

BUFFALO FISCAL STABILITY AUTHORITY

FINANCIAL STATEMENTS

JUNE 30, 2005

BUFFALO FISCAL STABILITY AUTHORITY

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INDEPENDENT AUDITORS' REPORT

The Board of Directors
Buffalo Fiscal Stability Authority
Buffalo, New York

We have audited the accompanying financial statements of the governmental activities and each major fund of the Buffalo Fiscal Stability Authority (the Authority) as of June 30, 2005, and for the year then ended, which collectively comprise the Authority's basic financial statements as listed in the foregoing table of contents. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of the Authority as of June 30, 2005, and the respective changes in financial position 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 September 28, 2005, on our consideration of the Authority's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contract 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis preceding the financial statements is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Authority's basic financial statements. The accompanying supplementary information as listed in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements of the Authority. The accompanying supplementary information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Lumsden & McCormick, LLP

September 28, 2005

BUFFALO FISCAL STABILITY AUTHORITY

MANAGEMENT'S DISCUSSION AND ANALYSIS YEAR ENDED JUNE 30, 2005 (UNAUDITED)

Introduction

The Buffalo Fiscal Stability Authority ("BFSA", the "Authority") is a corporate governmental agency and instrumentality of the State of New York constituting a public benefit corporation created by the BFSA Act (the Act) – Chapter 122 of the Laws of 2003, as amended, signed by the Governor on July 3, 2003. BFSA has a broad range of financial control and oversight powers over the City of Buffalo (the City), the Buffalo Public School District (the School District), the Buffalo Municipal Housing Authority, the Joint Schools Construction Board, and other covered organizations as defined by the Act. Among BFSA's explicit powers is the power to issue bonds and notes for various City capital and operating purposes. The Act provides for the Authority to be in existence until its oversight, control or other responsibilities and its liabilities (including the payment in full of Authority bonds and notes) have been met or discharged, which in no event may be later than June 30, 2037. The Act provides the Authority different financial control and oversight powers depending upon whether the City's financial condition causes it to be in a "control period" (which, under the current Authority-approved financial plan, would end no earlier than the City's fiscal year ending June 30, 2012) or an "advisory period". During a control period the Authority possesses significantly expanded powers, including the power to impose a wage and/or hiring freeze. Under the Act, the Authority began its existence during a City control period, which means that the Authority commenced operation with its maximum authorized complement of financial control and oversight powers. In the event that the City's finances improve sufficiently in the future to cause the Authority to determine that an advisory period should be in effect, the Authority would operate with a reduced set of financial oversight powers and responsibilities.

The Act empowers BFSA to finance a declining percentage of the yearly deficits of the City and covered organizations which are part of an approved budget and 4-year financial plan. This power expires in fiscal year 2007.

In its capacity to issue bonds and notes on behalf of the City, the Authority has funded deficits, capital projects and certain working capital needs of the City and recently issued bonds to refund City debt. Revenues to pay Authority debt service and to fund Authority operations are provided by the City's State aid, and the City's and School District's share of Erie County sales tax, on which the Authority has a first lien. BFSA became entitled to the City's share of Erie County sales tax revenues and state aid on July 3, 2003, the effective date of the Act. BFSA became entitled to the School District's share of Erie County sales tax revenues on July 1, 2004 as provided in Chapter 86 of the Laws of 2004, which amended the Act. Pursuant to the Act, the City and the School District have no right, title or interest in these revenues until transferred to the City and the School District by the Authority. The Authority has no independent operating income or taxing power.

Overview of the Financial Statements

The annual financial statements of the Authority consist of the following components: management's discussion and analysis (this section), financial statements, and notes to the financial statements.

Management's discussion and analysis of the Authority's financial performance provides an overview of the Authority's financial activities for the fiscal year ended June 30, 2005. The overview, which covers the most important financial events of the period, should be read in conjunction with the Authority's financial statements, including the notes to the financial statements.

Government-wide financial statements of the Authority are in accordance with Governmental Accounting Standards Board ("GASB") Statement No. 34, "Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments." The government-wide financial statements use the economic resource measurement focus and accrual basis of accounting. These statements are presented to display information about the reporting entity as a whole. The statement of net assets presents information on all the Authority's assets and liabilities, with the difference between the two reported as net assets. The statement of activities presents information showing how the Authority's net assets changed during the fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of timing of the related cash flows.

Governmental fund financial statements are presented using the current financial resources measurement focus and the modified accrual basis of accounting. These statements are the *balance sheet* and the *statement of revenues, expenditures and changes in fund balance*. They recognize revenue when it becomes susceptible to accrual, which is when it becomes both measurable and available to finance expenditures in the current fiscal period.

In addition to these two types of statements, the financial statements include reconciliation between the government-wide and governmental fund statements. Accompanying notes to the financial statements are an integral part of the financial statements.

Fiduciary fund statement of net assets is used as the Authority is the fiduciary for assets that belong to the City and are held at the City's request for specific future debt service payments and future operating expenses of the Authority. The Authority is responsible for ensuring that the assets reported in these funds are used only for their intended purpose and by those to whom the assets belong. The activities have been excluded from the Authority's other financial statements.

Financial Highlights and Overall Analysis

The most critical factors in the Authority's financial position are its revenues derived from the City's sales tax revenue, (since July 3, 2003), the School District's (beginning July 1, 2004) share of Erie County sales tax revenues, and the City state aid, which together provided close to 100% of the Authority's 2005 revenue. The Act granted the Authority a first lien and perfected security interest in net collections from sales and use taxes authorized by the State and imposed by Erie County (the County). Sales taxes are imposed by the County, collected by the State and remitted to the Authority, usually several times each month. After provision for Authority debt service deposits and operating expenses, the remaining funds are remitted immediately to the City or the School District. The State legislation also provided that all state aid appropriated as local government assistance for the benefit of the City is payable to the Authority to use for debt service requirements and operating expenses, with the remaining funds to be remitted to the City.

The amount of BFSAs sales tax revenues to be collected depends upon various factors, including the economic conditions in the County, which has experienced numerous cycles of growth and recession. In addition, in the past the State has enacted amendments to the Tax Law to exempt specific goods and services from the imposition of sales tax. The Act requires the County to impose the local sales tax at a rate of no less than 3% for the period ending June 30, 2037. Pursuant to State statutory authority, Erie County currently imposes sales tax at the rate of 4 ¼%. New York State has reauthorized the additional 1% sales tax rate, in Erie County every year since January 1978 above the general State authorization, but is under no obligation to continue to do so. On June 23, 2005 Erie County received special State authorization to impose an additional ¼%. Currently neither the City nor the School District share in the additional 1 ¼% sales tax. The Authority does not make projections of sales tax revenues.

Sales tax revenue for the year ended June 30, 2005 was \$97,317,692. The Authority also received state aid for the year ended June 30, 2005 in the amount of \$137,538,408. Investment income, which accounts for the remaining Authority revenue, totaled \$1,181,302.

The other significant element in the Authority's financial position is its long-term debt. During 2004, the Authority issued \$25,745,000 long-term bonds (Series 2004A). The bonding was intended to finance the City's deficits, with \$7,811,000 transferred to the City before the end of the fiscal year as its deficit funding for fiscal year 2004 and the remaining \$19,054,000, (which included a premium on the bonds net of debt issuance costs) transferred shortly after year end as deficit financing for fiscal year ending June 30, 2005. On June 7, 2005 the Authority issued \$28,030,000 long-term bonds (Series 2005A) to finance the cost of various City of Buffalo capital projects. The City in return issued a series of its own general obligation long term bonds, privately placed with the Authority, evidencing the obligations of the City. In October 2004, the Authority issued \$84,000,000 in bond anticipation notes to cover cash flow needs of the City. The City issued \$34,000,000 of its own notes to the Authority evidencing part of this obligation. \$34,000,000 of this financing remained outstanding at June 30, 2005.

The statement of net assets shows a total net deficit of \$23,701,372. The deficit results largely from Authority debt issuance which is backed by securitization of future sales tax revenue and State aid to the City. The debt is reported as a long-term liability, but the future revenues are not reportable. In some instances, the City issues its own general obligation bonds and places them with the Authority. As of June 30, 2005, the Authority had bonds payable of \$53,775,000 and long term receivables from the City of \$28,518,898. In any year where the Authority issues more long-term debt than it retires without a corresponding issuance from the City, the deficit is likely to increase. The reconciliation on page 7 of these financial statements provides additional detail on the determination of the net deficit amount.

Cash and investments were \$13,938,179 at June 30, 2005. This amount primarily includes monies set aside for debt repayment and \$10,988,288 of 2005 State aid which has been retained by the Authority and included in the statement of fiduciary net assets, at the request of the City as a reserve to cover debt service on the 2004A deficit bonds and the Authority's operating expenses.

Operating expenses for the Authority totaled \$1,025,895 under the fund basis of accounting, which includes capital asset purchases of \$17,148 as expenditures. The Authority currently employs 7 salaried staff members.

Staff Expenses

Wages	\$435,100
Other staff related expenses	7,152
Total Direct Staff expenses	\$442,252
Staff Benefits	
NYS Employees Retirement System contribution	42,544
Payroll taxes, workers' comp and NYS disability	33,730
Health Insurance (net of employee contributions)	34,621
Total Staff Benefits	\$110,895
Total Staff Expenses	\$553,147

The next largest category of expenses was for professional fees, of which \$313,664 was legal fees and \$44,095 was for other professional consultants and advisors. Legal fees included general counsel work as well as labor and litigation expenses.

Directors of the Authority do not receive any compensation for their services but are reimbursed for any Authority-related expenses, primarily travel expense for those attending meetings from outside the Buffalo area. Lunch is provided for the Board and staff on meeting days. The following chart details expenses connected with Authority meetings and Directors' travel.

Meeting Expenses

Facilities Expenses – Public Board Meetings (9)	\$10,915
Directors' travel reimbursements	6,312
Public Forum Expenses	9,520
Total Meeting Expenses	\$26,747

Other expenses include various items necessary for the running of the Authority's offices, as follows:

Other Expenses

Office services including postage and delivery	\$5,088
Rent	32,073
Telephone and data processing	15,166
Office Supplies	4,965
Staff travel	8,110
Other	686
Total Other Expenses	\$66,143

The Authority's rental payments are made to the Buffalo Economic Renaissance Corporation, the economic development arm of the City, where they can be used toward the City's economic development efforts. As stated before, the Authority also purchased \$17,148 in capital assets, primarily telecommunications and computing equipment. Furniture of the Authority was primarily donated by New York State from used surplus furniture.

Debt Service Fund

The Authority issued its 2005A 20-year serial premium bonds in the amount of \$28,030,000 for capital projects of the City on June 2, 2005. Net interest cost of the issue was 3.93%. Issuance costs were \$474,165. The Authority issued its 2004A-1 premium Bond Anticipation Notes in the amount of \$84,000,000 in October, 2004 to finance cash flow needs of the City. A \$50,000,000 note matured on May 16, 2005 and \$34,000,000 matured on September 1, 2005. The May maturity was paid from the Authority's revenues from State aid to the City while the \$34,000,000 was paid from the proceeds of the City's Revenue Anticipation Note issued by the City and placed with the Authority. Net interest cost of the issue 1.75%. Issuance costs were \$273,235

Subsequent Events

The Authority refunded \$47,015,000 of City of Buffalo serial bonds by issuing \$46,705,000 in 14-year bonds, (the 2005B series), and \$360,000 in 2-year taxable bonds (the 2005C Series). The City of Buffalo issued its own 13 ½-year premium bonds privately placed with the Authority in the amount \$48,157,000. Net interest cost of the issue was 3.91%. Issuance costs were \$836,855. Refunding provided net cash flow savings after costs of \$1,830,000 and present value savings of \$1,596,000

The Authority issued its 2005A-1 premium Bond Anticipation Notes in the amount of \$90,000,000 on July 28, 2005 to finance cash flow needs of the City. A \$50,000,000 note matures on May 15, 2006 and a \$40,000,000 matures August 15, 2006. Both maturities are expected to be paid from the Authority's revenues from State aid to the City. Net interest cost of the issue was 2.98% and issuance costs were \$247,750.

Contacting the Authority's Financial Management

This financial report is designed to provide, taxpayers, investors, and creditors with a general overview of the Authority's finances and to demonstrate its accountability for the money it receives. If you have questions about this report or need additional financial information, contact Bertha H. Mitchell, Chief Financial Officer, Buffalo Fiscal Stability Authority, Market Arcade Building - Suite 400, 617 Main Street, Buffalo, New York 14203.

BUFFALO FISCAL STABILITY AUTHORITY

Statement of Net Assets

June 30, 2005

(With comparative totals as of June 30, 2004)

	2005	2004
Assets		
Cash and cash equivalents	\$ 152,253	\$ 19,189,081
Investments	2,797,738	-
Due from other governments	64,883,913	4,458,299
Prepaid expenses	73,503	5,924
Notes receivable - City of Buffalo	29,715,838	-
Bond issuance costs, net	1,345,513	918,889
Capital assets	74,299	57,150
Accumulated depreciation	(18,860)	(5,715)
Total assets	<u>99,024,197</u>	<u>24,623,628</u>
Liabilities		
Accounts payable	189,528	65,494
Accrued liabilities	1,584,188	67,948
Bond anticipation note payable	34,079,526	-
Retirement system payments	44,714	5,219
Due to the City of Buffalo		
Sales tax	9,901,080	4,045,577
General purpose aid	19,165,879	-
Financeable costs	-	19,054,056
Bonds payable		
Bonds due within one year	2,035,000	-
Bonds due beyond one year	55,725,654	27,783,045
Total liabilities	<u>122,725,569</u>	<u>51,021,339</u>
Net Assets		
Invested in capital assets, net of related debt	55,439	51,435
Restricted for debt service	2,797,738	-
Unrestricted	(26,554,549)	(26,449,146)
Total net assets (deficit)	<u>\$ (23,701,372)</u>	<u>\$ (26,397,711)</u>

See accompanying notes.

BUFFALO FISCAL STABILITY AUTHORITY

Statement of Activities and Changes in Net Assets

For the year ended June 30, 2005

(With comparative totals for June 30, 2004)

	2005	2004
Expenses		
General and administrative	\$ 1,342,039	\$ 940,140
Distributions to City of Buffalo - financeable costs	50,213,765	26,865,056
Distributions to City of Buffalo - general operations	146,781,580	141,251,344
Distributions to City of Buffalo School District	32,297,004	-
Interest expense	2,706,675	-
Total expenses	<u>233,341,063</u>	<u>169,056,540</u>
General revenues		
Sales tax	97,317,692	62,875,280
State aid	137,538,408	79,772,529
Interest income	1,181,302	11,020
Total general revenues	<u>236,037,402</u>	<u>142,658,829</u>
Change in net assets	2,696,339	(26,397,711)
Net assets - beginning	<u>(26,397,711)</u>	<u>-</u>
Net assets (deficit) - ending	<u>\$ (23,701,372)</u>	<u>\$ (26,397,711)</u>

BUFFALO FISCAL STABILITY AUTHORITY

Balance Sheet - Governmental Funds

June 30, 2005

(With summarized comparative totals as of June 30, 2005)

			Total	
			Governmental Funds	
	General	Debt Service	2005	2004
Assets				
Cash and cash equivalents	\$ 152,253	\$ -	\$ 152,253	\$ 19,189,081
Investments	-	2,797,738	2,797,738	-
Due from other governments	64,861,526	29,715,838	94,577,364	4,458,299
Prepaid expenses	73,503	-	73,503	5,924
Total assets	\$ 65,087,282	\$ 32,513,576	\$ 97,600,858	\$ 23,653,304
Liabilities and Fund Balances				
Accounts payable	\$ 189,528	\$ -	\$ 189,528	\$ 65,494
Accrued liabilities	860,993	-	860,993	67,948
Due to the City of Buffalo	29,066,959	-	29,066,959	23,099,633
Bond anticipation note payable	34,000,000	-	34,000,000	-
Total liabilities	64,117,480	-	64,117,480	23,233,075
Fund Balances				
Designated for debt service	-	2,797,738	2,797,738	-
Undesignated	969,802	29,715,838	30,685,640	420,229
Total fund balances	969,802	32,513,576	33,483,378	420,229
Total liabilities and fund balances	\$ 65,087,282	\$ 32,513,576	\$ 97,600,858	\$ 23,653,304

See accompanying notes.

BUFFALO FISCAL STABILITY AUTHORITY

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

June 30, 2005

Total fund balances - governmental funds **\$ 33,483,378**

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 as assets in governmental funds. The cost of the assets is \$74,299 and accumulated depreciation is \$18,860

55,439

In the government-wide statements, bond and BAN premiums are deferred and recognized ratably over the related terms of the debt. In the fund statements these amounts are recognized as revenue when received. This is the amount remaining at June 30, 2005

(57,139)

Certain liabilities, including bonds payable, are not due and payable currently and therefore are not reported as liabilities of the governmental funds. These liabilities consist of:

Bonds	57,760,654	
Accrued interest on bonds and BANS	762,690	
Accrued retirement contributions	<u>5,219</u>	(58,528,563)

Costs associated with the issuance of bonds are capitalized in the statement of net assets and are expensed in the governmental funds in the year the bonds are issued. The costs amounted to:

1,345,513

Net assets (deficit)- governmental activities **\$ (23,701,372)**

BUFFALO FISCAL STABILITY AUTHORITY

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

For the year ended June 30, 2005
(With summarized comparative totals for June 30, 2004)

	General	Debt Service	Total Governmental Funds	
			2005	2004
Revenues				
State aid	\$ 137,538,408	\$ -	\$ 137,538,408	\$ 79,772,529
Sales tax	97,317,692	-	97,317,692	62,875,280
Interest income	1,181,302	-	1,181,302	11,020
Total revenues	236,037,402	-	236,037,402	142,658,829
Expenditures				
General and administrative	914,372	-	914,372	900,857
Distributions				
City of Buffalo - financeable costs	50,213,765	-	50,213,765	26,865,056
City of Buffalo - general operations	146,781,580	-	146,781,580	141,251,344
City of Buffalo School District	32,297,004	-	32,297,004	-
Cost of bond issuance	273,235	474,165	747,400	918,889
Employee benefits	110,895	-	110,895	85,499
Debt service				
Interest	1,764,166	830,900	2,595,066	-
Total expenditures	232,355,017	1,305,065	233,660,082	170,021,645
Excess revenues (expenditures)	3,682,385	(1,305,065)	2,377,320	(27,362,816)
Other financing sources (uses)				
Operating transfers in (out), net	(3,628,700)	3,628,700	-	-
Proceeds from the issuance of bonds	-	28,030,000	28,030,000	25,745,000
Premiums on BAN/bond obligations	495,888	2,159,941	2,655,829	2,038,045
Other financing sources (uses)	(3,132,812)	33,818,641	30,685,829	27,783,045
Net change in fund balances	549,573	32,513,576	33,063,149	420,229
Fund balances - beginning	420,229	-	420,229	-
Fund balances - ending	\$ 969,802	\$ 32,513,576	\$ 33,483,378	\$ 420,229

See accompanying notes.

BUFFALO FISCAL STABILITY AUTHORITY

**Reconciliation of the Governmental Funds Statement of Revenues, Expenditures,
and Change in Fund Balances to the Statement of Activities and Changes in Net Assets**

For year ended June 30, 2005

Total net change in fund balances - governmental funds **\$ 33,063,149**

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

Capital outlays are reported in governmental funds as expenditures. However in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which equipment costs \$17,148 exceeds depreciation in the period \$13,145 4,003

Interest on long-term debt is reported as an expenditure in the governmental funds when it is paid as it requires the use of current financial resources. In the statement of activities, interest expense is recognized when it is earned. This amount represents the difference in interest expense based on the difference in beginning and end of year accrued amounts: (762,690)

In the governmental fund statements, bond proceeds and premiums are reflected as other financing sources measured by the net cash flows received and bond issuance costs are expensed as paid. In the statement of activities, bonds are reflected as a liability, bond issuance costs are capitalized and bond premiums are deferred and recognized over the life of the bonds. The following summarizes these differences:

Bond proceeds	(28,030,000)	
Bond issuance costs	747,400	
Bond and BAN premiums received in the current period	(2,655,829)	
Amortization of bond and BAN premiums	651,082	
Amortization of bond issuance costs	(320,776)	(29,608,123)

Change in net assets - governmental activities **\$ 2,696,339**

BUFFALO FISCAL STABILITY AUTHORITY

Statement of Fiduciary Net Assets

June 30, 2005

	<u>Agency</u>
Assets	
Cash and cash equivalents	<u>\$ 10,988,288</u>
Liabilities	
Due to the City of Buffalo	<u>\$ 10,988,288</u>

BUFFALO FISCAL STABILITY AUTHORITY

Notes to Basic Financial Statements

1. Summary of Significant Accounting Policies

Reporting Entity

Buffalo Fiscal Stability Authority (the Authority) is a corporate governmental agency and instrumentality of the State of New York (the State) constituting a public benefit corporation created by the Buffalo Fiscal Stability Authority Act (the Act), Chapter 122 of the Laws of 2003, as amended by Chapter 86 of the Laws of 2004 and as may be amended from time to time. Although legally separate and independent of the City of Buffalo (the City), the Authority is a component unit of the City for financial reporting purposes and, accordingly, is included in the City's financial statements.

The Authority is governed by nine directors, with seven appointed by the Governor. One of the seven must be a resident of the City. One director is appointed following the recommendation of the State Comptroller; one director is appointed on the joint recommendation of the temporary president of the Senate and the Speaker of the Assembly. The Mayor of the City and the County Executive of Erie County, New York serve as ex-officio. The Governor also designates the chairperson and vice-chairperson from among the directors.

The Authority has power under the Act to monitor and oversee the finances of the City and "covered organizations" - City of Buffalo School District (the District), the Joint Schools Construction Board, Buffalo Municipal Housing Authority, and any governmental agency, public authority, or public benefit corporation which receives money from the City. The Authority is empowered to issue bonds and notes for various City purposes, defined in the Act as "Financeable Costs." The Act authorizes the issuance of bonds, notes, or other obligations in amounts necessary to pay any financeable costs and to fund reserves to secure such bonds. The aggregate principal amounts of such bonds, notes, or other obligations outstanding at any one time can not exceed \$175,000,000. The Authority may also issue bonds, notes or other obligations to pay the cost of issuance of such borrowings, to establish debt service reserves, to refund or advance refund any outstanding notes of the City. The Authority may issue cash flow borrowings which do not count toward the above limit, but are limited to \$145,000,000 of aggregate principal amounts outstanding at any one time.

A "control period," as defined in the Act became effective as of the date of the Act and will continue until conditions have been met regarding the stability of the City's finances, but, under the current financial plan, no sooner than the fiscal year ending June 30 2012. Thereafter an advisory period commences, and the Act permits a control period to be reestablished as determined by the Directors should conditions warrant. The Act provides for the continuing existence of the Authority through June 30, 2037.

The Act provides broad monitoring responsibility over the City's finances including the requirements for the City to provide an annual financial plan for the next four years to be approved by the Authority. The Act also allows the Authority to establish a maximum level of spending, impose a wage or hiring freeze, review and approve or disapprove any collective bargaining agreement entered into by the City or covered organization, and may require the City to explore certain actions regarding merger of services with the County of Erie.

The Authority receives all sales tax revenues designated for the City and State aid to be paid to the City. State aid includes all general purpose local government aid, emergency financial assistance to certain cities, emergency financial assistance to eligible municipalities, supplemental municipal aid, and any successor or new aid appropriated by the State as local government assistance for the benefit of the City. The Authority is also entitled to receive all other aid, rents, fees, charges, payments and other income to the extent such amounts are pledged to bondholders of the City. The Authority maintains amounts it deems necessary for its operations and debt service requirements with the excess transferred to the City as frequently as practicable.

Beginning July 1, 2004, as a result of Chapter 86 of the Laws of 2004, which amended the Act that created the Authority, all sales tax revenues designated for the City of Buffalo School District are paid directly by the State Comptroller to the Authority.

Basis of Presentation

Government-wide Statements: The statement of net assets and the statement of activities and changes in net assets display financial activities of the overall Authority. These statements are required to distinguish between *governmental* and *business-type* activities. Governmental activities generally are financed through taxes, intergovernmental revenues, and other nonexchange transactions. Business-type activities are financed in whole or in part by fees charged to external parties. The Authority does not maintain any business-type activities.

The statement of activities and changes in net assets is designed to present a comparison between direct expenses and program revenues for each function of the Authority's governmental activities. Given the specific nature of the Authority's purpose, its only function is displayed as the monitoring of the City's finances.

Fund Financial Statements: The Fund financial statements provide information about the Authority's funds. The emphasis of the fund financial statements is on major governmental funds, each displayed in a separate column.

The Authority reports the following major funds:

- *General fund.* This is the Authority's primary operating fund. It accounts for all financial resources except those required to be accounted for in another fund.
- *Debt service fund.* This fund accounts for resources accumulated and payments made for principal and interest on long-term debt obligations of governmental activities on behalf of the City.

The Authority reports the following fiduciary fund:

- *Agency fund.* This fund accounts for assets held by the Authority as agent for others. The agency fund is custodial in nature and does not involve measurement of results of operations. The agency fund holds proceeds from State spin-up aid at request of the City to be used for debt service on the 2004 deficit bonds and the Authority's operating expenses.

The basic financial statements include certain prior year summarized comparative information in total but not by separate governmental activities and major funds. Such information does not include sufficient detail to constitute a presentation in conformity with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the Authority's financial statements for the year ended June 30, 2004, from which the summarized information was derived.

Basis of Accounting and Measurement Focus

The government-wide and fiduciary fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place. Nonexchange transactions, in which the Authority receives value directly without giving equal value in exchange, include State aid and sales taxes. On an accrual basis, revenue is recognized in the fiscal year for which taxes and State aid are earned or designated. Revenue from grants and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied.

Governmental funds are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized when measurable and available. The Authority considers all revenues reported in the governmental funds to be available if they are collected within sixty days after year end, with the exception of amounts determined by statute as state general purpose aid. By law, although designated for the current fiscal year the amount is paid by the State in December. In 2005, both the amount paid in December 2004 as well as the amount to be received in December 2005 have been included in State aid and distributions to the City. In subsequent years, only the amount applicable to that fiscal year will be recognized.

Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt and claims and judgments, which are recognized as expenditures to the extent that they have matured. Capital asset purchases are reported as expenditures in governmental funds. Proceeds of long-term liabilities and acquisitions under capital leases are reported as other financing sources.

Interest expense is recognized on the accrual basis in the government-wide financial statements. In the governmental fund statements, interest expenditures are recognized when funds are deposited in the debt service fund.

The Authority receives sales tax revenues several times each month, and receives interest earnings from time to time as investments mature. Funds for debt service are required to be set aside from revenues on a monthly basis, and the Authority also deducts, as necessary, amounts which in its judgment are required for Authority operations and operating reserves. Residual sales tax revenues and investment earnings are then transferred to the City.

No revenues are generated from operating activities of the Authority; therefore, all revenues are defined by the Authority as non-operating revenues. Revenues are received in the general fund and debt service fund. Expenses of the Authority that arise in the course of providing the Authority's oversight and debt issuance services, such as payroll and administrative expenses are considered operating expenses and are accounted for in the general fund. Expenditures related to debt issuance are considered non-operating expenses and are accounted for in the debt service fund.

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 amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, demand deposits and commercial paper with original maturities of three months or less.

Capital Assets

Assets are capitalized at historical cost if their value is greater than \$500 and have a useful benefit in excess of one year. Contributed assets are recorded at fair value at the time received. Depreciation is provided in the government-wide statements over estimated useful lives using the straight-line method. Maintenance and repairs are expensed as incurred, significant improvements are capitalized.

Inventory and Prepaid Expenses

The Authority holds no inventory beyond small amounts of office supplies. Prepaid expense accruals are minor and are adjusted at the close of each fiscal year.

Other Assets

Bond issuance costs are expensed and recognized in the period issued in the governmental funds. Within the government-wide statements, bond issuance costs are capitalized and amortized over the life of the related debt issue.

Bond Premiums

In the government-wide statements, proceeds from the issuance of bonds received in excess of face value (premiums) are deferred and displayed together with the bonded liability. These amounts are subsequently amortized on a straight-line basis as a component of interest expense over the life of the bond. In the fund statements, these amounts are recognized currently as other financing sources.

Equity Classifications

Government-wide statements

- *Invested in capital assets, net of related debt* - consists of net capital assets reduced by outstanding balances of any related debt obligations attributable to the acquisition, construction, or improvement of those assets.
- *Restricted net assets* – net assets are considered restricted if their use is constrained to a particular purpose. Restrictions are imposed by external organizations such as federal or state laws or buyer's of the Authority's bonds.
- *Unrestricted net assets* – consists of all other net assets that do not meet the definition of the above two components and are available for general use by the Authority.

Governmental fund statements

Designations of fund balances are established to preserve resources for future expenditures as required by bond instruments or as determined by the Authority's Board of Directors. The debt service designation is used to accumulate resources for a sinking fund in connection with the requirements of the related bond agreements.

Contributed Services

No amounts have been reflected in the financial statements for donated services. The Board of Directors serves the Authority without compensation. Additionally, certain Directors have used resources of their businesses to provide numerous hours of contributed services in the form of specialized public relations assistance and human resource matters.

2. Transactions with and on Behalf of the City

The Act and other legal documents of the Authority establish various financial relationships between the Authority, the City, and the District. The resulting financial transactions between the Authority, the City, and the District include the receipt and use of revenues as well as Authority debt issuances to fund financeable costs of the City.

The receipt and remittance of revenues in 2005 include:

- The receipt and remittance to the City of sales tax revenues. Revenues of \$97,317,692 were received, of which \$59,930,129 was or will be paid to the City and \$32,297,004 was designated for the District. The balance was retained for Authority operations and to provide for a debt service sinking fund.
- The receipt of State aid for the City of \$137,538,408, with \$56,413,408 transferred to the City. At the request of the City, \$10,988,288 is retained by the Authority in trust to be used for debt service and \$50,970,833 repaid a bond anticipation note (BAN) including interest. An additional \$19,165,879 was accrued as revenue and will be transferred to the City when it is received in December 2005.

Authority debt issuance to fund financeable costs of the City encompassed the following:

- The issuance of Series 2004A-1 in the amount of \$84,000,000 in BANs with \$50,213,765 (including allocable BAN premium) distributed to the City and \$34,439,960 (inclusive of premium) issued in the form of a revenue anticipation note (RAN) from the City. The \$50,000,000 BAN was repaid in May 2005 with State aid.
- Series 2005A bond in the amount of \$28,030,000 by the Authority for specific capital project costs of the City. The bond included a premium of \$2,159,941. The Authority received a note from the City in the amount of \$28,518,898 with \$1,196,940 allocated to the premium. The bond carries interest at 5% with payments due annually through January 15, 2025.

3. Cash and Investments

Investment policies are governed by New York State laws in accordance with the Act and as established in the Authority's written policies. Cash resources must be deposited in FDIC-insured commercial banks or trust companies located within the State. The Executive Director is authorized to use demand accounts and certificates of deposit. Permissible investments include obligations of the United States Treasury and its Agencies, repurchase agreements, obligations of State or its localities, and commercial paper of any bank or corporation provided it has the highest rating of two independent rating agencies.

Collateral is required for demand and time deposits and certificates of deposit not covered by Federal Deposit Insurance. Obligations that may be pledged as collateral are obligations of the United States and its agencies and obligations of the state and its municipalities and school districts.

Deposits at year end were covered by Federal Deposit Insurance and collateral held by the Authority's custodial banks in the Authority's name based upon the average daily funds available as determined by the banks.

The Authority's cash and investments at June 30, 2005 consist of the following:

	Carrying Value	Fair Value
Governmental activities:		
Cash	\$ 52,063	\$ 52,063
Certificates of deposit	100,190	100,190
U.S. Treasury notes	1,225,980	1,235,207
U.S. Treasury strips	280,920	280,920
GE Capital Corp. commercial paper	1,290,838	1,290,951
	<u>\$ 2,949,991</u>	<u>\$ 2,959,331</u>
Fiduciary activities:		
Savings	\$ 388,288	\$ 388,288
Certificates of deposit	10,600,000	10,600,000
	<u>\$ 10,988,288</u>	<u>\$ 10,988,288</u>

The risk and type of investments presented above generally indicate activity and positions held throughout the year. Maturities are generally short term with certificates of deposits issued with 30 day maturities and U.S. Treasuries and commercial paper due within 45 days of purchase.

4. Due from Other Governments

Due from New York State:	
May and June sales tax receipts	\$ 10,786,511
June 2005 general purpose local aid	19,165,879
Due from the City:	
RAN (7/15/2005) interest at 3.473%	34,000,000
Mirror bond (1/15/2025) interest at 5.0% inclusive of premium of \$1,196,940	29,715,838
Accrued interest	931,523

Amounts to be received from the City on the mirror bond are as follows:

Year ending June 30,	Principal	Interest
2006	\$ 787,571	\$ 883,294
2007	2,223,102	1,386,566
2008	2,282,107	1,275,411
2009	2,946,813	1,161,306
2010	3,015,278	1,013,965
2011-2015	10,149,587	3,323,132
2016-2020	5,745,113	1,232,105
2021-2025	1,369,327	212,031
	<u>\$ 28,518,898</u>	<u>\$ 10,487,810</u>

5. Capital Assets

	2005	2004
Furniture, fixtures, and computers	\$ 74,299	\$ 57,150
Accumulated depreciation	(18,860)	(5,715)
	<u>\$ 55,439</u>	<u>\$ 51,435</u>

Capital assets increased by \$17,149 in fiscal 2005 and depreciation expense was \$13,145.

6. Short-Term Debt

Aggregate BANs outstanding at June 30, 2005 amounted to \$34,000,000 and carry interest at 3.0%. In 2005 \$84,000,000 of BANs were issued and \$50,000,000 were redeemed. The BANs mature September 1, 2005 and are secured by a RAN of similar amount due from the City on July 15, 2005. The carrying amount on the accompanying statement of net assets includes the unamortized portion of a premium on the BAN of \$79,526.

7. Long-Term Liabilities

	July 1, 2004	Increases	Decreases	June 30, 2005	Due in One Year
Series 2004A Bond, maturing August 2014 with interest ranging from 4.0% to 5.25% over the life of the bond.	\$ 25,745,000	\$ -	\$ -	\$ 25,745,000	\$ 2,035,000
Series 2005A bond maturing September 2025 with interest ranging from 4.0% to 5.0% over the life of the bond.	-	28,030,000	-	28,030,000	-
	<u>\$ 25,745,000</u>	<u>\$ 28,030,000</u>	<u>\$ -</u>	<u>\$ 53,775,000</u>	<u>\$ 2,035,000</u>

The amount reflected for the bonds included on the accompanying statement of net assets includes the premiums received upon issuance, net of amortization. This difference is amortized to interest expense over the life of the bonds on a straight-line method. The difference at June 30, 2005 is \$3,985,654.

Debt service requirements:

Year ending June 30,	Principal	Interest
2006	\$ 2,035,000	\$ 1,268,700
2007	2,125,000	2,845,740
2008	4,505,000	2,405,544
2009	4,670,000	2,188,769
2010	5,450,000	1,960,649
2011-2015	25,650,000	5,779,911
2016-2020	6,660,000	1,504,520
2021-2025	2,375,000	284,469
2026	305,000	12,581
	<u>\$ 53,775,000</u>	<u>\$ 18,250,883</u>

Lease obligations:

The Authority leases its office space from a City related entity under the terms of an operating lease. Rental expense amounted to \$32,073 for the year ended June 30, 2005. Future minimum rentals to be paid for all noncancelable operating leases are:

<u>Years ending June 30,</u>	
2006	\$ 31,200
2007	28,600
	<u>\$ 59,800</u>

8. Contributions to Pension Plans

The Authority participates in the New York State and Local Employees' Retirement System (ERS), which is a cost-sharing multiple employer, public employee retirement system. ERS offers a wide range of plans and benefits which are related to years of service and final average salary, vesting of retirement benefits, death and disability. All benefits generally vest after ten years of service.

ERS provides retirement benefits as well as death and disability benefits. The New York State Retirement and Social Security Law govern obligations of employers and employees to contribute and provide benefits to employees. ERS issues a publicly available financial report that includes financial statements and required supplementary information. This report may be obtained by writing to the New York State and Local Retirement System, Gov. Alfred E. Smith State Office Building, Albany, NY 12244.

ERS requires contributions of 3% of salary except for employees who joined prior to July 27, 1976 or have greater than 10 years of service. The Comptroller annually certifies the required contribution rate expressed as a percentage of participants' wages for contributions to the pension accumulation fund. The Authority made 100% of its required contributions for the years ended June 30, 2005 and 2004. ERS expense amounted to \$42,544 and \$31,419, respectively.

9. Commitments and Contingencies

The Authority is involved in various legal proceedings, which, in the opinion of management, will not have a material adverse effect upon the financial position of the Authority. These proceedings result from the Authority being named as a party to various suits initiated by bargaining units representing many of the City's workers challenging articles of the Act relative to wage and/or hiring freezes. No damages have been specified.

10. Subsequent Event

The Authority issued \$47,065,000 Series 2005B (\$46,705,000) and 2005C (\$360,000) bonds on July 7, 2005. The bonds carry interest at 5.0% and 4.07% and are due in varying amounts beginning September 1, 2006 through 2019. The bonds are used to refund existing debt of the City.

The Authority also issued its 2005A-1 premium BANs in the amount of \$90,000,000 on July 28, 2005 to finance cash flow needs of the City. A \$50,000,000 note matures on May 15, 2006 and a \$40,000,000 matures August 15, 2006. Both maturities are expected to be paid from the Authority's revenues from State aid to the City.

BUFFALO FISCAL STABILITY AUTHORITY

Supplementary Information Schedule of Administrative Expenditures - General Fund

For the years ended June 30, 2005 and 2004

See Independent Auditors' Report

	2005	2004
General and Administrative		
Board Functions		
Public meeting expenses	\$ 10,915	\$ 13,054
Public forums	9,520	14,133
Directors travel reimbursement	6,312	12,227
	<u>26,747</u>	<u>39,414</u>
Staff expenses		
Wages	435,100	345,601
Professional development	3,064	3,403
Parking	3,479	2,491
Temporary services and related fees	609	8,607
	<u>442,252</u>	<u>360,102</u>
Central services		
Postage, printing and dues	5,088	3,459
Rent	32,073	22,140
Telephone and data processing	15,166	13,025
Repairs and maintenance	1,202	-
Insurance	631	415
Office supplies	4,965	5,246
	<u>59,125</u>	<u>44,285</u>
Administrative		
Travel	8,110	9,390
Bank fees	55	1,640
Professional fees and consultants	44,095	67,546
Legal fees	313,664	321,088
Equipment	20,324	57,392
	<u>386,248</u>	<u>457,056</u>
Total General and Administrative	<u>914,372</u>	<u>900,857</u>
Employee Benefits		
New York State Employees' Retirement System contributions	42,544	31,419
Social security and Medicare taxes	31,336	29,487
Workers' compensation and disability insurance	2,394	2,573
Medical insurance net of employee contributions	34,621	22,020
Total Employee Benefits	<u>110,895</u>	<u>85,499</u>
Total administrative expenditures - general fund	<u>\$ 1,025,267</u>	<u>\$ 986,356</u>



**Report on Internal Control over Financial Reporting and on Compliance and Other Matters
Based on an Audit of Financial Statements Performed in Accordance with *Government
Auditing Standards***

The Board of Directors
Buffalo Fiscal Stability Authority
Buffalo, New York

We have audited the financial statements of the governmental activities and each major fund of the Buffalo Fiscal Stability Authority (the Authority), as of and for the year then ended June 30, 2005, which collectively comprise the Authority's basic financial statements and have issued our report thereon dated September 28, 2005. 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.

Internal Control over Financial Reporting

In planning and performing our audit, we considered the Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

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

This report is intended solely for the information and use of the Board of Directors, management, officials of the City of Buffalo, and the Office of the State Comptroller of the State of New York. It is not intended to be and should not be used by anyone other than these specified parties.

Lumsden & McCormick, LLP

September 28, 2005



**Independent Auditor's Report on Compliance
With Investment Guidelines for Public Authorities**

The Board of Directors
Buffalo Fiscal Stability Authority
Buffalo, New York

We have audited the basic financial statements of Buffalo Fiscal Stability Authority (the Authority) as of and for the year ended June 30, 2005, and have issued our report thereon dated September 28, 2005. 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 basic financial statements are free from material misstatement.

Compliance with the *Investment Guidelines for Public Authorities* (the Guidelines) issued by the Office of the State Comptroller, State of New York and investment guidelines established by the Authority are the responsibility of the management of the Authority. As part of obtaining reasonable assurance about whether the basic financial statements are free of material misstatement, we performed tests of the Authority's compliance with the Guidelines and the Authority's own investment guidelines. However, our objective was not to provide an opinion on overall compliance with such provisions. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Board of Directors and management of the Authority and the Office of the Comptroller, State of New York. It is not intended to be and should not be used by anyone other than these specified parties.

September 28, 2005