER INFORMATION. In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information concerning the City of Great Falls' budgetary control, on pages 73-78.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. At the end of the most recent fiscal year, the assets of the City of Great Falls exceeded its liabilities by \$151,228,173.

By far the largest portion of the City of Great Falls' net assets, \$113,006,443, (75 percent) reflects its investment in capital assets (land, buildings, machinery and equipment, etc.) less any related debt used to acquire those assets that is still outstanding. The City of Great Falls uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the City of Great Falls' investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

City of Great Falls' Net Assets

| | Governmental Activities | | Business-type Activities | | Total | |
|---------------------------------|-------------------------|----------------------|--------------------------|----------------------|-----------------------|-----------------------|
| | 2005 | 2004 | 2005 | 2004 | 2005 | 2004 |
| Assets: | | | | | | |
| Current and other assets | \$ 22,526,336 | \$ 27,620,152 | \$ 22,617,508 | \$ 19,371,642 | \$ 45,143,844 | \$ 46,991,794 |
| Capital assets | 49,953,103 | 45,901,816 | 108,668,459 | 103,944,778 | 158,621,562 | 149,846,594 |
| Total assets | <u>72,479,439</u> | <u>73,521,968</u> | <u>131,285,967</u> | <u>123,316,420</u> | <u>203,765,406</u> | <u>196,838,388</u> |
| Liabilities: | | | | | | |
| Long-term liabilities | | | | | | |
| outstanding | 8,018,524 | 8,444,432 | 35,090,443 | 30,347,628 | 43,108,967 | 38,792,060 |
| Other liabilities | 5,468,415 | 6,553,396 | 4,113,525 | 4,206,492 | 9,581,940 | 10,759,888 |
| Total liabilities | <u>13,486,939</u> | <u>14,997,828</u> | <u>39,203,968</u> | <u>34,554,120</u> | <u>52,690,907</u> | <u>49,551,948</u> |
| Net assets: | | | | | | |
| Invested in capital assets, net | | | | | | |
| of related debt | 40,855,589 | 36,396,557 | 71,225,154 | 69,331,957 | 112,080,743 | 105,728,514 |
| Restricted | 6,772,654 | 7,452,602 | 9,365,282 | 8,835,470 | 16,137,936 | 16,288,072 |
| Unrestricted | 11,364,257 | 14,674,981 | 11,491,563 | 10,594,873 | 22,855,820 | 25,269,854 |
| Total net assets | <u>\$ 58,992,500</u> | <u>\$ 58,524,140</u> | <u>\$ 92,081,999</u> | <u>\$ 88,762,300</u> | <u>\$ 151,074,499</u> | <u>\$ 147,286,440</u> |

An additional portion of the City of Great Falls' net assets, \$19,345,149, represents resources that are subject to external restrictions on how they may be used. Restricted assets reported for the business-type activities were \$12,266,972. The majority of these assets are related to the debt service reserve required for the issuance of revenue related debt. The remaining balance of unrestricted net assets, \$18,876,581, may be used to meet the government's ongoing obligations to citizens and creditors.

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

City of Great Falls' Changes in Net Assets

| | Governmental Activities | | Business-type Activities | | Total | |
|---|-------------------------|----------------------|--------------------------|----------------------|-----------------------|-----------------------|
| | 2004 | 2003 | 2004 | 2003 | 2004 | 2003 |
| Revenues: | | | | | | |
| Program revenues: | | | | | | |
| Charges for services | \$ 9,537,875 | \$ 8,401,089 | \$ 21,185,661 | \$ 20,094,251 | \$ 30,723,536 | \$ 28,495,340 |
| Operating grants and contributions | 281,504 | 583,207 | - | - | 281,504 | 583,207 |
| Capital grants and contributions | 3,701,084 | 2,336,484 | - | - | 3,701,084 | 2,336,484 |
| General revenues: | | | | | | |
| Property taxes, levied for general purposes | 10,979,102 | 10,889,623 | - | - | 10,979,102 | 10,889,623 |
| Grants and contributions, unrestricted | 7,906,709 | 7,218,956 | - | - | 7,906,709 | 7,218,956 |
| Other | 304,794 | 377,578 | 191,992 | 78,163 | 496,786 | 455,741 |
| Miscellaneous | 620,169 | 2,328,926 | 94,433 | 311,177 | 714,602 | 2,640,103 |
| Total revenues | 33,331,237 | 32,135,863 | 21,472,086 | 20,483,591 | 54,803,323 | 52,619,454 |
| Expenses: | | | | | | |
| General government | 8,044,127 | 7,572,738 | - | - | 8,044,127 | 7,572,738 |
| Public safety | 11,983,789 | 11,769,875 | - | - | 11,983,789 | 11,769,875 |
| Public works | 3,985,723 | 4,225,922 | - | - | 3,985,723 | 4,225,922 |
| Culture and recreation | 3,490,282 | 3,129,879 | - | - | 3,490,282 | 3,129,879 |
| Housing and development | 2,572,602 | 2,416,995 | - | - | 2,572,602 | 2,416,995 |
| Interest and fees | 271,990 | 750,348 | - | - | 271,990 | 750,348 |
| Water | - | - | 5,325,599 | 4,833,493 | 5,325,599 | 4,833,493 |
| Sewer | - | - | 5,416,556 | 4,629,286 | 5,416,556 | 4,629,286 |
| Storm Drain | - | - | 662,616 | 694,124 | 662,616 | 694,124 |
| Sanitation | - | - | 2,806,848 | 2,641,732 | 2,806,848 | 2,641,732 |
| Golf Courses | - | - | 1,449,714 | 1,453,833 | 1,449,714 | 1,453,833 |
| Other | - | - | 3,376,536 | 4,695,909 | 3,376,536 | 4,695,909 |
| Total expenses | 30,348,513 | 29,865,757 | 19,037,869 | 18,948,377 | 49,386,382 | 48,814,134 |
| Increase in net assets | | | | | | |
| before transfers | 2,982,724 | 2,270,106 | 2,434,217 | 1,535,214 | 5,416,941 | 3,805,320 |
| Transfers | (685,734) | (1,560,421) | 685,734 | 1,560,421 | - | - |
| Increase in net assets | 2,296,990 | 709,685 | 3,119,951 | 3,095,635 | 5,416,941 | 3,805,320 |
| Net assets - beginning - Restated | 56,227,150 | 55,517,465 | 85,348,836 | 82,253,201 | 141,575,986 | 137,770,666 |
| Prior Period Adjustment | - | - | 293,513 | - | 293,513 | - |
| Net assets - ending | \$ 58,524,140 | \$ 56,227,150 | \$ 88,762,300 | \$ 85,348,836 | \$ 147,286,440 | \$ 141,575,986 |

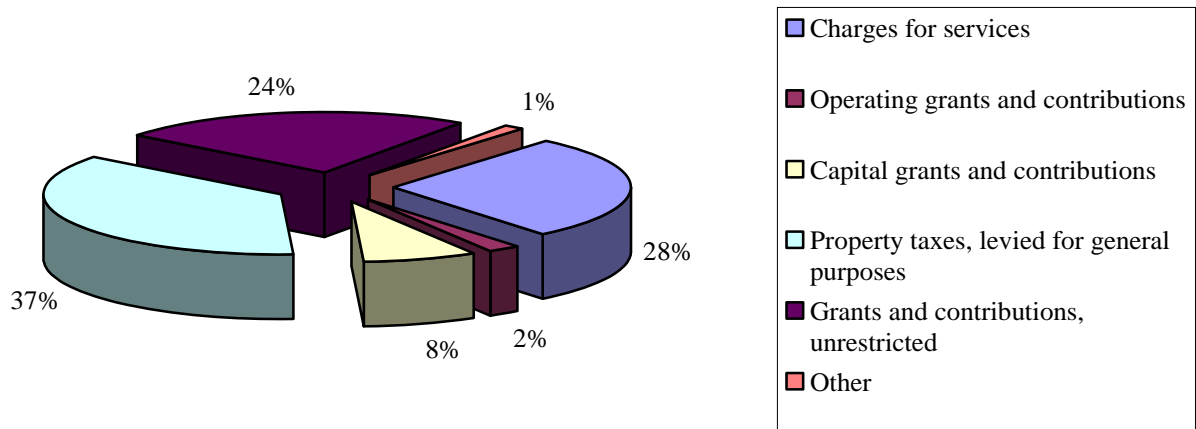
The City of Great Falls' revenues totaled \$57,716,528. The total cost of all programs and services was \$53,482,834. The government was able to cover this year's costs in both governmental activities and business-type activities. Our analysis below separately considers the operations of governmental and business-type activities.

Governmental activities. Revenues for the most recent year from governmental activities were \$35,606,423 while expenses were \$32,748,338. Net assets thus increased by \$2,858,085 before transfers. Taxes increased by \$799,445 primarily due to a voter approved soccer park mill and a statutorily authorized 1.25% increase for inflation. Grants and contributions revenues increased by \$1,470,027 primarily due to new grants being awarded for public safety, community development, housing and development, and culture and recreation functions of the City of Great Falls. Charges for services increased by \$683,610, primarily due to one-time charges for the Lewis and Clark Signature Event and loan adjustments for the Economic Revolving fund.

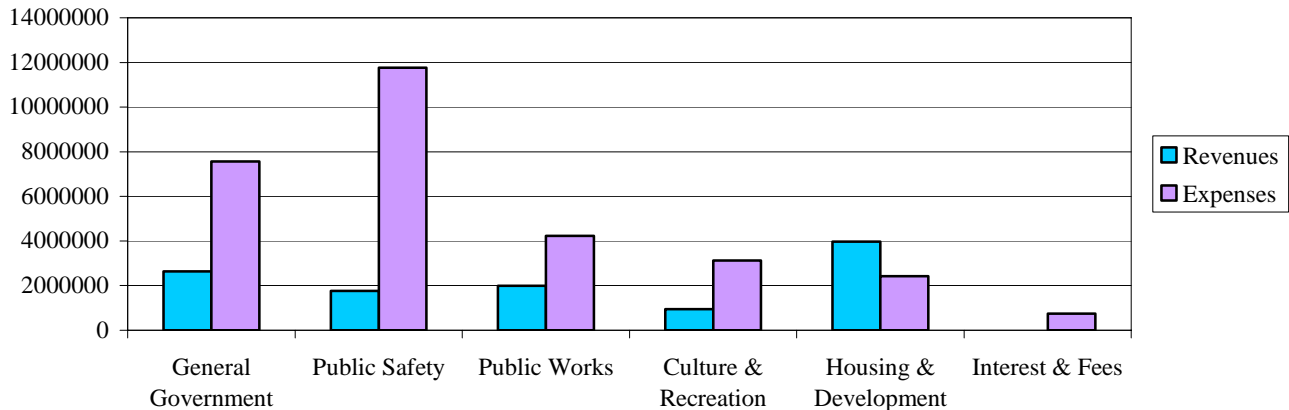
General government related expenses increased by \$389,506 primarily due to expenses for the Lewis and Clark Signature Event. Public safety related expenses increased by \$674,709 primarily due to the increased activity in the 911 Special Revenue fund and the Fire Special Revenue fund. Culture and recreation related expenses increased by \$553,535 due to increased activity in the Library fund and the Lewis and Clark Signature Event. Housing and development expenses increased by \$754,726 due to increased activity in the HOME Grant program. Interest and fees increased by \$192,270 due to the first debt payment for the General Obligation Bond.

Housing and development program revenues exceed program expenses by \$2,945,485 primarily due to capital grants and contributions expenses being charged to capital assets construction.

Revenues by Source - Governmental Activities

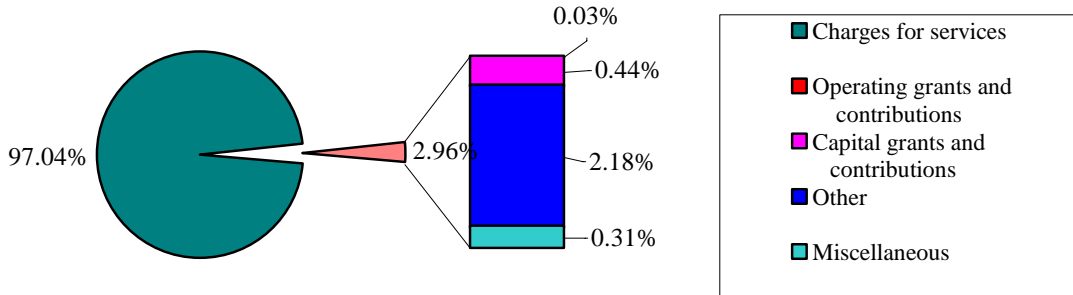


Program Revenues and Expenses - Governmental Activities

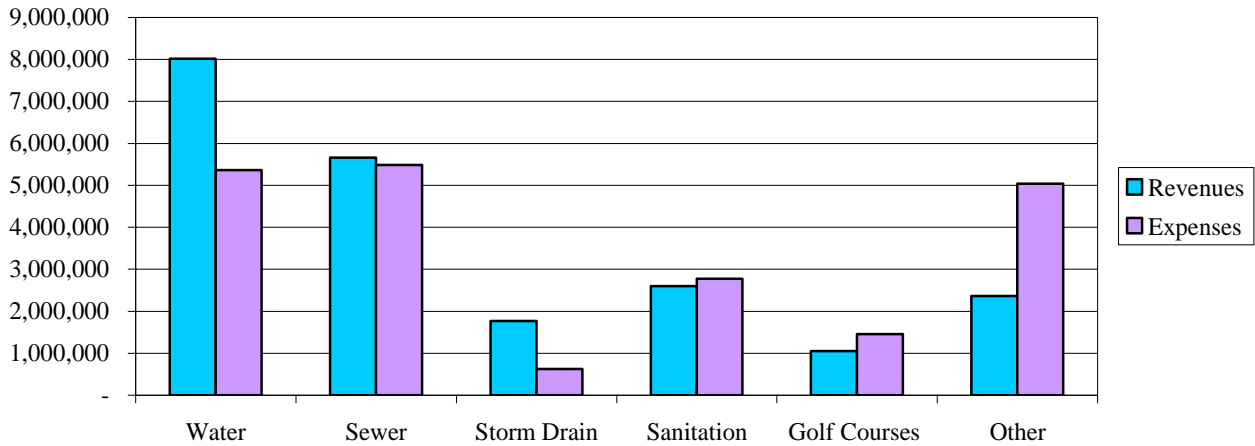


Business-type activities. Revenues for the most recent year from business-type activities were \$22,110,105 while expenses were \$20,734,496. Net assets thus increased by \$1,375,609 before transfers. Overall revenue derived from charges for services increased \$269,946 primarily due to a slight increase in rates charged for water, sewer and storm drain. Expenses for the business-type activities increased by \$1,696,627 due primarily to increased activity in the Electric Utility fund. Other business-type fund expenses were \$1,295,728 more than the revenues primarily due to the Electric Utility fund and the Swim Pools fund.

Revenues by Source - Business Activities



Program Revenues and Expenses - Business-type Activities



CITY OF GREAT FALLS' FUND FINANCIAL ANALYSIS

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

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

As of the end of the most recent fiscal year, the City of Great Falls' governmental funds reported combined ending fund balances of \$12,468,873, a decrease of \$3,652,028 in comparison with the previous year. Approximately three-fourths of this total amount, \$8,943,679, constitutes unreserved fund balance, which is available for spending at the government's discretion. The remainder of fund balance is reserved to indicate that it is not available for new spending because it has already been committed 1) to provide required security for long-term debt obligations, \$3,399,432, or 2) to finance miscellaneous future capital projects \$125,762.

The General fund is the chief operating fund of the City of Great Falls. At the end of the most recent fiscal year, unreserved fund balance in the General fund was \$3,280,357. As a measure of the General fund's liquidity, it may be useful to compare fund balance to total fund expenditures. Fund balance represents 22 percent of total General fund expenditures, in compliance with statutory requirements.

During the most recent fiscal year, the fund balance of the City of Great Falls' General fund decreased by \$664,488. Elements of this decrease include an increase in public safety expenses and transfers to the General Capital Projects fund to fund capital improvements and to the Lewis and Clark Signature Event to fund expenses.

Proprietary funds. The City of Great Falls' proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail.

Restricted net assets of the enterprise funds totaled \$12,266,972. Unrestricted net assets of the enterprise funds totaled \$7,630,741. The total increase in net assets for the enterprise funds is \$3,052,024 primarily due to an increase in unrestricted net assets in the Water and Sewer funds.

GENERAL FUND BUDGETARY HIGHLIGHTS

Differences between the original budget and the final amended budget netted an increased budget of \$379,641. The major differences were due to a General Fund carryover of contingency and a transfer out for construction of capital improvements. During the year, revenues exceeded budgetary estimates and expenditures were less than budgetary estimates.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital assets. The City of Great Falls' investment in capital assets for its governmental and business-type activities as of June 30, 2005, is \$161,030,488, net of accumulated depreciation. This investment in capital assets includes land, buildings and structures, improvements, machinery and equipment, infrastructure and construction in progress. The total increase in the City of Great Falls' investments in capital assets for the most recent fiscal year was 6 percent (a 9 percent increase for governmental activities and a 5 percent increase for business-type activities).

City of Great Falls' Capital Assets
(net of depreciation)

| | Governmental Activities | | Business-type activities | | Total | |
|--------------------------|-------------------------|---------------|--------------------------|---------------|----------------|----------------|
| | 2004 | 2003 | 2004 | 2003 | 2004 | 2003 |
| Land | \$ 9,928,798 | \$ 9,561,296 | \$ 3,911,678 | \$ 3,732,695 | \$ 13,840,476 | \$ 13,293,991 |
| Buildings and structures | 8,343,833 | 5,483,273 | 3,753,681 | 13,057,251 | 12,097,513 | 18,540,524 |
| Improvements | 19,174,487 | 19,337,665 | 42,359,554 | 41,200,408 | 61,534,041 | 60,538,073 |
| Machinery & equipment | 4,960,793 | 4,009,981 | 13,312,704 | 3,177,207 | 18,273,496 | 7,187,188 |
| Infrastructure | - | - | 28,021,356 | 30,027,992 | 28,021,356 | 30,027,992 |
| Construction in progress | 3,493,904 | 2,531,662 | 12,585,804 | 8,163,722 | 16,079,708 | 10,695,384 |
| Total net assets | \$ 45,901,814 | \$ 40,923,877 | \$ 103,944,776 | \$ 99,359,275 | \$ 149,846,591 | \$ 140,283,152 |

Major capital asset events during the most recent fiscal year included the reconstruction of streets, water mains, sewer mains, and storm drains. The City of Great Falls is implementing the option allowed in GASB 34 to phase in the addition of the governmental infrastructure. The governmental infrastructure will be added within the next two fiscal years. Further detail on capital assets is presented in Note 6 on pages 53-54.

Long-term debt. At the end of the most recent fiscal year, the City of Great Falls had total bonded debt of \$44,963,026. Of this amount, \$2,420,000 is general obligation bonds, \$1,305,000 is special assessment debt for which the City is

obligated to pay even if the assessments on the property owners are in default up to the amount available in the Special Improvement District Revolving fund; \$5,133,978 is tax increment urban renewal bonds to be repaid from the tax increments received by the City from its downtown urban renewal area; and \$36,104,048 are bonds secured solely by specified revenue sources. Further information on long-term debt is presented in Note 8 on pages 55-65.

City of Great Falls' Outstanding Debt
General Obligation and Revenue Bonds

| | Governmental Activities | | Business-type Activities | | Total | |
|-----------------------------------|-------------------------|---------------------|--------------------------|----------------------|----------------------|----------------------|
| | 2004 | 2003 | 2004 | 2003 | 2004 | 2003 |
| Revenue bonds | \$ - | \$ - | \$ 31,067,754 | \$ 30,819,961 | \$ 31,067,754 | \$ 30,819,961 |
| General Obligation bonds | 2,500,000 | | - | | 2,500,000 | |
| Special Assessment bonds | 880,000 | 1,184,000 | - | - | 880,000 | 1,184,000 |
| Urban Renewal Tax Increment bonds | 6,095,003 | 7,044,499 | - | - | 6,095,003 | 7,044,499 |
| Total | \$ 9,475,003 | \$ 8,228,499 | \$ 31,067,754 | \$ 30,819,961 | \$ 40,542,757 | \$ 39,048,460 |

During the most recent fiscal year, the City of Great Falls' bonded debt increased by \$4,420,269 (11 percent). This is primarily due to new issuances of revenue bonds debt for the sewer fund in the amount of \$5,005,000 and of \$630,000 special assessment bonds for Special Improvement District 1301.

The City of Great Falls maintains insured ratings of "A3" from Moody's.

State statutes limit the amount of general obligation debt a governmental entity may issue to 1.51% of its total assessed valuation. The current legal debt capacity for the City of Great Falls is \$30,244,129, of which \$27,824,129 is unused by the City.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS

The unemployment rate in July 2005 for Cascade County, Montana, of which the City of Great Falls is the county seat, was 3.9 percent, which is constant with a year ago. This compares favorably with the national unemployment rate of 5.2 percent and even with the Montana unemployment rate of 3.8 percent. Increased operating costs, such as insurance and fuel prices, the priority of protecting the City of Great Falls' investment in personnel, including a commitment to providing a quality health insurance program for the employees, and slow revenue growth were considered in preparing the City of Great Falls' budget for the 2006 fiscal year.

After reviewing all the financial indicators of the City of Great Falls, the City as a whole is better as a result of the year's activities. Investments in the City's capital assets were made that as a whole made the financial situation better.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the City of Great Falls' finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Coleen Balzarini, Fiscal Services Director, PO Box 5021, Great Falls, MT 59403.