

Letter of Transmittal

Mayor
A.J. Holloway

Council Member
George Lawrence, Ward 1
William "Bill" Stallworth, Ward 2
Charles T. Harrison Jr., Ward 3
Mike Fitzpatrick, Ward 4
Tom Wall, Ward 5
Edward "Ed" Gemmill, Ward 6
David Fayard, Ward 7



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April 20, 2011

Mayor and City Council
City of Biloxi, Mississippi

We are pleased to submit the Comprehensive Annual Financial Report of the City of Biloxi (municipal government and its component unit) for the fiscal year ended September 30, 2010. The Administration of the City of Biloxi is responsible for the information presented in this report. We believe that the accompanying information is accurate and complete and fairly presents the financial position of the municipal government of the City of Biloxi as of September 30, 2010 and results of operations for the fiscal year then ended.

Control Environment

The City's management is responsible for maintaining a system of internal controls sufficient to provide reasonable assurance that City assets are safeguarded from loss and that financial transactions are recorded timely and accurately. Reasonable assurance means that internal controls are selected or designed to reduce the risk of asset loss or inaccurate bookkeeping to an acceptable level, considering the constraint that the cost of the control should not exceed the expected benefit. Management is responsible for communicating the purpose and importance of internal controls to employees and for providing the resources necessary to establish and maintain the control system.

Budgetary Controls

Prior to the beginning of each fiscal year, each department director prepares a projection of expenditures for his department. The City's budget staff develops a projection of revenues for all funds and a projection of the expenditures not included in the departmental budgets. The revenue projections and proposed expenditures are presented to the Mayor. After reviewing the draft budget proposal, the Mayor will meet with department directors to discuss their budget requests. Each director must justify his department's budget request by explaining the cost of the programs they propose for the coming year. When the Mayor is satisfied that the proposed budget conforms to the objectives and goals he has set for the coming year, the entire budget proposal is presented to the City Council. During a series of budget workshops, the City Council will review, discuss, question and debate the proposed budget and make modifications to it. The Council will invite public comment on the taxing and spending plan at a special public hearing. After determining that the revenue projections in the budget are sound and that the proposed spending is necessary to provide the level of services and to accomplish the program goals and capital improvements proposed in the budget, the City Council will publish the proposed budget. After adopting the budget for the coming year the City Council will set the property tax rate at a level that will generate the property tax revenue necessary to raise the budgeted ad valorem tax revenue.

Mississippi law prohibits spending in excess of the budget formally adopted by the City Council and spread upon the Council's minutes. The formal budget adopted by the Council sets a limit for total expenditures for each department. For management and control purposes, a budget with greater detail is utilized by City management personnel to monitor spending. For this purpose, the total budget of each department is spread to the expenditure accounts of each department's various divisions and sections. Programmatic constraints within the City's computerized purchasing system prohibit unauthorized purchases in excess of the budget at the expenditure account level.

The City utilizes an encumbrance accounting system in monitoring spending. An encumbrance system provides for charges against the budget at the time goods or services are ordered rather than waiting until the invoice is received or the payment is made.

Independent Audit

In accordance with Section 21-35-31, Miss Code of 1972 and guidelines prescribed by the State Auditor, the financial statements presented herein have been audited by Piltz, Williams, LaRosa & Company, PA, an independent firm of Certified Public Accountants. The objective of the auditor's work is to provide the auditor with a basis upon which to express an opinion on the fairness of the City's financial statements. The auditor's opinion is included in The Financial Section of this report. The auditor's work involves examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements; assessing the accounting principles used and significant estimates made by management and evaluating the overall financial statement presentation.

State Department of Audit regulations require the independent auditor to disclose any instance of non-compliance with certain state laws, that may come to their attention during the audit of the City's financial statements. The auditor must test for non-compliance with federal requirements applicable to each major federal program under which the City of Biloxi receives federal financial assistance.

Managements Discussion and Analysis

Management's Discussion and Analysis follows the opinion of the independent auditor and provides a narrative overview and analysis of the basic financial statements.

Profile of the City of Biloxi (The Reporting Entity)

The City of Biloxi, Mississippi was incorporated in 1838. Biloxi is located in Harrison County, and its southern corporate boundary is the Gulf of Mexico. Biloxi is part of the Biloxi, Gulfport, Pascagoula Combined Statistical Area (MSA). This area has a diverse economic base which includes tourism, casino gaming, fishing, seafood processing, shipping, shipbuilding, and petroleum and chemical processing. Keesler Air Force Base, Naval Construction Battalion Center-Gulfport and Northrop Grumman Shipbuilding's Pascagoula facility are located within this Combined Statistical Area. The City of Biloxi's employees provide a full range of services to the City's citizens and visitors including planning and zoning, police and fire protection, culture and recreation, infrastructure maintenance, water and sanitation.

This report includes all funds of the City of Biloxi and any entity that management has determined to be a component unit of the City of Biloxi municipal government. Component units are entities for which the primary government (the City) is financially accountable and other entities whose relationship with the City is such that its exclusion would create misleading or incomplete financial information. The Point Cadet Development Corporation, a non-profit organization, is blended in the

financial statements of the City of Biloxi as a proprietary fund. During the fiscal year 03/04, the City of Biloxi assumed responsibility for the assets, liabilities and operation of the Biloxi Port Commission. This activity is presented as a business-type activity in the City's Government-wide financial statements and as a proprietary fund in the City's fund financial statements.

Long-Term Financial Planning

The City ended fiscal 09/10 with a General Fund balance of \$18 million which is adequate for the City. However, fund balance is not a recurring resource therefore, its use to pay recurring operating expenses cannot continue indefinitely. The City's Governing Authority initiated cost reduction measures in fiscal 08/09. In fiscal 09/10, management took additional steps to reduce costs, including employee furlough days, reduction in longevity pay, reductions in over-time and increases in employee share of health insurance costs. The City's governing authority decreased donations to social service agencies and other non-profits by 25 percent. Also, the City has decreased General Fund cash funding of capital projects. City management's goal is to equalize General Fund revenues and expenditures in fiscal 10/11.

Local Economy and Relevant Financial Policies

In response to the national economic contraction, City management initiated policies to restrict expenditures early in fiscal 08/09 including a policy of attrition and a hiring freeze. These policies were continued in fiscal 09/10.

The City has not changed its ad valorem tax rate since fiscal year 2001 when it decreased the rate by 34.8 percent. As shown in Figure 1 below, the City's ad valorem tax revenue and sales tax revenue remained about the same as in prior year while gaming tax declined slightly. In the last quarter of calendar year 2010 and the first two months of calendar 2011, the City's sales tax and gaming tax revenues showed improvement over prior year. Grant revenue in the City's Capital Projects Fund, increased significantly because of the progress the City made on federally funded, Katrina recovery projects.

The following charts disclose financial data for the City's governmental funds including the General Fund, Special Revenue, Capital Projects Funds and Debt Service Funds.

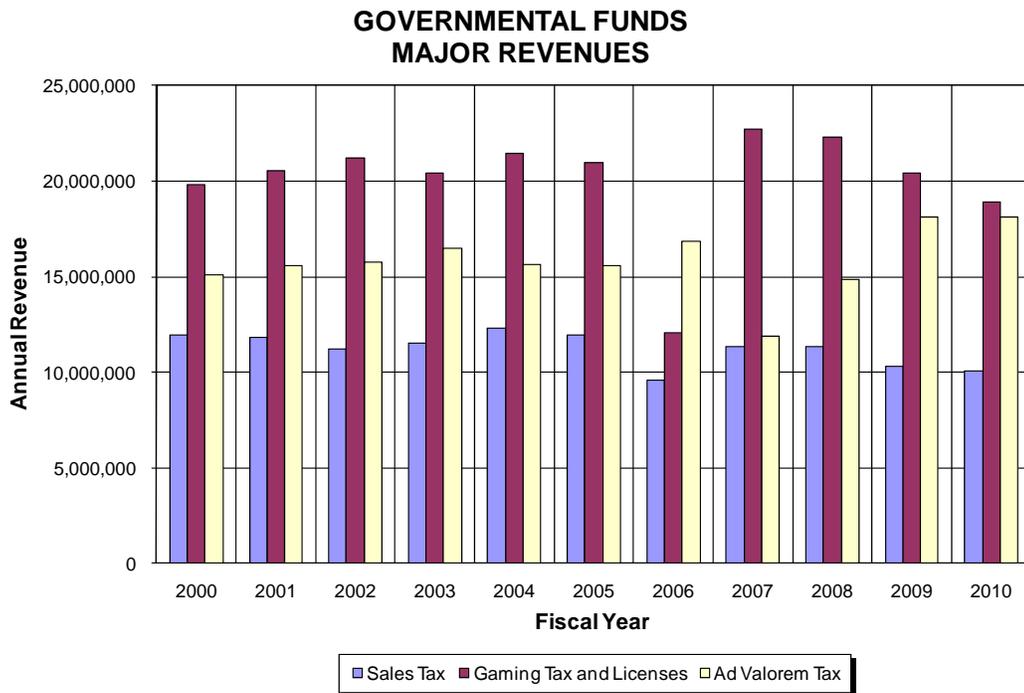


Figure 1

The amount of construction and reconstruction in fiscal 09/10 continued to decline from a post-Katrina peak in 06/07 as measured by the number and value of building permits issued. The City issued 3,686 building permits with a total valuation of \$118,553,851. (Fig. 2).

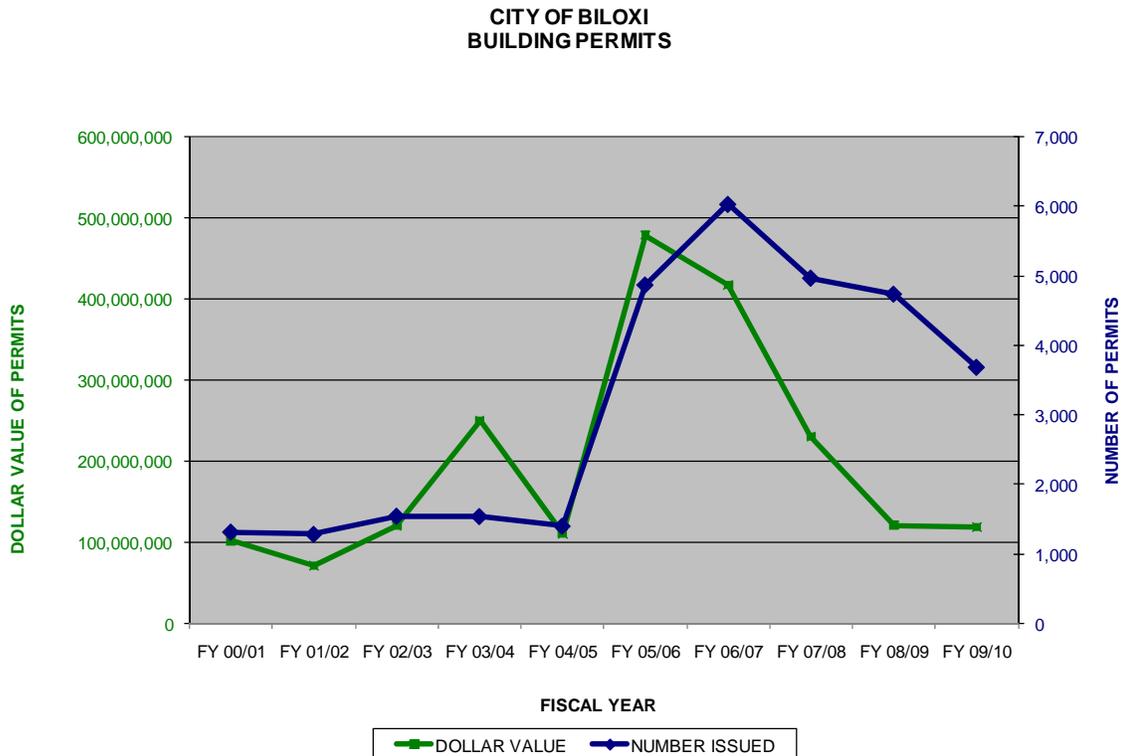


Figure 2

Governmental funds are used to account for most City functions and operations including the various City departments, the City’s two closed retirement plans, Community Development Block Grants, capital projects, and the City’s general obligation debt payments. Figure 3 illustrates the relative amounts of various general governmental revenues for the fiscal year. Usually, the City’s three largest sources of operating revenues for general governmental activities are gaming tax, ad valorem tax and sales tax. In FY 09/10 the City’s governmental funds received \$2.1 million in operating grants and \$33.9 million in capital grants for its governmental activities. The largest granting Federal departments were the Department of Homeland Security (FEMA) and the Department of Housing and Urban Development. Federal grant revenues are included in Other Intergovernmental.

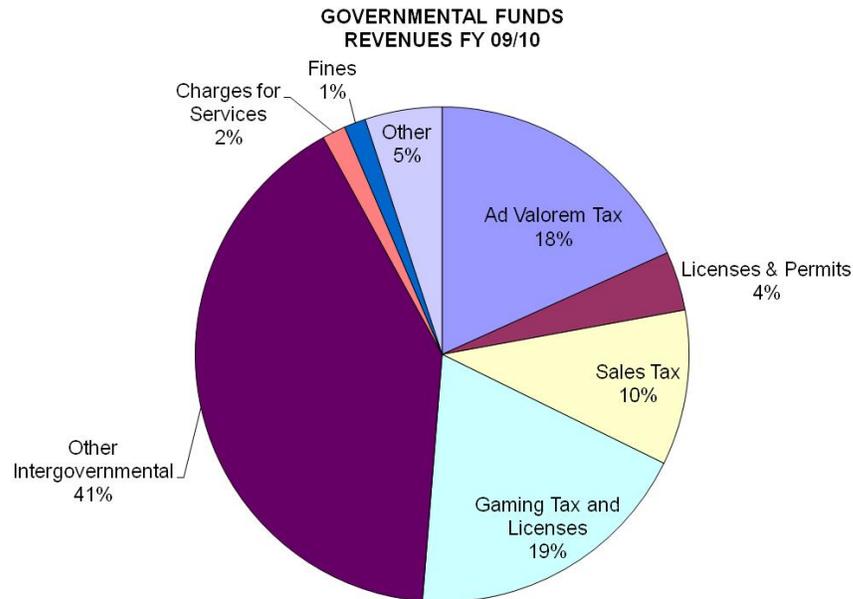


Figure 3

Gaming tax and sales tax are shown separately here but are included in the City’s governmental funds financial statements on the line titled “Intergovernmental Revenues”. Intergovernmental revenues are collected by other governmental entities such as state government and distributed to the City. Other Intergovernmental Revenue includes other taxes collected by Harrison County and the State of Mississippi and state and federal grants

Property Taxes - In Mississippi, property taxes are levied by municipalities and counties on the assessed value of land and buildings, mobile homes, automobiles, business inventory and equipment. Assessed value is a prescribed percentage of the true (appraised) value of each class of property. Classes of property and assessment ratios are defined in Section 112 of the Mississippi Constitution of 1890.

<u>Class of Property</u>	<u>Ratio</u>
Class I Single-family, owner-occupied, residential real	10%
Class II All other real property, except Class I or IV	15%
Class III Personal property, except motor vehicles and Class IV	15%
Class IV Public Utility property	30%
Class V Motor vehicles	30%

Ad valorem taxes are collected in arrears. The taxes for a calendar tax year are due by February 1 of the subsequent calendar year. Each year the governing authorities of the City of Biloxi determine the total assessed value of property situated within the City limits. Prior to the beginning of a new fiscal year, October 1, they set the tax rate (levy) that will generate the tax revenue needed for the upcoming fiscal year. In each fiscal year, the City collects the ad valorem taxes for the prior calendar tax year. To

summarize, the formula for determining tax revenues from each class of property is “Appraised value X assessment ratio X tax levy = tax amount”.

Sales Tax - State law requires sellers of goods and services to collect and remit to the state sales taxes of various rates specified in the statutes. A tax rate of 7% applies to retail sales of tangible personal property. Of the taxes collected by the state each month, 18.5% of the sales tax revenue from activities within a municipal corporation is remitted to the municipal government.

Gaming Taxes - All taxes on gross gaming revenue and gaming devices are collected by the State Tax Commission, including those taxes levied by municipalities. The Gaming control act of 1990 provided a tax of eight tenths of one percent (.8%) on casino gross gaming income. This tax revenue is divided between Harrison County and the City in the proportion of the population of each.

House Bill 1504, Regular Session of 1992 (Local and Private Legislation) provided for a tax of three and two tenths of one percent (3.2%) of gross gaming revenue. On the tenth day of each month the State Tax Commission remits the taxes collected in the previous month to the municipality to be distributed in the following ratios:

- 20% for public safety
- 20% for education purposes (Biloxi sends this 20% to the Biloxi Separate School District)
- 10% to Harrison County for public safety purposes
- 10% for educational purposes in Harrison County (This 10% is distributed to the various school districts in Harrison County in the proportion of each district student enrollment to total enrollment of all school districts in the county.)

House Bill 1504 also provided for a licensing fee of \$150, annually, for each gaming device. In addition to local taxes, the Mississippi Gaming Control Act, codified in chapter 76, in title 75 of the Mississippi Code of 1972, provides that casinos pay a fee of 8% of gross gaming revenue to the State of Mississippi.

Figure 4 illustrates the trends in annual totals of revenue sources for the City’s governmental funds. Casino gaming and the resulting gaming taxes were implemented in 1992, and since that time, gaming tax revenues have become the largest, regular revenue source for the City. Note that Other Intergovernmental Revenue increased significantly in fiscal year 05/06 due to grants for Hurricane Katrina debris removal received by the City of Biloxi from the Department of Homeland Security, Federal Emergency Management Agency.

GOVERNMENTAL FUNDS REVENUE TRENDS

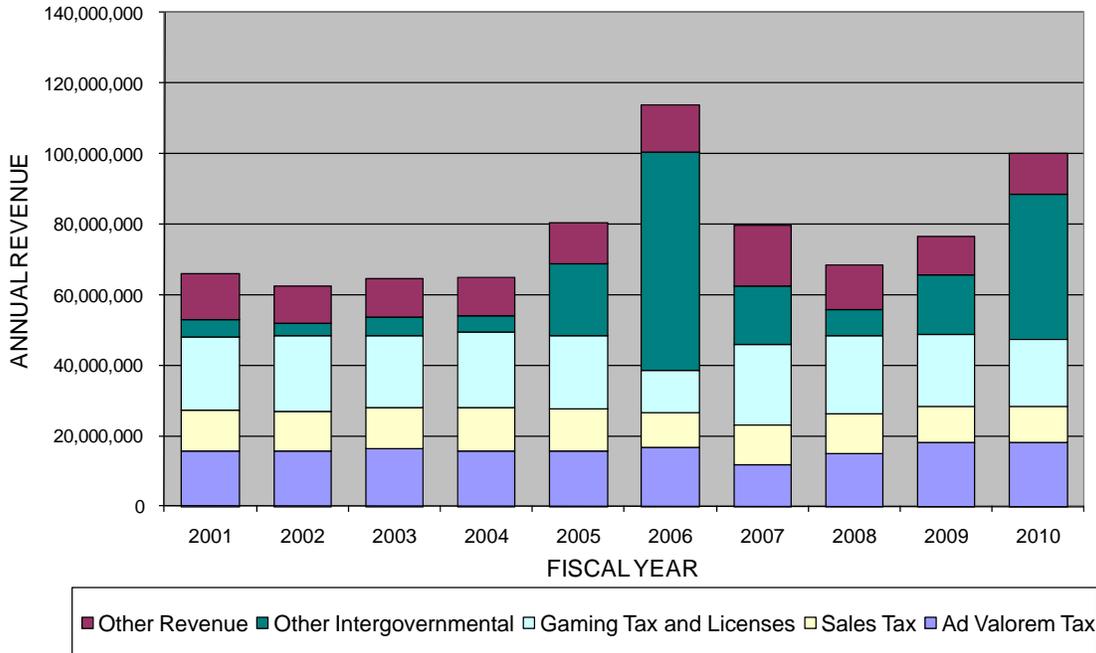


Figure 4

General Governmental Expenditures

Figure 5 illustrates the trends in spending for the various services and functions accounted for in the City’s governmental funds. Normally, public safety and capital projects are the largest expenditure categories of the City’s governmental funds. In FY 05/06 expenditures for Public Works increased due to the cost of removing debris left by Hurricane Katrina and capital project spending was curtailed. Debris removal costs were completed in FY 06/07.

GOVERNMENTAL FUNDS EXPENDITURE TRENDS

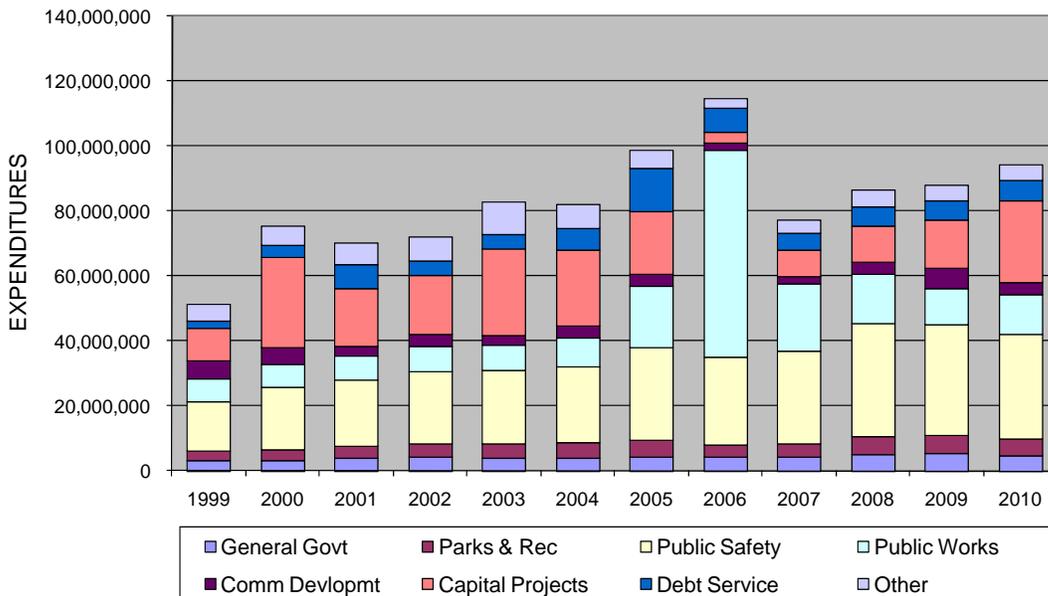


Figure 5

Water and Sewer Fund

The City of Biloxi provides water production and distribution and sewer collection and treatment services. The City accounts for the cost of these services and related revenues in an enterprise fund. The City's goal is to pay the cost of the services with the revenue generated by billing customers for their use of the service. In 2005 the City lost approximately twelve percent of its customer base to the destruction of Hurricane Katrina.

A large portion of the cost of water/sewer service is the City's share of the debt service of the Harrison County Utility Authority, which provides sewer treatment service. Because the debt service is a "fixed" cost (does not vary due to the number of customers served) the City's rates, applied to the consumption of the reduced number of customers, did not generate revenue sufficient to cover the cost of services. Although the City's Water and Sewer Fund incurred an operating loss of \$3.7 million for fiscal 09/10, the net, unrestricted assets of the fund increased by \$11 million. The increase in net, unrestricted assets was due to cancellation of the Special Community Disaster Loan and transfers from the City's General Fund and Capital Projects Fund. The City increased water and sewer rates at the end of fiscal year 08/09 and again at the end of 09/10. City management believes that the increased rates will produce revenue adequate to cover system costs in fiscal 10/11. The City's governing authority has committed to annual cost and rate adjustments in order to reach and maintain 100 percent cost recovery.

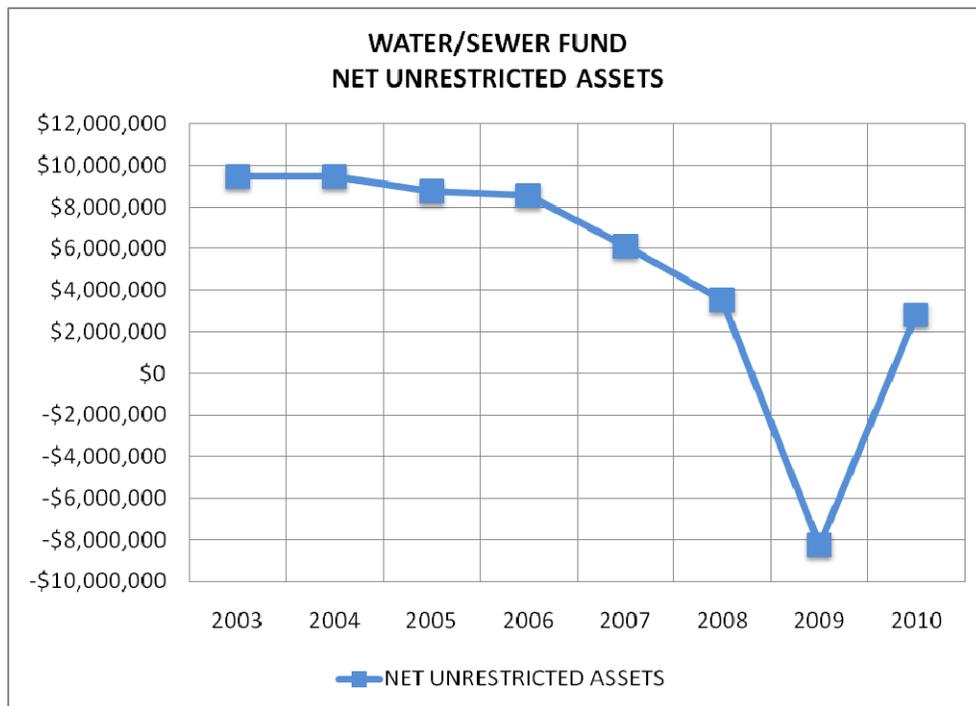


Figure 6

Major Initiatives

The Federal Emergency Management Agency has obligated \$513,321,140 of grant funding for Hurricane Katrina recovery in the City of Biloxi. The City has allocated \$24,111,221 of insurance proceeds toward this work which will cost an estimated \$537,432,361. Approximately \$363,929,485 of this cost is related to water, sewer and drainage infrastructure repairs. The City has hired HNTB Corporation to manage the infrastructure repair program. City management is cognizant of the fact that this amount of capital outlay, financed with federal funding, will require significant attention over the next few years. City management believes that this federally funded investment will significantly improve the City's infrastructure and provide future operating and maintenance cost savings.

Respectfully submitted,



David Staehling, Director of Administration



W. L. Lanham, Controller

Management's Discussion and Analysis

City of Biloxi, Mississippi

Management's Discussion and Analysis

Brief Discussion of the Basic Financial Statements

The City's management has prepared this discussion and analysis to provide an objective analysis of the City's financial activities and financial condition as presented in the basic financial statements which form a part of the City's Comprehensive Annual Financial Report (CAFR). The basic financial statements are presented in three parts: government-wide financial statements, fund financial statements and the notes to financial statements.

Government-wide financial statements focus on the overall financial position and activities of the City, in total, rather than the City's individual funds. In these statements, all governmental activities are consolidated into a column and all business-type activities are consolidated into a column. The two columns are added to present a total for the City as a whole. These statements include the Statement of Net Assets which discloses all of the City's assets and liabilities and the difference which is titled "net assets". Also included is the Statement of Activities which focuses on the cost of services provided and activities performed by the City and the source of money used to pay for the services and activities. The Statement of Activities also explains how the City's net assets increased or decreased during the fiscal year. Both of the government-wide financial statements segregate functions of the City that are supported by taxes and intergovernmental revenues (governmental activities) from those functions that are mainly supported through charges to the consumer (business-type activities). The City's water and sewer utilities and the City's port operations are business-type activities. The government-wide financial statements present information for both governmental funds and proprietary funds on the accrual basis of accounting.

Fund financial statements follow the government-wide statements. These statements present the balance sheets and the statement of revenues, expenditures and changes in fund balance of the City's funds. The fund financial statements present governmental funds on the modified accrual basis of accounting. Some examples of the differences between the government-wide financial statements and the governmental fund financial statements, inherent in the differences in the basis of accounting are:

Under the modified accrual basis of accounting, capital outlays are expenditures of resources with no offsetting capital asset increase because capital assets are not shown on the balance sheet.

Principal payments on long-term debt are reported as expenditures with no offsetting reduction of liabilities because long-term liabilities are not show on the balance sheet.

The proceeds of debt borrowing is reported as an increase (inflow) of expendable resources with no offsetting increase in liabilities.

A fund is a fiscal and accounting entity with a balanced set of accounts for recording and disclosing the reporting entity’s stewardship of resources received and segregated for specific activities including the amount of resources received, the amount expended, liabilities owed and the residual balance (equity) of the funds. The City uses funds to segregate resources and resource use according to the purpose for which the resources were segregated. The objective of fund accounting is to demonstrate compliance with budgetary and legal requirements that apply to the resources segregated in each fund.

In the fund financial statements, each of the City’s major funds is presented in a separate column. The City’s non-major funds are combined and the totals presented in one column. The distinction between governmental type activities and proprietary type activities is maintained through the presentation of separate statements for these two types of funds.

Governmental funds are used to account for governmental functions of the City of Biloxi including administration, executive, legislative, legal (general governmental activities), public safety, public works, parks and recreation, public health and welfare, capital projects and debt service. These are the functions that are presented as “Governmental Activities” in the government-wide financial statements. Presentation of financial information for the City’s governmental funds differs from the information presented in the government-wide financial statements because the focus of fund accounting is on near-term inflows and outflows of spendable resources and the balances of spendable resources available at year-end.

Proprietary funds include enterprise funds and internal service funds. Enterprise funds are used for those activities which are financed, primarily, by charges to users and customers. Internal service funds are used for city activities that provide goods or services for the City’s various funds and departments such as the City’s Self Insurance Fund. In the government-wide financial statements these activities are called “business-type activities”.

Notes to the Financial Statements provide additional information to explain the data presented in the basic financial statements.

Government-wide Condensed Data – Governmental and Business-type Activities

Table 1
City of Biloxi
Net Assets

	Governmental Activities		Business-Type Activities		Total Primary Government	
	2010	2009	2010	2009	2010	2009
Current and other assets	\$ 76,205,339	\$ 80,131,738	\$ 5,485,834	\$ 7,946,104	\$ 81,691,173	\$ 88,077,842
Capital assets	241,005,613 [▼]	220,489,214	73,480,630	64,772,510 [▼]	314,486,243	285,261,724
Total assets	<u>\$317,210,952</u>	<u>\$ 300,620,952</u>	<u>\$ 78,966,464</u>	<u>\$ 72,718,614</u>	<u>\$ 396,177,416</u>	<u>\$ 373,339,566</u>
Current & other liabilities	\$ 23,759,834	\$ 13,131,034 [▼]	\$ 2,483,194 [▼]	\$ 15,682,987	\$ 26,243,028	\$ 28,814,021
Long-term liabilities	70,383,395	70,220,094 [▼]	2,644,037	5,717,484 [▼]	73,027,432	75,937,578
Total liabilities	<u>94,143,229</u>	<u>83,351,128</u>	<u>5,127,231</u>	<u>21,400,471</u>	<u>99,270,460</u>	<u>104,751,599</u>
Net assets						
Investment in capital assets						
net of related debt	182,350,760	162,209,803	70,719,525	61,716,508	253,070,285	223,926,311
Restricted	30,767,976	35,399,734	1,117,520	1,105,935	31,885,496	36,505,669
Unrestricted	9,948,987	19,660,287	2,002,188	(11,504,300)	11,951,175	8,155,987
Total net assets	<u>\$223,067,723</u>	<u>\$ 217,269,824</u>	<u>\$ 73,839,233</u>	<u>\$ 51,318,143</u>	<u>\$ 296,906,956</u>	<u>\$ 268,587,967</u>

Table 2
City of Biloxi
Changes in Net Assets

	Governmental Activities		Business-Type Activities		Total Primary Government	
	2010	2009	2010	2009	2010	2009
Revenues						
Program revenues						
Charges for services	\$ 7,851,945	\$ 7,571,286	\$ 11,352,878	\$ 9,015,436	\$ 19,204,823	\$ 16,586,722
Operating grants	2,180,921	4,311,030	3,085,487	-	5,266,408	4,311,030
Capital grants and contributions	33,925,142	9,135,507	202,226	1,379,466	34,127,368	10,514,973
General revenues						
Property taxes	18,148,452	18,125,894	219,590	209,134	18,368,042	18,335,028
Sales taxes	10,012,878	10,309,316	-	-	10,012,878	10,309,316
Gaming taxes	18,902,497	19,631,434	-	-	18,902,497	19,631,434
Franchise taxes	3,040,417	3,095,826	-	-	3,040,417	3,095,826
Other revenue	5,400,672	7,380,116	22,430	46,799	5,423,102	7,426,915
Total revenues	99,462,924	79,560,409	14,882,611	10,650,835	114,345,535	90,211,244
Expenses						
General government	5,293,011	6,289,441	-	-	5,293,011	6,289,441
Parks and recreation	5,456,041	5,892,707	-	-	5,456,041	5,892,707
Public safety	36,873,912	39,554,918	-	-	36,873,912	39,554,918
Public works	12,577,626	12,174,671	-	-	12,577,626	12,174,671
Community development	4,810,435	7,633,964	-	-	4,810,435	7,633,964
Unallocated depreciation	2,583,406	2,355,172	-	-	2,583,406	2,355,172
Interest on long-term debt	2,740,362	2,750,274	-	-	2,740,362	2,750,274
Water and sewer service	-	-	14,080,437	13,064,569	14,080,437	13,064,569
Port Fund activities	-	-	1,611,282	1,594,012	1,611,282	1,594,012
PCDC activities	-	-	34	471	34	471
Total expenses	70,334,793	76,651,147	15,691,753	14,659,052	86,026,546	91,310,199
Increase (decrease) in net assets						
before transfers	29,128,131	2,909,262	(809,142)	(4,008,217)	28,318,989	(1,098,955)
Transfers	(23,330,232)	3,419,459	23,330,232	(702,459)	-	2,717,000
Net increase (decrease) in net assets	5,797,899	6,328,721	22,521,090	(4,710,676)	28,318,989	1,618,045
Net assets, beginning of year	217,269,824	210,941,103	51,318,143	56,028,819	268,587,967	266,969,922
Net assets, end of year	\$ 223,067,723	\$ 217,269,824	\$ 73,839,233	\$ 51,318,143	\$ 296,906,956	\$ 268,587,967

Overall Financial Position and Results of Operations

The net assets of governmental activities increased by \$5.8 million while the fund balances of governmental funds decreased by \$12.6 million. The positive change in net assets is reconciled to the decrease in fund balances of governmental funds in the schedule titled Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balances of Governmental Funds to the Statement of Activities. One major reconciling item is capital expenditures which decrease fund balance in the governmental fund financial statements. These capital expenditures are reported as increases in capital assets in the Statement of Net Assets rather than as an expense on the statement of Changes in Net Assets.

The net assets of business-type activities (Water and Sewer Fund and Port Fund) increased by \$22.5 million during FY 09/10. The increase was due to transfers from the City's General Fund and Capital Projects Fund and cancellation of the Water and Sewer Fund's Special Community Disaster loan from the Federal Emergency Management Agency. Water and Sewer Fund revenues were not adequate, under the existing rate structure and with the realized consumption quantities, to cover operating costs and depreciation. At the end of fiscal 08/09 and again at the end of 09/10, the City of Biloxi governing authority increased water and sewer billing rates. With the increase effective for FY 10/11, City management expects water and sewer rates to be adequate to pay the costs of water and sewer utility services.

Analysis of Significant Balances and Operation of Individual Funds

Fund Balances

General Fund – The General Fund is the City's primary operating fund. The City began fiscal year 09/10 with a General Fund balance of \$27.4 million and ended the year with a fund balance of \$18.1

million. The decrease of \$9.3 million is attributable to deficit spending, capital project and debt service funding. For the last three fiscal years, 07/08, 08/09 and 09/10, the governing authority budgeted spending that exceeded projected revenues. In these three fiscal years, the City has drawn down the General Fund balance by \$39 million. Approximately \$24.8 million of the three year draw down is attributable to deficit spending in the City's General Fund.

Debt Service Fund – The Special Community Disaster Loans are operating loans the City received from the Federal Emergency Management Agency (FEMA), Department of Homeland Security. The loans totaled \$13.7 million. The City's General Fund borrowed \$11 million and the City's Water and Sewer Enterprise Fund borrowed \$2,787,113. The money was borrowed in fiscal years ending in 2006 and 2007 to pay operating costs following Hurricane Katrina. The Special Community Disaster Loans were for a period of 5 years and with possible extension for another five years. The City requested and received a five year extension of the \$11 million loan to the General Fund. The City requested and received cancellation of the \$2,787,113 loan to the Water and Sewer Enterprise Fund. The City has accumulated \$6.9 million in its Debt Service Fund to repay the General Fund loan.

The remaining fund balance in the City's debt service funds is required to pay principal and interest maturities due at the beginning of each fiscal year before ad valorem tax revenues collections for the year are sufficient to cover debt service for the year. Ad valorem tax revenue is the primary resource of the Debt Service Fund for payment of interest and principal.

Water and Sewer Fund – Revenues and other Water and Sewer Fund resources have not been not adequate to pay the cost of operations. The Water and Sewer Fund incurred an operating loss of \$3.7 million including depreciation expense of \$2.2 million. The City's water and sewer rates were relatively low compared to other service providers in Mississippi. The loss of a significant number of utility customers due to destruction of residences and businesses by Hurricane Katrina further exacerbated this problem. At the end of fiscal 08/09 the Governing Authority increased water and sewer rates by approximately 150 percent and again increased rates at the end of FY 09/10. The City's governing authority believes that the rate increases will provide sufficient revenue to stabilize the Water and Sewer Fund in future fiscal years.

General Capital Projects Fund – The General Capital Projects Fund holds bond proceeds and insurance claim proceeds which will be expended as projects progress. The decline in fund balance of the General Capital Projects Fund resulted from expenditure of these resources.

Budget Variances in the General Fund

The Basic Financial Statements include a budget to actual comparison for the City's General Fund revenues and expenditures. The comparison is made on the cash basis which differs from modified accrual because receivables and payables are not recognized. An explanation of the budget basis is provided in Note II.A. For FY 09/10 the City's governing authority originally budgeted a reduction in the City's General Fund, budget basis fund balance of \$13.3 million. At year-end, the actual reduction was \$9.9 million. The City's General Fund, budget basis fund balance fell from \$21.5 million to \$11.6 million. Revenues of the City's General Fund were below expectations by \$6.9 million. \$4 million of the negative variance in revenue was due to Federal Katrina grants that were not expended and drawn down. City management was able to keep actual expenditures below the budgeted expenditures by \$9.2 million. The net transfers-out was below budget by \$2.8 million. During the year the City Council amended the budget, primarily, for grant awards and related expenditures.

Capital Assets Activity

During FY 09/10 the City increased its investment in capital assets for governmental activities by \$20.5 million, net of dispositions and depreciation. For business type activities (Water/Sewer and Port) the City increased its investment in capital assets by \$8.7 million after dispositions and depreciation. Most of the additions were for construction of facilities and infrastructure. Much of the City's capital outlay was financed by FEMA grants. See Detail Note III. F, for additional information concerning capital asset activity for the fiscal year ended September 30, 2010.

Long-Term Debt

At the beginning of the fiscal year the City of Biloxi had outstanding debt consisting of general obligation bonds, notes, limited obligation bonds and notes, and pollution control loans. These outstanding debts totaled \$75,122,236 at the beginning of the fiscal year 09/10. During the fiscal year 09/10, the City paid \$4,419,119 of principal and paid \$2,514,502 of interest on all debt. \$2,787,113 of Special Community Disaster Loan principal was cancelled by the Federal Emergency Management Agency. The City borrowed \$4,500,000 from the Mississippi Development Bank to fund capital project spending. So, total outstanding debt decreased by \$2,706,567 in fiscal 09/10. In the Supplemental Information section of the financial report is a schedule titled Schedule of Long-Term Debt which discloses the beginning balances of each debt, new debt incurred and the principal amount paid during the year.

State laws limit the amount of debt a municipality may incur. General obligation bonded debt, excluding debt issued for utility purposes, is limited to 15% of assessed valuation. All debt, excluding utility revenue debt and tax increment financing bonds, is subject to a limit of 20% of assessed value. Note III. H discloses the City's compliance with statutory debt limitations.

Credit Rating

When a governmental entity issues bonds, it may obtain a rating from one or more of the bond rating agencies. The rating is a measure of the issuer's ability to repay the debt and provides a means whereby investors may measure the risk of their investment in the bonds.

On May 21, 2010, Standard & Poor's Rating Services raised its standard long-term rating from BBB+ to AA- with a stable outlook. Standard & Poor's Rating Services' rationale was based on:

- Historically very strong financial reserves that allowed it to absorb the loss of revenues associated with the impact of Hurricane Katrina;
- Stable tax base; and
- Moderate overall debt burden.

On August 11, 2006 Moody's Investors Service announced that they "affirmed the City of Biloxi's general obligation rating of "Baa1" with a stable outlook." Prior to Hurricane Katrina, Moody's Investors Service rated the City's debt "A2". See Detail Note III. H and the Supplementary Information section of the CAFR for additional information concerning the City's debt. The City's credit ratings have not been reviewed or changed since the above ratings by Standard and Poor's Ratings Services and Moody's Investors Service. The City of Biloxi \$34,020,000 Tax Increment Limited Obligation Refunding Bond, Series 2006A and B, issued during FY 06/07 were not rated.

Contact Information

Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Controller, William L. Lanham, City of Biloxi, P.O. Box 429, Biloxi, MS 39533.