

YELLOWSTONE COUNTY, MONTANA
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)
JUNE 30, 2006

As financial management of Yellowstone County, Montana, we offer readers of the attached financial statements this narrative overview and analysis of the financial activities of Yellowstone County for the fiscal year ended June 30, 2006 and the financial position as of June 30, 2006. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our letter of transmittal, which precedes this report.

Financial Highlights

- The general fund incurred a net change to fund balance of \$417,151. The ascent of short term interest rates resulted in interest collections exceeding budget by \$257,582. Clerk and recorder document filing fees stayed stronger than expected with this revenue source exceeding budget by \$206,958. The phone system fund was able to return \$130,000 to the general fund, which was transferred from the general fund to the phone fund in prior years. As a result of these revenues and savings in appropriations the general fund was also able to transfer \$330,000 to Metra in operational funding assistance to enhance Metra's financial position.
- The property and liability insurance fund incurred a gain of \$122,276 during FY06. In FY05, the County was able to acquire a reinsurance policy for general liability that was financially similar to previous policies (see footnote #9) in terms of price and coverage levels through a new carrier. The liability and property insurance fund has a fund balance of \$2,137,448, which is anticipated to be sufficient to provide for defense and settlement costs of known existing claims; however, there is a need for reasonable tort reform and employer liability protections.
- The capital improvement fund had a decrease to fund balance of (\$180,790). The decrease was primarily a result of the delivery of the new motor graders and bridge replacement projects.
- METRA's overall financial position continued to decline during FY06 as a result of a shortfall in revenues designated for capital replacement, financing, and maintenance funding failing to meet those needs. Revenues dedicated for funding depreciation, capital maintenance costs, and capital financing were 33.3% of the amount necessary to offset those costs. Metra's unrestricted net assets were \$517,017 on June 30, 2006. The operating fund was assisted by \$330,000 of non-recurring transfers from the general fund in FY06. The FY07 Metra operations budget is projected to improve the net assets for operations as well as provide for some funding for capital needs. Recent management decisions are expected to improve the results of operations in FY07. Hopefully, improved operations will allow for improvement in the operations reserve and provide additional funding for capital, although capital needs still are expected to exceed anticipated revenue streams by a significant margin.

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Explanation of the Financial Statements

The MD&A is intended to serve as an introduction to the basic financial statements of Yellowstone County. The basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other unaudited supplementary information in addition to the basic financial statements.

Government-wide financial statements. The Government-wide financial statements are designed to provide readers with a broad overview of Yellowstone County's finances, in a manner similar to a private sector business on a full accrual accounting basis.

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

The statement of activities presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (example: uncollected property taxes, and earned but unused vacation leave).

Both of the government-wide financial statements distinguish functions of Yellowstone County that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs from user fees and charges (business-type activities). The governmental activities of Yellowstone County include general government, public safety, public works (roads and bridges), public health, social and economic programs, cultural and recreational programs, conservation of natural resources, and community/economic development. The business-type activities include refuse disposal and METRA civic center.

The government-wide financial statements can be found on pages 20-22 of this report.

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

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

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

Yellowstone County maintains many individual governmental funds. The general fund, road fund, property and liability insurance fund, public safety-sheriff fund, RSID Bond Fund, and capital improvement fund are all reported as major funds. Information for the major funds is reported separately in the governmental fund balance sheet and in the governmental fund of revenues, expenditures, and changes in fund balances. Each of the major funds also reports the revenues and expenditures on a comparative basis with the annually appropriated budget both original and revised to demonstrate compliance with this budget. The remaining governmental funds are combined in a single aggregate presentation titled other nonmajor governmental funds. Individual fund reports for each of the nonmajor governmental funds are presented in the combining financial statements in this report.

The basic governmental fund financial statements can be found on pages 23-29 of this report.

Proprietary funds. Yellowstone County maintains two different types of proprietary funds. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. Yellowstone County uses enterprise funds to account for operations of the refuse disposal fund and METRA civic center both of which are reported as major funds. Internal service funds are used to accumulate and allocate costs internally among various government department users or affiliated organizations. The three internal service funds utilized by the county include the health insurance fund, motor pool, and telephone fund. Because these services predominately benefit governmental rather than business-type functions, they have been

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included within the governmental activities in the government-wide financial statements. Interdepartmental charges for internal service funds have been eliminated from the Statement of Activities.

Proprietary funds are reported in the same way that all activities are reported in the statement of net assets and the statement of activities, but provide more detail in addition to a cash flow statement. Internal service funds are combined into a single aggregated presentation in the proprietary fund financial statements. Individual fund statements for the internal service funds are presented in the combining statements in this report.

The basic proprietary fund financial statements can be found on pages 30-34 of this report.

Fiduciary funds. Fiduciary funds are used to account for resources held for the benefit of parties and entities outside the government of Yellowstone County. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support Yellowstone County's own programs.

The basic fiduciary fund financial statements can be found on pages 35-36 of this report.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data and reports presented in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 37-61 of this report.

Required supplementary information. All required supplementary information precedes the basic financial statements or is included in the basic financial statements and accompanying notes, therefore no other information is presented in the section for required supplementary information.

Government-wide Financial Analysis.

Net assets may serve as a useful indicator of a government's financial position, which is one of the reasons why the Governmental Accounting Standards Board (GASB) instituted GASB Statement #34 and required local governments to present net asset information. Yellowstone County's net assets (assets less liabilities) were \$55,096,848 for the year ended June 30, 2006. The change to net assets for governmental and business-type activities for the fiscal year ended June 30, 2006 was \$3,241,734. These figures do not include retroactive infrastructure capital assets, which have not been incorporated into the County's reports for fiscal year 2006.

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Of the County's yearend total net assets of \$55,096,848, capital assets net of the related debt accounted for \$33,910,162 or 61.5% of total net assets. Capital assets reflect the large investments in facilities and equipment that are necessary to provide large scale programs and services for the community. The restricted net assets (\$640,467 or 1.2%) are those funds legally required to be used for debt service payments. Unrestricted net assets of \$20,546,219 account for 37.3% of the total net assets. Unrestricted unreserved net assets are primarily used as reserves that are used for cash flow purposes in between property tax collections, which are due in 50% installments on November 30 and May 31 of each year, and as reserves to provide against large unforeseen costs or events. A comparison of the County's net assets follows:

Yellowstone County Capital Assets
(net of accumulated depreciation)

| | Governmental Activities | | Business Activities | | Total | |
|--|-------------------------|----------------------------|----------------------|----------------------------|----------------------|----------------------------|
| | 2005 | 2006 | 2005 | 2006 | 2005 | 2006 |
| Current assets | \$ 28,210,569 | \$ 30,150,690 | \$ 1,726,369 | \$ 2,199,621 | \$ 29,936,938 | \$ 32,350,311 |
| Noncurrent assets | 1,271,363 | 1,122,423 | 0 | 0 | 1,271,363 | 1,122,423 |
| Capital assets | 21,481,087 | 22,360,602 | 12,773,081 | 12,189,962 | 34,254,168 | 34,550,564 |
| Total assets | 50,963,019 | 53,633,715 | 14,499,450 | 14,389,583 | 65,462,469 | 68,023,298 |
| Current liabilities | 4,273,980 | 4,291,775 | 411,695 | 774,294 | 4,685,675 | 5,066,069 |
| Noncurrent liabilities | 8,397,113 | 7,441,695 | 524,567 | 418,686 | 8,921,680 | 7,860,381 |
| Total liabilities | 12,671,093 | 11,733,470 | 936,262 | 1,192,980 | 13,607,355 | 12,926,450 |
| Net assets: | | | | | | |
| Invested in capital assets, net of related debt | 21,388,592 | 22,114,187 | 12,276,806 | 11,795,975 | 33,665,398 | 33,910,162 |
| Restricted for debt service | 792,684 | 640,467 | 0 | 0 | 792,684 | 640,467 |
| Unrestricted | 16,110,650 | 19,145,591 | 1,286,382 | 1,400,628 | 17,397,032 | 20,546,219 |
| Total net assets | \$ 38,291,926 | \$ 41,900,245 | \$ 13,563,188 | \$ 13,196,603 | \$ 51,855,114 | \$ 55,096,848 |
| Change in net assets | | <u>\$ 3,608,319</u> | | <u>\$ (366,585)</u> | | <u>\$ 3,241,734</u> |

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The decrease in net assets for business-type activities was primarily a result of METRA's operations and the associated depreciation of \$810,227 on the capital intensive facilities. The unrestricted portion of net assets for business-type activities related to METRA is \$517,017, which is an increase of \$200,349 from FY05. Unrestricted net assets of \$380,056 or 73.5% is currently reserved for capital maintenance and replacement at Metra.

The ending net asset position of the Interest on Long-Term Debt category on the Statement of Activities is a result of the related assets being donated to a business-type activity (METRA buildings and grounds improvements funded with general obligation debt). The negative net asset position will be funded in future years with taxing authority previously approved by local residents.

Governmental activities.

Of the County's \$40.6 million in expenses for governmental activities, \$14.0 million (34.3%) was funded with program revenues. The balance of funding came from general revenues, which is primarily property tax revenue (74.4% of the general revenues for governmental activities), or use of reserves. The major sources of program revenues (and change from prior year) include:

- State District Court Reimbursement Program \$1,355,770 / (+\$144,399)
- Gas tax \$274,846 / (-\$11,634)
- Justice Court fines \$663,734 / (+\$14,617)
- Clerk & Recorder filing fees \$1,305,319 / (+\$242,985)
- Health insurance premiums less County funded premium for employees \$2,282,283 / (+\$358,962)
- Adult detention boarding fees \$2,503,983 (+260,485)
- Youth detention and secure shelter boarding and program fees \$1,591,613 / (+\$136,964)

The increase in net assets for governmental activities of \$3,608,319 was primarily a result of:

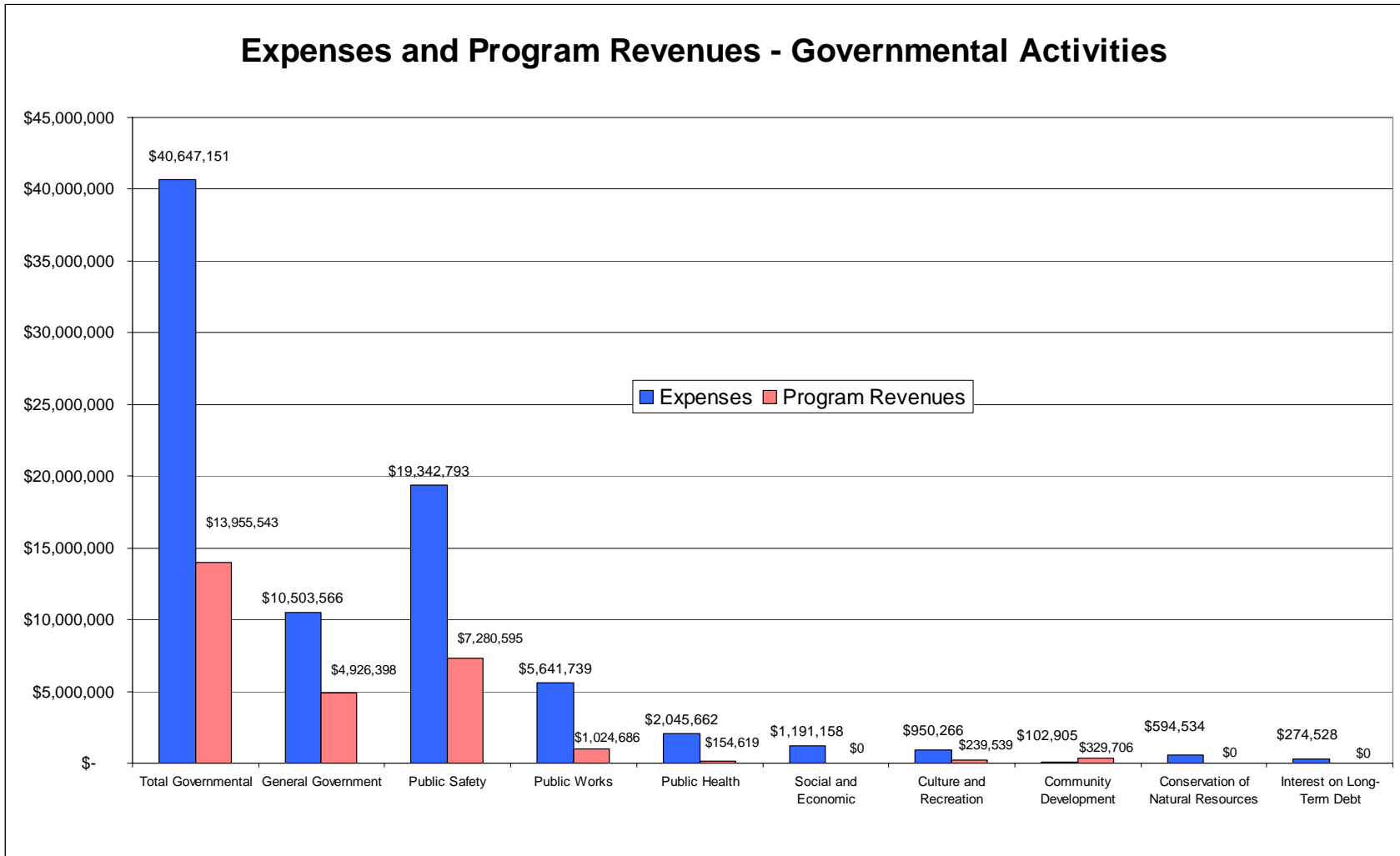
- \$1,078,796 increase in net assets of the health insurance fund
- \$417,151 increase in fund balance of general fund as a result of increased interest revenues and document recording fees and budget savings
- \$953,654 increase in net assets as a result of the decrease in long-term debt
- \$683,456 in growth of capital assets

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Yellowstone County's Change in Net Assets

| | Governmental Activities | | Business-type Activities | | Total | |
|--|--------------------------------|---------------------|---------------------------------|-------------------|---------------------|---------------------|
| | 2005 | 2006 | 2005 | 2006 | 2005 | 2006 |
| Revenues: | | | | | | |
| Program revenues: | | | | | | |
| Special assessments | \$ 1,402,391 | \$ 458,768 | \$ 300,927 | \$ 292,318 | \$ 1,703,318 | \$ 751,086 |
| Licenses and permits | 97,598 | 81,756 | 0 | 0 | 97,598 | 81,756 |
| Intergovernmental | 576,923 | 1,745,996 | 0 | 0 | 576,923 | 1,745,996 |
| Fines and forfeitures | 686,062 | 691,857 | 0 | 0 | 686,062 | 691,857 |
| Charges for services | 8,109,116 | 8,806,718 | 3,791,856 | 3,639,749 | 11,900,972 | 12,446,467 |
| Operating grants and contributions | 1,229,062 | 811,661 | 0 | 0 | 1,229,062 | 811,661 |
| Capital grants and contributions | 1,327,036 | 1,358,787 | 0 | 0 | 1,327,036 | 1,358,787 |
| Total program revenues | 13,428,188 | 13,955,543 | 4,092,783 | 3,932,067 | 17,520,971 | 17,887,610 |
| General revenues: | | | | | | |
| Property taxes | 20,919,057 | 22,808,060 | 933,731 | 1,024,514 | 21,852,788 | 23,832,574 |
| Licenses and permits | 3,542,973 | 3,718,188 | 0 | 0 | 3,542,973 | 3,718,188 |
| Intergovernmental | 3,660,561 | 2,718,038 | 24,874 | 18,656 | 3,685,435 | 2,736,694 |
| Other revenues | 1,004,988 | 1,413,477 | 13,431 | -72 | 1,018,419 | 1,413,405 |
| Total general revenues | 29,127,579 | 30,657,763 | 972,036 | 1,043,098 | 30,099,615 | 31,700,861 |
| Total revenues | 42,555,767 | 44,613,306 | 5,064,819 | 4,975,165 | 47,620,586 | 49,588,471 |
| Expenses: | | | | | | |
| General government | 10,907,340 | 10,503,566 | 0 | 0 | 10,907,340 | 10,503,566 |
| Public Safety | 18,376,544 | 19,342,793 | 0 | 0 | 18,376,544 | 19,342,793 |
| Public Works | 5,479,634 | 5,641,739 | 0 | 0 | 5,479,634 | 5,641,739 |
| Public Health | 1,878,717 | 2,045,662 | 0 | 0 | 1,878,717 | 2,045,662 |
| Social and Economic | 1,744,917 | 1,191,158 | 0 | 0 | 1,744,917 | 1,191,158 |
| Culture and Recreation | 334,760 | 950,266 | 0 | 0 | 334,760 | 950,266 |
| Community Development | 1,441 | 102,905 | 0 | 0 | 1,441 | 102,905 |
| Conservation of Natural Resources | 102,133 | 594,534 | 0 | 0 | 102,133 | 594,534 |
| Interest on Long-Term Debt | 305,469 | 274,528 | 0 | 0 | 305,469 | 274,528 |
| Sanitation, refuse disposal | 0 | 0 | 351,469 | 353,421 | 351,469 | 353,421 |
| Civic center, METRA | 0 | 0 | 5,383,030 | 5,346,165 | 5,383,030 | 5,346,165 |
| Total expenses | 39,130,955 | 40,647,151 | 5,734,499 | 5,699,586 | 44,865,454 | 46,346,737 |
| Increase (decr.) in net assets before transfers | 3,424,812 | 3,966,155 | (669,680) | (724,421) | 2,755,132 | 3,241,734 |
| Transfers | (171,785) | (357,836) | 171,785 | 357,836 | 0 | 0 |
| Increase (decrease) in net assets | 3,253,027 | 3,608,319 | (497,895) | (366,585) | 2,755,132 | 3,241,734 |
| Beginning net assets | 35,038,899 | 38,291,926 | 14,061,083 | 13,563,188 | 49,099,982 | 51,855,114 |
| Ending net assets | \$38,291,926 | \$41,900,245 | 13,563,188 | 13,196,603 | \$51,855,114 | \$55,096,848 |

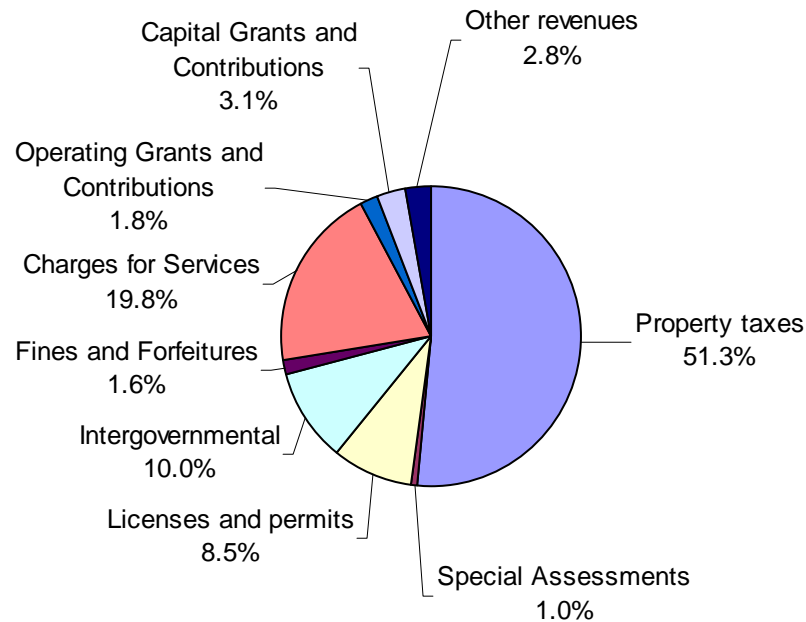
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See the Statement of Activities for additional detail information regarding revenues and expenditures.

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Total Revenues by Source - Governmental Activities

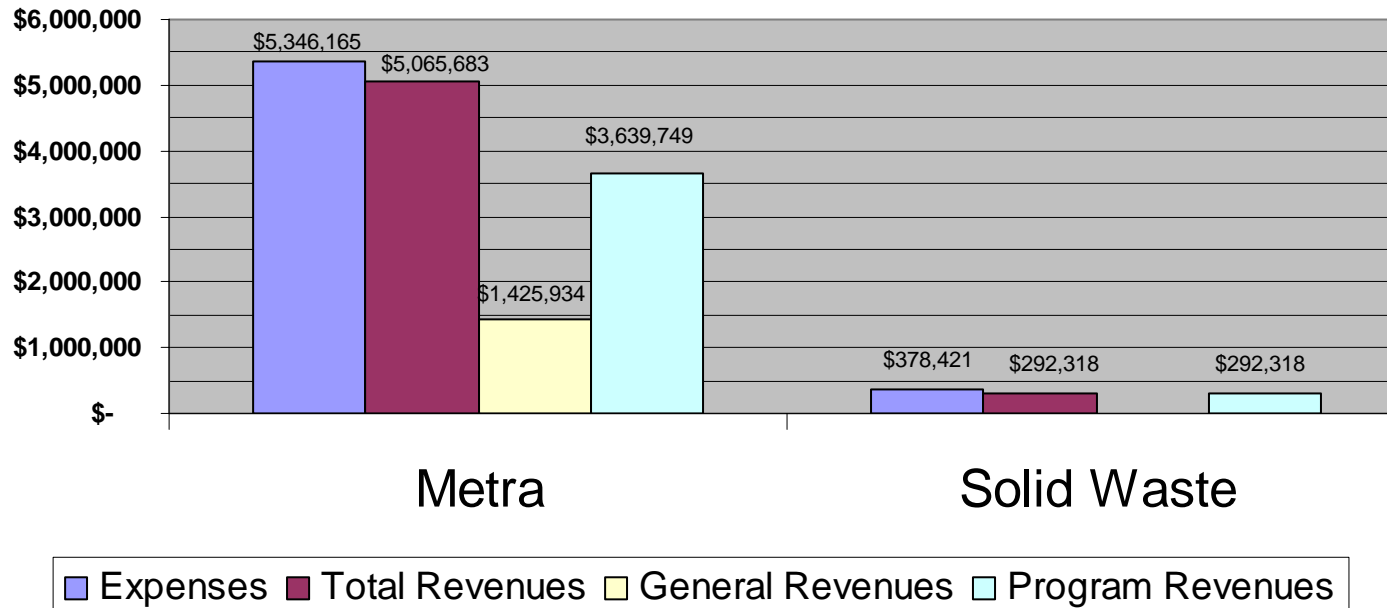


Business-type activities.

Total expenses of \$5,699,586 exceeded total revenues of \$5,333,001, which resulted in a net loss of (\$366,585) for business-type activities. METRA had a FY06 net loss of (\$280,482). Depreciation expense accounted for \$810,227 of the net loss, however, revenues of \$298,103 intended for funding capital depreciation expense is included as a revenue source. If the capital replacement and maintenance and financing activities of METRA were reported separately, it would have a net loss of (\$604,214). Operations would have had a net gain of \$323,732, however, \$330,000 of the gain was attributed to a one-time general fund transfer to enhance the financial position of METRA.

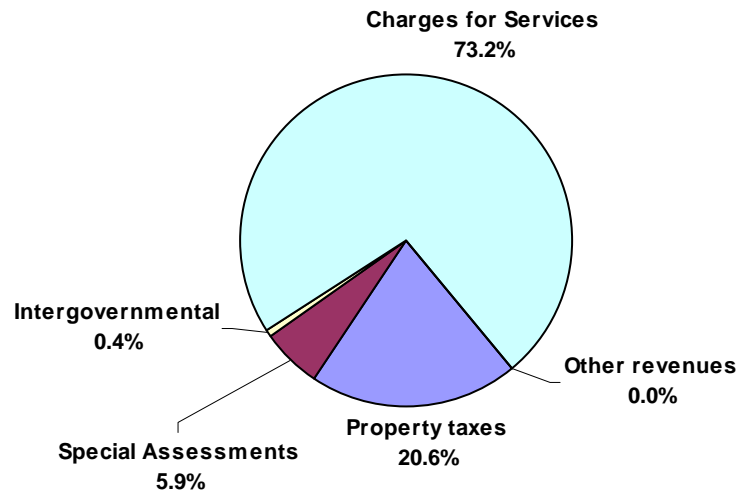
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Total Expenses and Revenues - Business Type Activities



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Total Revenues by Source - Business Type Activities



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Fund Financial Statement Analysis

Governmental funds.

Overall, Yellowstone County's governmental funds' change in fund balance for FY06 was an increase of \$784,030 resulting in an ending total governmental fund balance of \$22,941,115.

The general fund increased fund balance by \$417,151 during fiscal year 2006. The primary causes of the increase are explained in MD&A financial highlights section above .

The road fund increased its fund balance by \$91,102. An equipment storage building costing \$366,692 (\$261,692 from road fund and \$105,000 from bridge fund) was constructed in FY07 to enhance safety, and equipment readiness. Weather cooperated in permitting planned road projects to be completed timely.

The property and liability insurance fund incurred an increase in fund balance of \$122,276, since large settlement claims were minimal in FY06. Although the County was able to obtain reinsurance coverages at similar premiums to recent years, there is still concern about future funding losses in this fund without some improvement in tort reform and employment law. It is anticipated that the reserves in this fund will be able to adequately fund the County's property and liability insurance needs for the immediate future.

The RSID bond fund decreased in fund balance by (\$159,642) because of assessment prepayment collections on \$1,148,000 of new RSID bonds issued in FY05, which was used to call principal on RSID debt in FY06.

The capital improvement fund decreased its fund balance (\$180,790) primarily due to the expenditure of \$388,980 for the cyclical replacement of the County's motor graders and the expenditure of \$221,280 on bridge projects.

See financial highlights section above for discussion related to other notable changes to governmental fund balances.

Proprietary funds.

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The refuse disposal fund had a decrease in net assets of (\$86,103) for FY06. This fund has total net asset of \$883,611 on June 30, 2006, which substantially exceeds the amount necessary for the operation of the fund. The fund accumulated this amount as a result of anticipation of funding landfill contract costs that did not occur. As a result, it is anticipated that future year's reserves will be reduced in order to reduce the net assets of this fund. The current assessment rate is set below the expected costs of operations and a reduction to reserves began occurring in FY05.

In FY06, the METRA fund had an overall reduction to net assets of (\$280,482). The operations component of METRA improved \$323,732 during FY06, while the capital replacement component of METRA had a net asset reduction of (\$604,214). The reduction to net assets in the operations component would have been larger, however, the County general fund contributed \$330,000 to improving Metra's operating reserve. The capital replacement component of METRA includes capital replacement and depreciation, capital maintenance expenses, and capital financing. Most of the loss in the capital replacement fund is a result of annual depreciation, which was \$810,227. The recurring revenues dedicated for capital replacement generated only 33.3% of the related expenses incurred for FY06. The FY07 budget projects a \$250,000 transfer from Metra operations to Metra capital in hopes of sufficient net revenues being generated by Metra's FY07 operations. It is a goal for Metra to generate additional operational revenues to assist with capital maintenance and replacement needs, although it is likely that additional revenues will be necessary to fund long term facility capital maintenance and replacement. See financial highlights section above for additional discussion related to METRA.

The health insurance fund had a net asset increase of \$1,192,772 for FY06 to bring the ending net assets to \$2,271,568. This was a result of better than expected claims for the year, and a planned building of reserves by funding an additional \$200,000 to the plan above the FY06 projected claims level. For FY07 the health plan is again funded to cover costs based on a projected cost level determined by our health plan third party administrator. The County's FY07 exposure for claims above funding is approximately \$752,000. The aggregate stop-loss would pay claims after that amount. Medical inflation remains a major concern and continues to present challenges to maintain a health plan that provides good benefits at affordable premiums. The County systematically reviews the health plan every year to review premium rates, benefits, and plan administration.

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Differences between original and final revised budget were a result of state and federal grant awards and related match funding being added to the original budget. The original budget does not include either new or continuing grant activity and is subsequently amended into the budget by resolution of the Board of County Commissioners. The major grants included in the fiscal year 2006 budget were:

- \$1,146,676 in various Homeland Security, emergency preparedness and mitigation grants
- \$696,126 in multiple grants for Pompey's Pillar improvements and grants for the Lewis and Clark bicentennial event
- \$376,500 Community Development Block Grant (CDBG) for Link Communications
- \$500,000 for a CDBG Town of Custer sewer improvement grant
- \$97,326 in various weed control grants
- \$383,229 in various crime control grants, primarily for juvenile programs and gun violence

Some of the significant final budget to actual revenue variances include:

- (\$1,434,697) of unearned grant revenue, which is offset by a similar amount of unexpended grant appropriations
- \$365,319 of additional clerk & recorder fees driven by a higher than normal amount of mortgage refinancings and new construction due to low interest rates and community development.
- \$78,078 in additional motor vehicle option tax for public safety
- \$304,223 in prisoner boarding fees for sheriff's detention facility
- \$94,541 in boarding and program fees for youth services and detention
- \$122,992 of interest earnings in the general fund due to increasing interest rates.

The appropriation final budget to actual variances of significance include:

- \$1,613,772 in unspent contingency budgets
- \$4,124,861 in unspent capital reserve budgets
- \$865,006 of unspent road budget due to cost savings from using asphalt millings from State road projects, and a mild winter
- \$750,754 in unspent bridge projects, which are carried forward to next budget cycle

Capital Assets

A comparison of capital assets for the last two fiscal years is presented below:

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| | Governmental Activities | | Business Activities | | Total | |
|-----------------------------------|----------------------------|----------------------|------------------------|----------------------|----------------------|----------------------|
| | <u>2005</u> | <u>2006</u> | <u>2005</u> | <u>2006</u> | <u>2005</u> | <u>2006</u> |
| Land | \$ 1,132,792 | \$ 1,215,292 | \$ 368,574 | \$ 368,574 | \$ 1,501,366 | \$ 1,583,866 |
| Buildings | 12,164,352 | 11,988,421 | 11,461,234 | 10,980,388 | 23,625,586 | 22,968,809 |
| Improvements other than buildings | 480,638 | 434,727 | 668,997 | 555,141 | 1,149,635 | 989,868 |
| Equipment and vehicles | 5,326,845 | 6,291,437 | 274,276 | 251,925 | 5,601,121 | 6,543,362 |
| Infrastructure | 1,909,632 | 2,198,200 | 0 | 0 | 1,909,632 | 2,198,200 |
| Construction in progress | 466,828 | 232,525 | 0 | 33,934 | 466,828 | 266,459 |
| Total Capital Assets | \$ 21,481,087 | \$ 22,360,602 | \$ 12,773,081 | \$ 12,189,962 | \$ 34,254,168 | \$ 34,550,564 |

Governmental capital assets increased \$879,515 in total during the year as a result of the addition of new capital assets in the governmental funds of \$2,395,503 while being offset by depreciation of \$1,875,969 and a gain on disposal of assets of \$163,922 and increasing net capital assets in the internal service funds by \$196,059.

Some of the larger capital acquisitions in the governmental activities were:

- Motor vehicle office renovation \$116,920
- Pompey's Pillar riverwalk (construction-in-progress) \$206,157
- Heavy equipment for road department \$919,995
- Heavy equipment storage building for road and bridge departments \$366,693
- Bridge and culvert replacements \$401,539
- Replacement of sheriff patrol vehicles \$173,008

Some of the larger capital acquisitions in the business activities were:

- Metra upper parking lot stairway tunnel cover \$18,479
- Metra fire alarm improvements \$65,450
- Metra electrical power improvements \$28,652
- Skid steer loader \$25,273

For the financial statements issued for June 30, 2006, the infrastructure for the County acquired prior to July 1, 2002 has not been reported. See footnote 7 for additional information on capital assets.

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Long-term Debt

As of June 30, 2006 the County has \$9,569,666 of outstanding long-term debt. Governmental funds account for \$9,001,386 and the enterprise funds account for \$568,280.

The largest component of long-term debt is \$5,355,000 of general obligation bonds issued by the County to expand and improve the event facilities located at METRA. This voter approved debt is being funded by an annual tax levy on citizens within the County. Law requires an annual levy sufficient to service the general obligation bond.

Another major component of long-term debt includes rural special improvement district (RSID) bonds issued to provide property improvements to properties located within a specified area. Repayment of this debt is assessed to the benefited property owners, which can be repaid over the life of the bond or the remaining principal assessment against the property can be repaid anytime. The County provides additional bond debt service collateralization with the County's RSID Revolving Fund and other contingent funding requirements as specified by law. The County currently has \$1,308,225 of outstanding RSID bonds and the RSID Revolving Fund has a fund balance of \$241,510. The County issued no new RSID bonds during the year.

Notes payable are occasionally used to finance equipment that a particular fund may not have adequate reserves or funding to acquire within a budget cycle. Outstanding notes payable at year end were \$418,796. No new notes payable were issued during FY06.

Claims and judgments represent the amount of the estimated liability established that is expected to pay for the known liability cases pending against the County. The amount of the estimated liability at year end was \$475,000 for all cases.

Compensated absences is the amount of the liability for unpaid vacation and sick leave at yearend. The amount of the liability generally increases on an annual basis as a result of increasing wages and a general growth in number of total compensable hours. The amount of this liability at yearend was \$2,023,965.

Economic Factors and Next Year's Budget

YELLOWSTONE COUNTY, MONTANA
MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)
JUNE 30, 2006

New construction taxable value growth has averaged 5.73% for 2005 and 2006, which has exceeded the area's typical growth trend of 3%. The new construction growth rate is expected to begin slowing, although low mortgage interest rates may help to maintain a favorable growth rate. Growth has been in the form of both new residential and commercial construction. Local refineries, which represent major taxpayers, continue to enhance their facilities. Local medical facilities have been expanding their operations. While the medical facilities do not add to the property tax base, they do add to the local economy. The new construction provides some property tax revenue growth to offset inflationary trends in salaries and other operating costs. As with many local government entities, the growth provides funding to help offset inflation trends with existing programs but often leaves little for new or enhanced programs or services. The government often has to find ways to be more efficient at service delivery.

Some of the more significant projected financial changes to operations for fiscal year 2007 include:

- Effective July 1, 2006 the operations of public defender's office were transferred to the State of Montana. As a result over \$1.1 million of budget was eliminated from revenues and expenses for the district court fund in FY07.
- Voters approved property tax increase for one year for \$1,033,820 Metra roof replacement.
- The County has acquired two tracts of land in proximity to the county road shop and jail at a cost of \$729,400 to be used for future expansion needs of those facilities.
- 5.9% increase in health insurance funding. Although the medical inflation for FY07 is modest compared to prior years, cost control in this field is imperative.

Requests for Information

This financial report is designed to provide a general overview of Yellowstone County's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to:

Yellowstone County Finance Director
P.O. Box 35003
Billings, MT 59107