

TOWN OF FRONT ROYAL, VIRGINIA

*COMPREHENSIVE
ANNUAL FINANCIAL REPORT*

FOR THE FISCAL YEAR ENDED JUNE 30, 2006

**Prepared by the
Department of Finance
Kim Gilkey-Breeden
Director of Finance**

FOREWARD

Front Royal is located in Warren County in Northern Virginia approximately 17 miles south of Winchester and 70 miles west of Washington, DC. The Town was founded in 1754 and chartered by the General Assembly of Virginia in 1788. U.S. Highways 522 and 340, and State Route 55 provide access to the Town. Interstate Highways 66 and 81 are located 1 mile north and 6 miles west of the Town, respectively. The Town covers an area of approximately 9 square miles and has a population estimated at 13,720.

The Town is governed under a Council-Manager form of government. The Town Council is comprised of six members, who are elected at large, to serve four-year terms. Elections for three seats on the Town Council are held every two years. The Mayor, who serves a two-year term, presides over the Town Council, but may vote only to break a tie.

The Town Manager is appointed by the Town Council as the chief executive officer of the Town and is responsible to the Town Council for proper administration of the Town government. The Town Manger also serves as Town Treasurer and is responsible for the financial operations of the Town. The Town Council appoints the Clerk of the Town Council. The department directors for the finance, electric, engineering, public works and utilities, planning/zoning, and police departments are appointed by and are under the supervision of the Town Manager.

In Virginia, incorporated towns are part of the county in which they are located. Accordingly, the residents of an incorporated town are required to pay certain taxes, including ad valorem taxes, to both the town and the county. The town provides certain services received by residents of the town with other services being provided by the county.

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INTRODUCTORY SECTION

PART I



TOWN OF FRONT ROYAL

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FRONT ROYAL, VIRGINIA 22630
(540) 635-8007
(540) 636-7475 (Fax)
mgraham@ci.front-royal.va.us

Town Manager
J. Michael Graham

November 27, 2006

The Honorable Mayor, Members of the
Town Council and Citizens of the Town of
Front Royal, Virginia

State law requires that all general-purpose local governments publish, within six months of the close of each fiscal year, a complete set of financial statements presented in conformity with generally accepted accounting principles (GAAP) and audited in accordance with generally auditing standards by a firm of licensed certified public accountants. Pursuant to the requirement, we hereby issue the Comprehensive Annual Financial Report of the Town of Front Royal, Virginia for the fiscal year ending June 30, 2006.

This report consists of management's representations concerning the finances of the Town of Front Royal, Virginia. Consequently, management assumes full responsibility for the completeness and reliability of all of the information presented in this report. To provide a reasonable basis for making these representations, the management of the Town of Front Royal, Virginia has established a comprehensive internal control framework. These controls are designed both to protect the government's assets from loss, theft, or misuse and to compile sufficient reliable information for the preparation of the Town of Front Royal, Virginia's financial statements in conformity with GAAP. Because the cost of internal controls should not outweigh their benefits, the Town of Front Royal, Virginia's comprehensive framework of internal controls has been designed to provide reasonable rather than absolute assurance that the financial statements will be free from material misstatement. As management, we assert that, to the best of our knowledge and belief, this financial report is complete and reliable in all material respects.

The Town of Front Royal, Virginia's financial statements have been audited by Mitchell & Co., P.C., a firm of licensed certified public accountants. The goal of the independent audit was to provide reasonable assurance that the financial statements of the Town of Front Royal, Virginia for the fiscal year ending June 30, 2006, are free of material misstatement. The independent audit involved 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. The independent auditor concluded, based upon the audit, that there was a reasonable basis for rendering an

unqualified opinion that the Town of Front Royal, Virginia's financial statements for the fiscal year ending June 30, 2006, are fairly presented in conformity with GAAP. The independent auditor's report is presented as the first component of the financial section of this report.

GAAP require that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with it. The Town of Front Royal, Virginia's MD&A can be found immediately following the report of the independent auditors.

Profile of the Government. Front Royal is located in Warren County in Northern Virginia approximately 17 miles south of Winchester and 70 miles west of Washington D.C. The Town was founded in 1754 and Chartered by the General Assembly of Virginia in 1788. U.S. Highways 522 and 340, and State Route 55 provide access to the Town. Interstate Highways 66 and 81 are located at the northern town limits and 6 miles west of the Town, respectively. The Town covers an area of approximately 9 square miles and has a population estimated at 13,589.

The Town is governed under a Council-Mayor form of government. The Town Council is comprised of six (6) members, who are elected at large, to serve four-year terms. Elections for three (3) seats on the Town Council are held every two (2) years. The Mayor, who serves a two-year term, presides over the Town Council, but votes only to break a tie.

The Town Manager is appointed by the Town Council as the chief executive officer of the Town and is responsible to the Town Council for proper administration of the Town government. The Town Manager also serves as the Town Treasurer and is responsible for the financial operations of the Town. The Clerk of Council and Town Attorney are appointed by the Town Council. The department directors of finance, public works, public utilities, human resources, office of tourism, public safety and planning/zoning are appointed by and under the supervision of the Town Manager.

In Virginia, incorporated towns are part of the country in which they are located. Accordingly, the residents of an incorporated town are required to pay certain taxes, including ad valorem taxes, to both the town and the county. Certain services received by residents of a town are provided by the town with other services being provided by the county.

The government maintains a budgetary control over its spending. The objective of these budgetary controls is to ensure compliance with the legal provisions embodied in the annual appropriated budget approved by the Town Council. Activities of the general fund and all enterprise funds are included in the annual appropriated budget. The level of budgetary control (that is, the level at which expenditures cannot legally exceed the appropriate amount) is established by function and activity within the individual fund. The government also maintains an encumbrance accounting system as one technique for

accomplishing budgetary control. Encumbered amounts lapse at year-end. However, encumbrances generally are re-appropriated as part of the following year's budget. As demonstrated by the statements and schedules included in the financial section of the report, the government continues to meet its responsibility for sound financial management.

Factors Affecting Financial Condition. The information presented in the financial statements is perhaps best understood when it is considered from the broader perspective of the environment within which the Town of Front Royal, Virginia operates.

Local Economy. Since 1994, one thousand new jobs have been created and \$200 million have been invested by a number of companies including Toray Plastics (Amercian), Inc., Family Dollar Stores Distribution center, Walden Foods, Tartan Textiles, Precision Systems, Ferguson Enterprises, CorrecTech (BioMed Devices), Valley Redi-Mix, Blue Ridge Prestain, GeoDigital Mapping, AirPac, Satisfice and The Lynx Group. Sysco's Baugh Northeast Cooperative will open its distribution center will complete its Warren County power plant in late 2005, respectively, creating an additional 410 new jobs and \$330 million in investments.

DuPont has been a mainstay for the economy since 1981, as it has steadily grown its local operation, and now 400 employees at its Front Royal plant. Downtown Front Royal has seen a resurgence of commercial activity, including shopping, dining, arts and entertainment establishments that attract residents as well as tourists. The Town helped to establish a special service district to assist downtown commercial properties with promotional projects and capital improvements. The downtown district expired on June 30, 2005. The Town also helped to establish a Technology Zone that encompasses 125 acres of downtown area and provides incentives and grants to technology companies that are located in the zone.

The Economic Development Authority (EDA), FMC Corporation, Virginia's Department of Environmental Quality (DEQ) and the Environmental Protection Agency (EPA) are working in partnership to rehabilitate the 500-acre Avtex Fibers Superfund site located in the Town of Front Royal for redevelopment and reuse. The Avtex Administration building has been rehabilitated and houses over 8,000 square feet of available office space for lease. The EDA reports that they lease two (2) of the four (4) available office suites, with the EDA administrative office occupying the fifth.

The Town has made investments in its gateway and primary corridors to improve their appearance. The Town also continued to expand its Civil War Battle of Front Royal Tour Program that is attracting tourists from around the world. Front Royal is host to the gateway to the Skyline Drive and Shenandoah National Park, which positions it well for tourism revenue. The Town has recently been certified as a 2007 community for the State's 400th birthday celebration "Come Home to Virginia".

Long-Term financial planning. During fiscal year 2005, the Town continued its efforts to advance in the use of technology. In 2004 a fiber optic backbone network was

constructed to serve many of the Town's facilities. This has allowed the Town to begin implementation of a Town-wide telephone system. Upon completion of the fiber lighting a LAN/Wan will be created, allowing departments to communicate electronically.

Cash management policies and practices. The Town maintains a zero balance, checks-cleared checking account whereby all access funds are invested until a check is presented for payment. At that time, the necessary funds are transferred to the account by the bank. Any funds not needed for anticipated expenses are invested in certificates of deposit with local banks and with the Local Government Investment Pool (LGIP) maintained by the Commonwealth of Virginia on behalf of municipalities.

Risk Management. Risk management functions continue to be organized as a responsibility of the Director of Human Resources. No major, new initiatives were undertaken in the area of risk management. Efforts taken in prior years to reduce losses were continued in 2006. The overall goals of risk management are to reduce the Town's losses to the lowest possible level and to protect the Town's assets from loss, theft and misuse.

Pension and other post-employment benefits. The contributes to the Virginia Retirement System (VRS) on behalf of its employees. All full-time permanent employees must participate in the system. Benefits vest after five (5) years of service so that employees are eligible for unreduced retirement at age 65 with five (5) years of service or at age 55 with 30 years of service. Benefits are actuarially reduced for employees who retire prior to becoming eligible for retirement benefits.

In addition to providing pension benefits, the Town provides certain health care insurance benefits for its retired employees. Substantially all employees may become eligible at varying levels depending on the years of service and employment with the Town.

Awards and Acknowledgements. The Government Finance Officers' Association (GFOA) awarded a Certificate of Achievement for Excellence in Financial to the Town of Front Royal for its comprehensive annual financial report (CAFR) for the fiscal year ending June 30, 2005. This is the nineteenth (19) consecutive years that the government has received this prestigious award. In order to be awarded a Certificate of Achievement, the Town published an easily readable and efficiently organized CAFR. This report satisfied both generally accepted accounting principals and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe that our current CAFR continues to meet the Certificate of Achievement Program's requirements, and we are submitting it to the GFOA to determine its eligibility for another certificate.

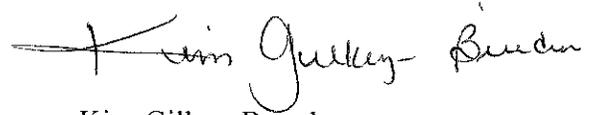
The preparation of this report would not have been possible without the efficient and dedicated services of the entire staff of the Town of Front Royal, Virginia Finance Department. We would like to express our appreciation to all members of the Department and especially, Sue McIntosh, who assisted and contributed to the preparation of this report. Credit must also be given to the Mayor and Town Council for their unfailing

support for maintaining the highest standards of professionalism in the management of the Town of Front Royal, Virginia's finances.

Respectfully submitted,



J. Michael Graham
Town Manager



Kim Gilkey-Breeden
Director of Finance

Certificate of Achievement for Excellence in Financial Reporting

Presented to

Town of Front Royal Virginia

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2005

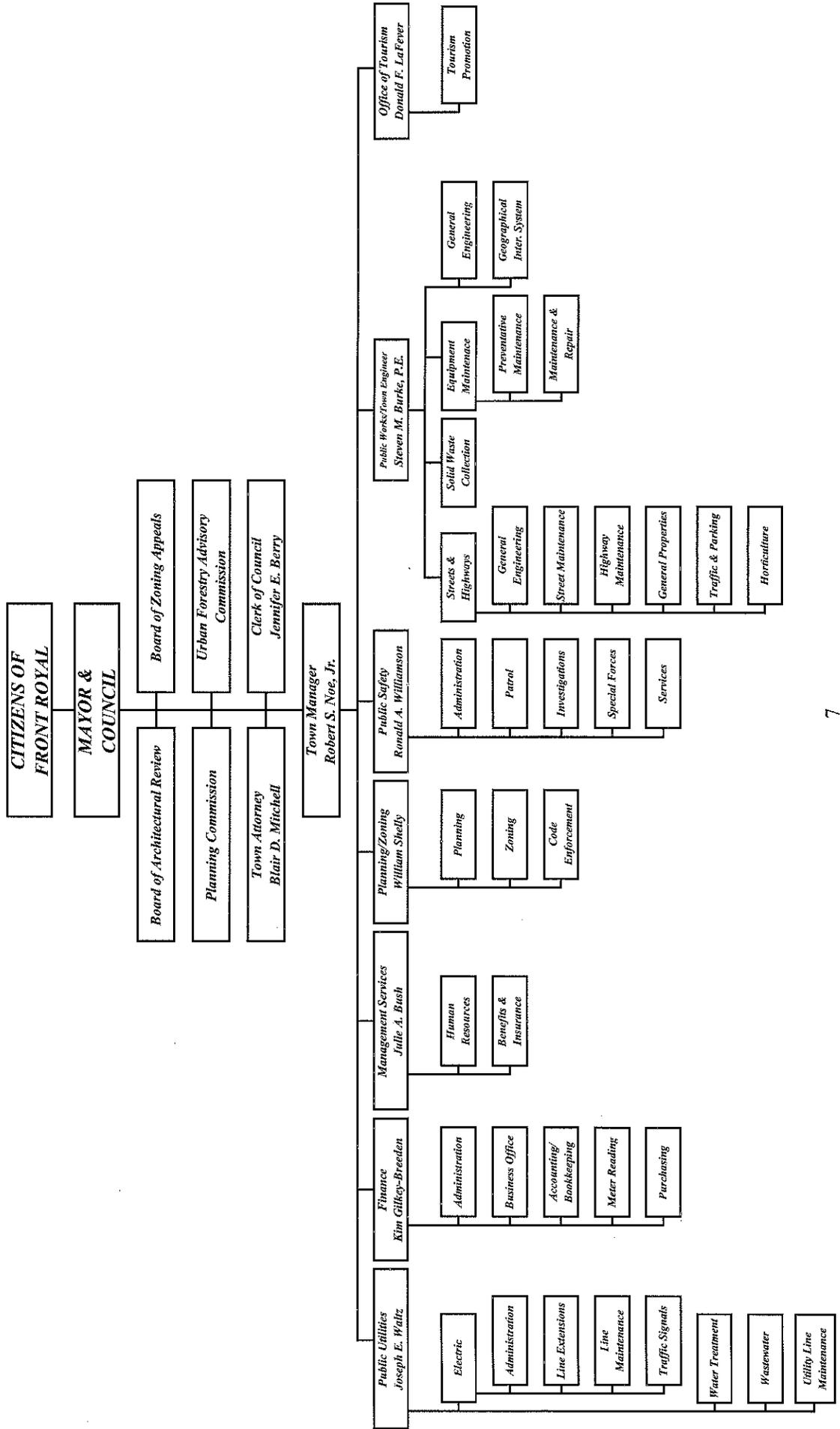
A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



President

Executive Director

TOWN OF FRONT ROYAL
ORGANIZATIONAL CHART
FISCAL YEAR ENDED JUNE 30, 2006
(With Full-Time Employees)



**TOWN OF FRONT ROYAL, VIRGINIA
JUNE 30, 2006**

Town Council

James M. Eastham - Mayor
Timothy W. Darr - Vice Mayor

Stanley W. Brooks, Jr.
M. Eileen Grady
Eugene R. Tewalt
Thomas H. Sayre
Bret W. Hrbek

Administrative and Budget Officers

Robert S. Noe, Jr. - Interim Town Manager
Blair D. Mitchell - Town Attorney
Ronald A. Williamson - Chief of Police
William Shelly - Director of Planning - Interim
Steven M. Burke, P.E. - Director of Public Works/Town Engineer
Cynthia A. Hartman - Purchasing Agent
Julie A. Bush - Director of Management Services
Jennifer E. Berry - Clerk of Council
Andrea D. Lilley - Zoning Officer
Don McPaters - Superintendent of Vehicle Maintenance
Kim Gilkey-Breeden - Director of Finance
Joseph Waltz - Director of Public Utilities

FINANCIAL SECTION

PART II

MITCHELL & Co., P.C.

CERTIFIED PUBLIC ACCOUNTANTS

110 EAST MARKET STREET, SUITE 200

LEESBURG, VIRGINIA 20176

JEFFREY D. MITCHELL, CPA

SANDRA M. TONDREAU, CPA
LORI M. ROOD, CPA

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Fax: 703-771-3082

E-mail mco@mco CPA.com

INDEPENDENT AUDITOR'S REPORT

To The Honorable Mayor and Members of Town Council
Town of Front Royal, Virginia

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Town of Front Royal, Virginia, as of and for the year ended June 30, 2006, which collectively comprise the Town of Front Royal, Virginia's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Town of Front Royal, Virginia'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, *Government Auditing Standards*, issued by the Comptroller General of the United States and the *Specifications for Audits of Counties, Cities and Towns* issued by the Auditor of Public Accounts of the Commonwealth of Virginia. 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 opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Town of Front Royal, Virginia, as of June 30, 2006, and the respective changes in financial position and cash flows, where applicable, thereof, and the respective budgetary comparison for the general fund 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 October 27, 2006 on our consideration of the Town's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, 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 not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The management's discussion and analysis as identified in the Financial Section of the accompanying table of contents 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 Town of Front Royal, Virginia's basic financial statements. The introductory section, supplementary information, and statistical section are presented for purposes of additional analysis and are not a required part of the basic financial statements. The supplementary information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

October 27, 2006
Leesburg, Virginia

Mitchell & Company, P.C.

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the Town of Front Royal, Virginia, we offer readers of the Town's financial statements this narrative overview and analysis of the financial activities of the Town of Front Royal, Virginia for the fiscal year ended June 30, 2006. We encourage readers to consider the information presented here in conjunction with the additional information that we have furnished in our letter of transmittal, which can be found on pages 1-5 of this report.

Financial Highlights

- The assets of the Town exceeded its liabilities at the close of the most recent fiscal year by \$127,071,800. Of this amount, \$32,695,839 may be used to meet the Town's ongoing obligations to its citizens and creditors.
- The Town's total net assets increased by \$16,732.
- As of the close of the current fiscal year, the Town of Front Royal's governmental funds reported combined ending fund balances of \$6,953,870, an increase of \$1,350,992 in comparison with the prior year. Most of this total amount, \$6,852,895, is available for spending at the government's discretion.
- At the end of the current fiscal year, unreserved fund balance for the general fund was \$5,391,587, or 63.5 percent of total general fund expenditures.
- The Town's total bonded debt increased by 9,464,728 (179 percent) during the current fiscal year.

Overview of the Financial Statements

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

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

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

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

Both of the government-wide financial statements distinguish functions of the Town of Front Royal that are principally supported by taxes and intergovernmental revenues, (governmental activities), from other functions that are intended to recover all or a significant portion of their costs through user fees and charges, (business-type activities). The governmental activities of the Town of Front Royal include general government, public safety, public works, planning, zoning and community development, and culture and recreation. The business-type activities of the Town include water, sewer, electricity, and refuse operations.

The government-wide financial statements can be found on pages 20 -- 21 of this report.

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

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

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

The Town of Front Royal, Virginia maintains nine individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the general fund and the debt service fund, both of which are considered to be major funds. Data from the other seven governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these non-major governmental funds is provided in the form of combining statements elsewhere in this report.

The Town of Front Royal adopts an annual appropriated budget for its general fund. A budgetary comparison statement has been provided for the general fund to demonstrate compliance with this budget.

The basic governmental fund financial statements can be found on pages 22 – 25 of this report.

Proprietary funds. The Town of Front Royal, Virginia uses enterprise funds to report the same functions presented as business-type activities in the government-wide financial statements. The Town's enterprise funds include the water fund, sewer fund, electric fund, and refuse fund.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statements provide separate information for the water, sewer, electric, and refuse funds, all of which are considered to be major funds of the Town.

The basic proprietary fund financial statements can be found starting on pages 26 – 30 of this report.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 31 – 53 of this report.

Supplementary Information. The combining statements referred to earlier in connection with non-major governmental funds are presented immediately following the notes to the financial statements. Combining and individual fund statements and schedules can be found on 54 – 68 of this report. Additional state required supplementary schedules follow the combining and individual fund statements and can be found on pages 69 – 71 of this report.

Government-wide Financial Analysis

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. In the case of the Town of Front Royal, Virginia, assets exceeded liabilities by \$127,071,800 at the close of the most recent fiscal year.

By far the largest portion of the Town's net assets (74 percent) reflects its investment in capital assets (e.g., land, buildings, machinery, and equipment) less any related debt used to acquire those assets that is still outstanding. The Town of Front Royal uses these capital assets to provide services to its citizens; consequently, these assets are not available for future spending. Although the Town's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities. The following table presents a summary of the Town's net assets by type of activity as of June 30, 2006 and 2005.

TOWN OF FRONT ROYAL -- NET ASSETS						
	Governmental Activities		Business-type Activities		Total	
	2006	2005	2006	2005	2006	2005
Current and other assets	\$ 7,685,866	\$ 6,478,431	\$ 27,778,626	\$ 14,630,461	\$ 35,464,492	\$ 21,108,892
Capital assets	75,193,089	78,843,279	33,948,130	34,862,430	109,141,219	113,705,709
Total Assets	82,878,955	85,321,710	61,726,756	49,492,891	144,605,711	134,814,601
Long-term liabilities	1,122,244	1,080,855	14,712,862	4,150,954	15,835,106	5,231,809
Other liabilities	440,749	591,229	1,258,056	1,936,497	1,698,805	2,527,726
Total Liabilities	1,562,993	1,672,084	15,970,918	6,087,451	17,533,911	7,759,535
Net Assets						
Invested-capital assets, net of related debt	74,624,593	78,199,373	19,751,368	39,531,599	94,375,961	117,730,972
Unrestricted	6,691,369	5,450,254	26,004,470	3,873,842	32,695,839	9,324,096
Total Net Assets	\$ 81,315,962	\$ 83,649,627	\$ 45,755,838	\$ 43,405,441	\$ 127,071,800	\$ 127,055,068

An additional portion of the Town of Front Royal's net assets (0.07 percent) represents resources that are subject to external restrictions on how they may be used. The remaining balance of unrestricted net assets may be used to meet the government's ongoing obligations to its citizens and creditors.

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

The Town's net assets increased by \$16,732 during the current fiscal year.

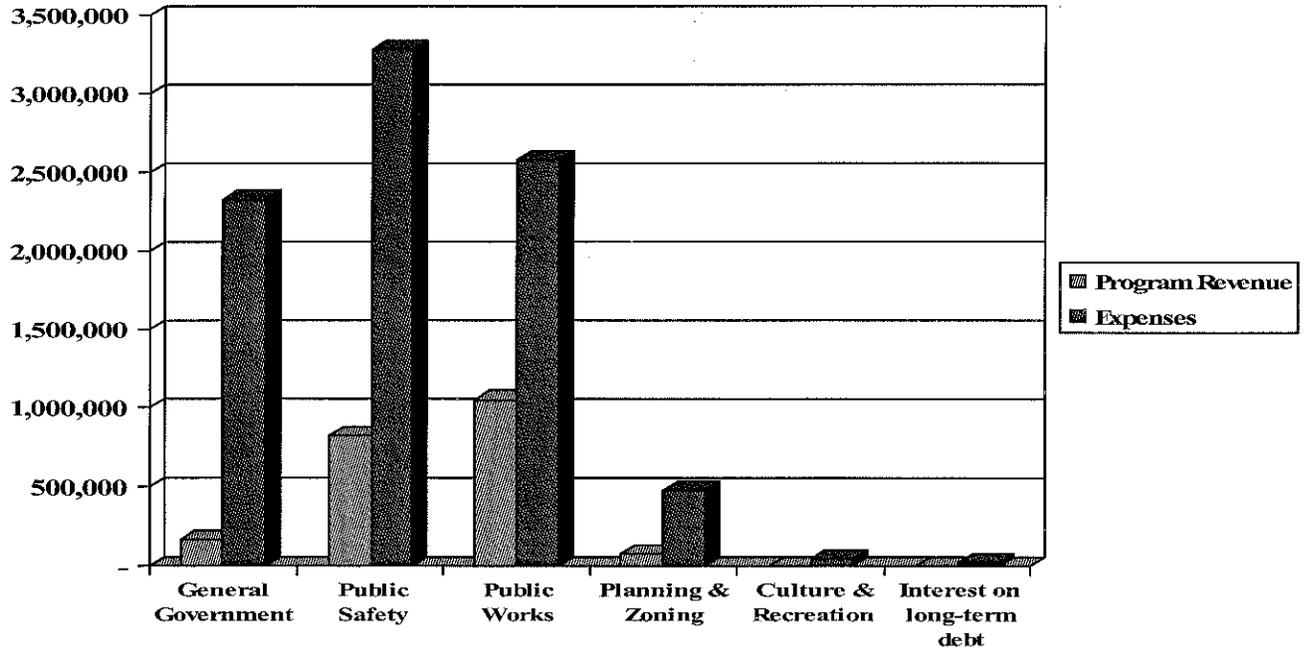
Governmental activities. Governmental activities decreased the Town of Front Royal, Virginia's net assets by \$2,333,665. These changes are presented in column one of the following table:

TOWN OF FRONT ROYAL -- CHANGES IN NET ASSETS						
	Governmental Activities		Business-type Activities		Total	
	2006	2005	2006	2005	2006	2005
Revenues						
Program revenues						
Charges for services	\$ 633,735	\$ 446,182	\$ 18,524,876	\$ 17,656,514	\$ 19,158,611	\$ 18,102,696
Operating grants and contributions	1,447,990	1,704,613	-	-	1,447,990	1,704,613
Capital grants and Contributions	43,416	80,484	71,706	226,919	115,122	307,403
General revenues						
Property taxes	1,280,730	1,213,101	-	-	1,280,730	1,213,101
Other taxes	4,190,751	3,856,913	-	-	4,190,751	3,856,913
Grants and contributions not restricted	-	-	-	-	-	-
Other	262,811	160,006	497,182	173,241	759,993	333,247
Total revenues	7,859,433	7,461,299	19,093,764	18,056,674	26,953,197	25,517,973
Expenses						
General government	2,326,711	2,493,723	-	-	2,326,711	2,493,723
Public safety	3,276,981	3,150,426	-	-	3,276,981	3,150,426
Public works	2,574,487	2,086,799	-	-	2,574,487	2,086,799
Planning and zoning	484,132	652,296	-	-	484,132	652,296
Culture and recreation	52,985	45,142	-	-	52,985	45,142
Interest on long-term debt	28,180	69,567	-	-	28,180	69,567
Infrastructure depreciation	3,591,054	3,588,522	-	-	3,591,054	3,588,522
Electric	-	-	9,523,363	9,082,609	9,523,363	9,082,609
Water	-	-	1,964,023	2,328,499	1,964,023	2,328,499
Sewer	-	-	2,285,966	2,636,183	2,285,966	2,636,183
Refuse	-	-	828,583	739,132	828,583	739,132
Total expenses	12,334,530	12,086,475	14,601,935	14,786,423	26,936,465	26,872,898
Increase in net assets before transfers	(4,475,097)	(4,625,176)	4,491,829	3,270,251	16,732	(1,354,925)
Transfers	2,141,432	2,127,400	(2,141,432)	(2,127,400)	-	-
Increase (decrease) in net assets	(2,333,665)	(2,497,776)	2,350,397	1,142,851	16,732	(1,354,925)
Net assets – 7/1/05	83,649,627	86,147,403	43,405,441	42,262,590	127,055,068	128,409,993
Net assets – 6/30/06	\$ 81,315,962	\$ 83,649,627	\$ 45,755,838	\$ 43,405,441	\$ 127,071,800	\$ 127,055,068

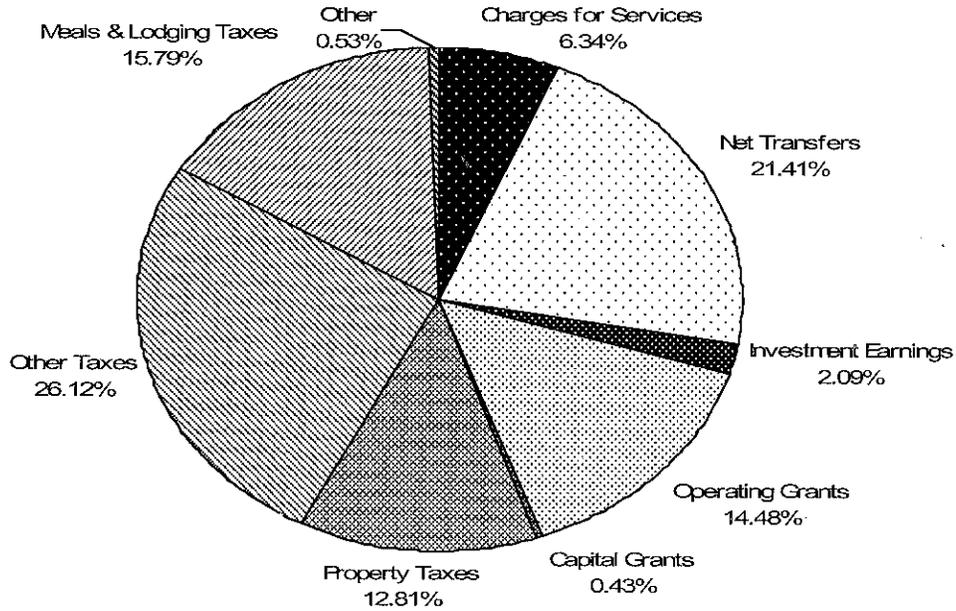
- Revenue from property taxes increased by \$67,629 (5.6 percent) during the current year.
- Operating grants for governmental activities amounted to \$1,447,990, mostly as a result of Virginia state funding. The Virginia state funding furnished resources to support two of the Town's primary functions: public safety and public works and engineering.
- For the most part, increases in expenses closely paralleled inflation and growth in the demand for services.

The following charts present a graphic representation of the Town's Governmental activities and the related revenue structure for fiscal year 2006.

EXPENSES AND PROGRAM REVENUES – GOVERNMENTAL ACTIVITIES



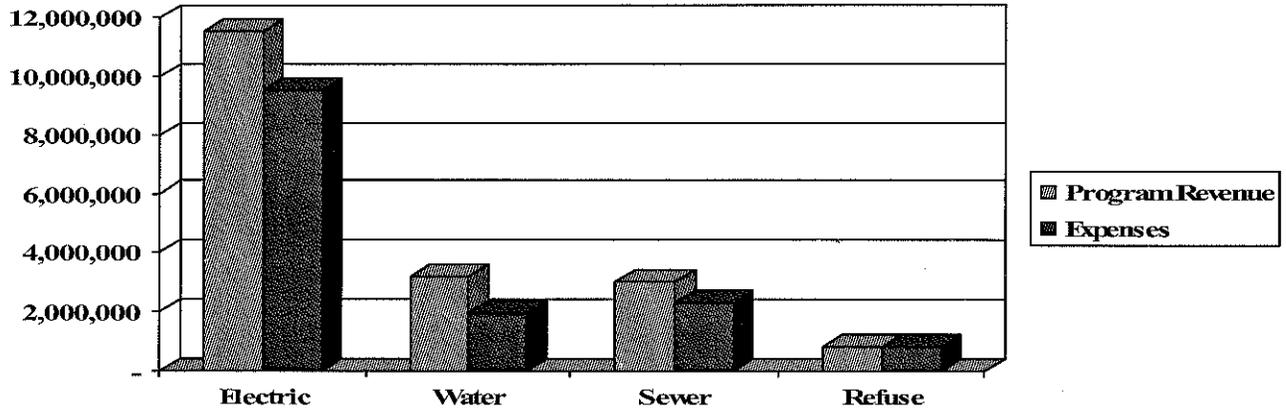
REVENUES BY SOURCE – GOVERNMENTAL ACTIVITIES



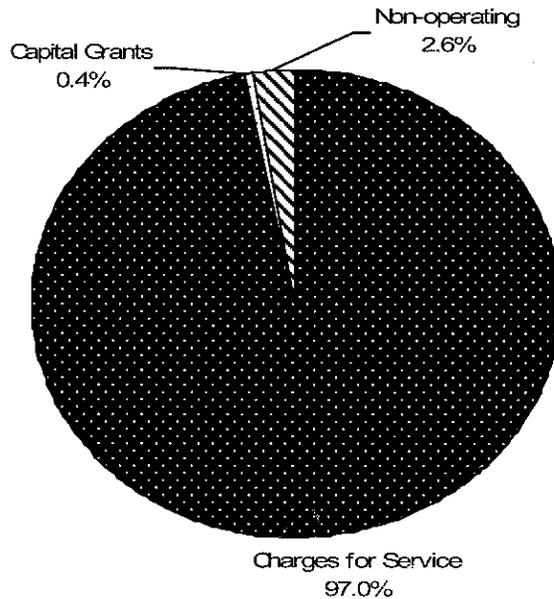
Business-type activities. Business-type activities increased the Town of Front Royal, Virginia's net assets by \$2,350,397, accounting for all the growth in the town's net assets. Key elements of this increase are as follows.

- Charges for services for business-type activities increased by \$868,362.
- Capital contributions by developers are a source of water system expansion resulting in donated systems valued at \$71,706.
- Investment earnings increased by \$323,941 for business-type activities.

EXPENSES AND PROGRAM REVENUES – BUSINESS-TYPE ACTIVITIES



REVENUES BY SOURCE – BUSINESS-TYPE ACTIVITIES



Financial Analysis of the Government's Funds

As noted earlier, the Town of Front Royal, Virginia uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

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

As of the end of the current fiscal year, the Town of Front Royal, Virginia's governmental funds reported combined ending fund balances of \$6,953,870, an increase of \$1,350,992 in comparison with the prior year. More than half of this total amount (\$6,852,895) constitutes unreserved fund balance, which is available for spending at the government's discretion. The remainder of fund balance is reserved to indicate that it is not available for new spending because it has already been committed to liquidate contracts and purchase orders of the prior period (\$100,975 for a variety of restricted purposes).

The general fund is the chief operating fund of the Town of Front Royal, Virginia. At the end of the current fiscal year, unreserved fund balance of the general fund was \$5,391,587, while total fund balance reached \$5,492,562. As a measure of the general fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved fund balance represents 63.5 percent of total general fund expenditures, while total fund balance represents 64.8 percent of that same amount.

The fund balance of the Town of Front Royal, Virginia's general fund increased by \$948,277 during the current fiscal year. Key factors in this increase are as follows:

- Expenditures were in excess of revenues by 1,193,155.
- The general fund received its annual transfers from the proprietary funds. These net transfers of \$2,141,432 are used to subsidize the need for a property tax increase.

Proprietary funds. The Town of Front Royal, Virginia's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail.

Net assets of the water, sewer and refuse functions at the end of the year amounted to \$45,755,838 and those for the electric function amounted to \$14,476,342. The total growth in net assets for all enterprise funds was \$2,350,397. Other factors concerning the finances of these funds have already been addressed in the discussion of the Town's business-type activities.

General Fund Budgetary Highlights

Additional net appropriations between the original budget and the final amended budget totaled \$883,671 and are noted as follows: a \$2,010 decrease in Town Council; a \$4,650 decrease in Clerk of Council; a \$51,910 increase in Town Manager; a \$250 increase in Management services; a \$4,250 increase in Auto/Motorpool; a \$58,559 increase in Office of Information Technology; an \$18,600 increase in the Office of Tourism; a \$4,456 increase in Legal expenditures; a \$21,532 increase in Finance; a \$179,437 increase in Planning and Zoning; an \$8,377 increase in Economic Development; a \$10,196 increase in Police Department; a \$6,700 increase in Engineering; a \$526,394 increase in Streets and Sidewalks; a \$78,204 increase in General Properties; a \$4,922 increase in Horticulture; a decrease of 83,454 in Nondepartmental expenditures.

Capital Asset and Debt Administration

Capital assets. The Town of Front Royal, Virginia's investment in capital assets for its governmental and business-type activities as of June 30, 2006, amounts to \$109,141,219 (net of accumulated depreciation). This investment in capital assets includes land, buildings and system improvements, machinery and equipment, roads, highways, and bridges.

The table below summarizes the capital assets of the Town at June 30, 2006 and 2005.

TOWN OF FRONT ROYAL - CAPITAL ASSETS (Net of Depreciation)						
	Governmental Activities		Business-type Activities		Total	
	2006	2005	2006	2005	2006	2005
Land	\$ 1,117,508	\$ 1,117,508	\$ 1,368,968	\$ 1,368,968	\$ 2,486,476	\$ 2,486,476
Construction in progress	77,927	77,927	-	-	77,927	77,927
Buildings and Improvements	2,465,791	2,552,435	3,826,184	4,025,611	6,291,975	6,578,046
Utility distribution systems	-	-	27,183,626	27,831,595	27,183,626	27,831,595
Vehicles	374,887	411,618	818,196	912,949	1,193,083	1,324,567
Machinery and Equipment	987,020	922,781	751,156	723,307	1,738,176	1,646,088
Infrastructure	70,169,956	73,761,010	-	-	70,169,956	73,761,010
Total	\$ 75,193,089	\$ 78,843,279	\$ 33,948,130	\$ 34,862,430	\$ 109,141,219	\$ 113,705,709

Additional information on the Town of Front Royal's capital assets can be found in note IV. E on pages 44 – 46 of this report.

Long-term debt. At the end of the current fiscal year, the Town of Front Royal, Virginia had total bonded debt outstanding of \$14,765,252. All of this amount comprises debt backed by the full faith and credit of the government even though most (88 percent) of it will be repaid from enterprise fund revenue.

TOWN OF FRONT ROYAL -- OUTSTANDING DEBT (General Obligation Bonds)						
	Governmental Activities		Business-type Activities		Total	
	2006	2005	2006	2005	2006	2005
General Obligation Bonds	\$ 568,496	\$ 643,906	\$ 14,196,756	\$ 4,656,618	\$ 14,765,252	\$ 5,300,524

The Town of Front Royal's total debt increased by \$9,464,728 (179 percent) during the current fiscal year. The key factor in this increase was the issue of a \$10,315,000 general obligation bond in the Water Fund.

The Town of Front Royal and its water and sewer functions maintain an "A" rating from Standard and Poor's and from Moody's for general obligation debt.

State statutes limit the amount of general obligation debt a governmental entity may issue to 10 percent of its total taxable assessed valuation. The current debt limitation for the Town of Front Royal is \$78,458,758 which is significantly in excess of the Town's outstanding general obligation debt.

Additional information on the Town of Front Royal's long-term debt can be found in note IV. G on pages 46 – 48 of this report.

Economic Factors and Next Year's Budgets and Rates

- The unemployment rate for the Town of Front Royal is currently 2.5 percent, which is less than a year ago.
- This compares favorably to the state's average unemployment rate of 3.1 percent and the national average rate of 4.4 percent.
- Inflationary trends in the region compare favorably to national indices.

All of these factors were considered in preparing the Town of Front Royal, Virginia's budget for the 2007 fiscal year.

During the current fiscal year, unreserved fund balance in the general fund increased to \$5,391,587. Town of Front Royal has appropriated none of this amount for spending in the 2007 fiscal year budget. It also is available to obviate the need for the transfer of additional resources to the general fund from the electric fund.

The electric distribution operation's rates were increased for the 2004 budget year. This increase was the result of a new contract for the purchase of wholesale electric power. Unfortunately, the new contract brought to an end the extremely profitable rates that were negotiated five years ago. Consequently, the Town's wholesale rates increased almost 32 percent necessitating an increase in the retail rates. The Town Council has committed by ordinance to phase in annual increases of seven percent over three years in order to recover the increased cost.

Requests for Information

This report is designed to provide a general overview of the Town of Front Royal's finances for all those with an interest in the government's financial operations. Questions concerning any of the information provided in this report or requests for additional financial information should be directed to the Office of the Director of Finance, 16 North Royal Avenue, P.O. Box 1560, Front Royal, Virginia 22630-1560.

TOWN OF FRONT ROYAL, VIRGINIA
GOVERNMENT WIDE STATEMENT OF NET ASSETS
JUNE 30, 2006

	Primary Government		
	Governmental Activities	Business-type Activities	Total
Assets			
Cash and cash equivalents	\$ 2,795,748	\$ 17,644,916	\$ 20,440,664
Investments	5,197,889	6,385,505	11,583,394
Receivables (net, where applicable, of allowance for uncollectibles)			
Delinquent taxes, including penalties	231,990	-	231,990
Accrued interest	1,300	2,450	3,750
Accounts	-	2,010,615	2,010,615
Other	23,127	6,510	29,637
Internal balances	(717,531)	717,531	-
Due from other governments	51,116	-	51,116
Inventories and other assets	84,563	643,983	728,546
Temporarily restricted assets			
Cash and cash equivalents	17,664	185,902	203,566
Deferred charges	-	181,214	181,214
Escrow deposit	-	-	-
Capital assets (net of accumulated depreciation)			
Land	1,117,508	1,368,968	2,486,476
Construction in progress	77,927	-	77,927
Buildings and improvements	2,465,791	3,826,184	6,291,975
Utility distribution systems	-	27,183,626	27,183,626
Vehicles	374,887	818,196	1,193,083
Machinery and equipment	987,020	751,156	1,738,176
Infrastructure	70,169,956	-	70,169,956
Total Assets	82,878,955	61,726,756	144,605,711
Liabilities			
Accounts payable	411,068	1,013,683	1,424,751
Cash advances	15,677	-	15,677
Accrued interest payable	-	75,044	75,044
Liabilities payable with restricted assets	14,004	169,329	183,333
Noncurrent liabilities			
Due within one year	70,495	553,467	623,962
Due in more than one year	1,051,749	14,159,395	15,211,144
Total Liabilities	1,562,993	15,970,918	17,533,911
Net Assets			
Invested in capital assets, net of related debt	74,624,593	19,751,368	94,375,961
Unrestricted	6,691,369	26,004,470	32,695,839
Total Net Assets	\$ 81,315,962	\$ 45,755,838	\$ 127,071,800

The notes to the financial statements are an integral part of this statement.

**TOWN OF FRONT ROYAL, VIRGINIA
GOVERNMENT WIDE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2006**

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Change in Net Assets		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Government		
					Governmental Activities	Business-type Activities	Total
Primary government:							
Governmental activities							
General government	\$ 2,326,711	\$ 131,037		\$ 43,416	\$ (2,152,258)	\$ -	\$ (2,152,258)
Public safety	3,276,981	406,081	415,047		(2,455,853)	-	(2,455,853)
Public works	2,574,487	18,759	1,032,943		(1,522,785)	-	(1,522,785)
Planning, zoning, and community development	484,132	77,858			(406,274)	-	(406,274)
Culture and recreation	52,985				(52,985)	-	(52,985)
Interest on long-term debt	28,180				(28,180)	-	(28,180)
Infrastructure depreciation - unallocated	3,591,054				(3,591,054)	-	(3,591,054)
Total governmental activities	12,334,530	633,735	1,447,990	43,416	(10,209,389)	-	(10,209,389)
Business-type activities							
Electric	9,523,363	11,507,238	-	-	-	1,983,875	1,983,875
Water	1,964,023	3,198,691	-	62,127	-	1,296,795	1,296,795
Sewer	2,285,966	3,011,979	-	9,579	-	735,592	735,592
Refuse	828,583	806,968	-	-	-	(21,615)	(21,615)
Total business-type activities	14,601,935	18,524,876	-	71,706	-	3,994,647	3,994,647
Total primary government	\$ 26,936,465	\$ 19,158,611	\$ 1,447,990	\$ 115,122	(10,209,389)	3,994,647	(6,214,742)
General Revenues							
Property taxes					1,280,730	-	1,280,730
Sales taxes					586,133	-	586,133
Business and occupational taxes					740,268	-	740,268
Franchise taxes					213,601	-	213,601
Consumer taxes					191,554	-	191,554
Alcoholic beverage taxes					16,316	-	16,316
Meals and lodging taxes					1,578,910	-	1,578,910
Virginia personal property tax reduction					280,041	-	280,041
Other general taxes					583,928	-	583,928
Unrestricted investment earnings					209,469	497,182	706,651
Gain on sale of capital assets and other recoveries					53,342	-	53,342
Transfers					2,141,432	(2,141,432)	-
Total general revenues and transfers					7,875,724	(1,644,250)	6,231,474
Change in net assets					(2,333,665)	2,350,397	16,732
Net assets - beginning					83,649,627	43,405,441	127,055,068
Net assets - ending					\$ 81,315,962	\$ 45,755,838	\$ 127,071,800

The notes to the financial statements are an integral part of this statement.

**TOWN OF FRONT ROYAL, VIRGINIA
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2006**

	General	Other Governmental Funds	Total Governmental Funds
Assets			
Cash and cash equivalents	\$ 1,189,610	\$ 1,606,138	\$ 2,795,748
Investments	5,197,889	-	5,197,889
Receivables (net, where applicable, of allowance for uncollectibles)			
Delinquent taxes, including penalties	277,231	(45,241)	231,990
Accrued interest	1,300	-	1,300
Other	23,127	-	23,127
Due from other governments	51,116	-	51,116
Interfund advances	-	4,500	4,500
Inventories and other assets	84,563	-	84,563
Cash - restricted	17,664	-	17,664
Total Assets	6,842,500	1,565,397	8,407,897
Liabilities and Fund Balances			
Liabilities			
Accounts payable	237,296	(50)	237,246
Cash advances	12,802	2,875	15,677
Accrued liabilities	173,822	-	173,822
Deferred revenue	287,014	4,233	291,247
Interfund advances	625,000	97,031	722,031
Liabilities payable with restricted assets	14,004	-	14,004
Total Liabilities	1,349,938	104,089	1,454,027
Fund balances			
Reserved for			
Inventory	60,975	-	60,975
Restricted use	40,000	-	40,000
Unreserved, reported in			
General fund	5,391,587	-	5,391,587
Special revenue funds	-	1,460,920	1,460,920
Capital projects funds	-	388	388
Total Fund Balances	5,492,562	1,461,308	6,953,870
Total Liabilities and Fund Balances	\$ 6,842,500	\$ 1,565,397	

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

Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds.	75,193,089
Other long-term assets are not available to pay for current-period expenditures and, therefore, are deferred in the funds.	291,247
Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds.	(1,122,244)
Net assets of governmental activities	<u>\$ 81,315,962</u>

The notes to the financial statements are an integral part of this statement.

TOWN OF FRONT ROYAL, VIRGINIA
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2006

	General	Debt Service	Other Governmental Funds	Total Governmental Funds
Revenues				
Taxes				
Property	\$ 1,053,326	\$ -	\$ 295,902	\$ 1,349,228
Sales	586,133	-	-	586,133
Business and occupational	740,268	-	-	740,268
Franchise	213,601	-	-	213,601
Consumer	191,554	-	-	191,554
Vehicle licenses	246,458	-	-	246,458
Bank stock	197,212	-	-	197,212
Meals and lodging	1,259,249	-	319,661	1,578,910
Permits, fees, and licenses	77,858	-	-	77,858
Fines and forfeitures	307,275	-	-	307,275
Revenues from use of money & property	209,469	-	-	209,469
Charges for services	84,363	-	-	84,363
Miscellaneous	115,343	-	3,324	118,667
Recovered costs	75,552	-	23,254	98,806
Payment in lieu of taxes	80,200	-	-	80,200
Intergovernmental	1,847,929	-	-	1,847,929
Total revenues	<u>7,285,790</u>	<u>-</u>	<u>642,141</u>	<u>7,927,931</u>
Expenditures				
General government				
Legislative	135,379	-	-	135,379
Executive	1,188,427	-	-	1,188,427
Legal	215,991	-	-	215,991
Finance	673,576	-	-	673,576
Public safety				
Police	2,926,282	-	-	2,926,282
Fire protection	88,073	-	-	88,073
Planning, zoning, and community development	306,286	-	128,590	434,876
Engineering and public works	2,312,554	-	-	2,312,554
Parks and recreation	47,596	-	-	47,596
Nondepartmental	584,781	-	-	584,781
Debt Service				
Principal	-	75,410	-	75,410
Interest	-	28,180	-	28,180
Capital outlay	-	-	7,246	7,246
Total expenditures	<u>8,478,945</u>	<u>103,590</u>	<u>135,836</u>	<u>8,718,371</u>
Excess (deficiency) of revenues over (under) expenditures	<u>(1,193,155)</u>	<u>(103,590)</u>	<u>506,305</u>	<u>(790,440)</u>
Other Financing Sources (Uses)				
Transfers in	2,141,432	103,590	-	2,245,022
Transfers (out)	-	-	(103,590)	(103,590)
Total other financing sources and uses	<u>2,141,432</u>	<u>103,590</u>	<u>(103,590)</u>	<u>2,141,432</u>
Net change in fund balances	<u>948,277</u>	<u>-</u>	<u>402,715</u>	<u>1,350,992</u>
Fund balances - beginning	<u>4,544,285</u>	<u>-</u>	<u>1,058,593</u>	<u>5,602,878</u>
Fund balances - ending	<u>\$ 5,492,562</u>	<u>\$ -</u>	<u>\$ 1,461,308</u>	<u>\$ 6,953,870</u>

The notes to the financial statements are an integral part of this statement.

**TOWN OF FRONT ROYAL, VIRGINIA
RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2006**

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

Net change in fund balances - total governmental funds	\$ 1,350,992
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.	(3,650,190)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.	(68,498)
The issuance of long term debt (e.g. bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets. Also, governmental funds report the effect of issuance costs, premiums, discounts, and similar items when debt is first issued, whereas these amount are deferred and amortized in the statement of activities. This amount is the net effect of these differences in the treatment of long-term debt and related items.	75,410
Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.	<u>(41,379)</u>
Change in net assets of governmental activities	<u>\$ (2,333,665)</u>

The notes to the financial statements are an integral part of this statement.

**TOWN OF FRONT ROYAL, VIRGINIA
GENERAL FUND
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN
FUND BALANCES - BUDGET AND ACTUAL
FOR THE YEAR ENDED JUNE 30, 2006**

	Budgeted Amounts			Variance Positive (Negative)
	Original	Final	Actual Amounts	
Revenues				
General property taxes	\$ 1,071,490	\$ 1,071,490	\$ 1,053,326	\$ (18,164)
Other local taxes	3,236,126	3,236,126	3,514,675	278,549
Permits, fees, and licenses	87,350	87,350	77,858	(9,492)
Fines and forfeitures	135,300	135,300	307,275	171,975
Revenues from use of money & property	57,400	57,400	209,469	152,069
Charges for services	106,900	106,900	84,363	(22,537)
Miscellaneous	38,000	38,000	115,343	77,343
Recovered costs	50,000	50,000	75,552	25,552
Intergovernmental	2,280,017	2,285,472	1,847,929	(437,543)
Total revenues	7,062,583	7,068,038	7,285,790	217,752
Expenditures				
General Government				
Legislative	175,383	168,723	135,379	33,344
Executive	1,323,388	1,456,957	1,188,427	268,530
Legal	228,340	232,796	215,991	16,805
Finance	783,372	804,904	673,576	131,328
Total general government	2,510,483	2,663,380	2,213,373	450,007
Public Safety				
Police	2,961,469	2,971,665	2,926,282	45,383
Fire protection	50,000	50,000	88,073	(38,073)
Total public safety	3,011,469	3,021,665	3,014,355	7,310
Subtotal	5,521,952	5,685,045	5,227,728	457,317
Planning and zoning	433,981	621,795	306,286	315,509
Public works and engineering	2,398,576	3,014,794	2,312,554	702,240
Parks and recreation	47,596	47,596	47,596	-
Non-departmental	814,410	730,956	584,781	146,175
Total Expenditures	9,216,515	10,100,186	8,478,945	1,621,241
Excess (Deficiency) of Revenues over (under) Expenditures	(2,153,932)	(3,032,148)	(1,193,155)	1,838,993
Other Financing Sources (Uses)				
Transfers in	2,298,932	2,298,932	2,141,432	(157,500)
Transfers (out)	(145,000)	(145,000)	-	145,000
Total other financing sources (uses)	2,153,932	2,153,932	2,141,432	(12,500)
Net change in fund balances	-	(878,216)	948,277	1,826,493
Fund balances - beginning	4,544,285	4,544,285	4,544,285	-
Fund balances - ending	\$ 4,544,285	\$ 3,666,069	\$ 5,492,562	\$ 1,826,493

The notes to the financial statements are an integral part of this statement.

TOWN OF FRONT ROYAL, VIRGINIA
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
JUNE 30, 2006

	Business-type Activities - Enterprise Funds			
	Electric Current Year	Electric Prior Year	Water Current Year	Water Prior Year
Assets				
Current assets				
Cash and cash equivalents	\$ 5,121,283	\$ 603,910	\$ 11,530,699	\$ 952,776
Investments	2,871,967	6,226,231	2,142,905	1,547,205
Due from other funds	625,000	750,000	46,266	123,215
Interest receivable	200	200	2,250	2,250
Accounts receivable (net of allowance for uncollectibles)	1,263,119	1,333,251	342,500	276,338
Other receivables	6,157	8,327	-	1,090
Inventories	517,781	506,491	63,101	79,633
Total current assets	10,405,507	9,428,410	14,127,721	2,982,507
Noncurrent assets				
Restricted cash - cash equivalents	147,154	194,201	22,175	21,150
Deferred charges	-	-	130,230	71,474
Escrow deposit	-	-	-	-
	147,154	194,201	152,405	92,624
Capital assets				
Land, buildings and structures	1,430,654	1,430,654	2,863,640	2,863,640
Utility distribution systems	7,122,612	6,972,560	18,989,285	18,857,949
Vehicles	827,511	827,511	320,282	320,283
Equipment	555,204	520,829	384,860	382,283
Less accumulated depreciation	(4,906,550)	(4,748,294)	(8,529,823)	(8,110,243)
Total capital assets (net of accumulated depreciation)	5,029,431	5,003,260	14,028,244	14,313,912
Total noncurrent assets	5,176,585	5,197,461	14,180,649	14,406,536
Total Assets	15,582,092	14,625,871	28,308,370	17,389,043
Liabilities				
Current liabilities				
Accounts payable	923,111	744,832	25,733	160,172
Accrued interest payable	-	-	57,206	23,800
General obligation bonds - current	-	-	276,734	387,431
Total current liabilities	923,111	744,832	359,673	571,403
Noncurrent liabilities				
Customer deposits payable	147,154	178,978	22,175	21,150
Compensated absences	35,485	25,363	98,394	106,536
General obligation bonds payable	-	-	11,979,144	1,940,878
Premium on general obligation bonds payable	-	-	259,073	-
Total noncurrent liabilities	182,639	204,341	12,358,786	2,068,564
Total Liabilities	1,105,750	949,173	12,718,459	2,639,967
Net Assets				
Invested in capital assets, net of related debt	5,029,431	5,003,261	1,772,360	16,648,496
* Unrestricted	9,446,911	8,673,437	13,817,551	(1,899,420)
Total Net Assets	\$ 14,476,342	\$ 13,676,698	\$ 15,589,911	\$ 14,749,076

The notes to the financial statements are an integral part of this statement.

**TOWN OF FRONT ROYAL, VIRGINIA
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
JUNE 30, 2006**

EXHIBIT VII
(Continued)

	Business-type Activities - Enterprise Funds				
	Sewer	Sewer	Refuse	Refuse	Totals
	Current Year	Prior Year	Current Year	Prior Year	Current Year
Assets					
Current assets					
Cash and cash equivalents	\$ 992,934	\$ 952,776	\$ -	\$ -	\$ 17,644,916
Investments	1,182,131	107,117	188,502	221,096	6,385,505
Due from other funds	46,265	123,215	-	-	717,531
Interest receivable	-	-	-	-	2,450
Accounts receivable (net of allowance for uncollectibles)	310,058	254,087	94,938	89,932	2,010,615
Other receivables	201	9,554	152	-	6,510
Inventories	63,101	79,633	-	-	643,983
Total current assets	2,594,690	1,526,382	283,592	311,028	27,411,510
Noncurrent assets					
Restricted cash - cash equivalents	16,573	16,599	-	-	185,902
Deferred charges	50,984	62,110	-	-	181,214
Escrow deposit	-	16,600	-	-	-
	67,557	95,309	-	-	367,116
Capital assets					
Land, buildings and structures	4,061,137	4,061,137	-	-	8,355,431
Utility distribution systems	21,611,152	21,576,549	-	-	47,723,049
Vehicles	320,282	320,282	897,359	897,359	2,365,434
Equipment	537,233	493,834	465,767	452,040	1,943,064
Less accumulated depreciation	(12,170,393)	(11,507,148)	(832,082)	(748,795)	(26,438,848)
Total capital assets (net of accumulated depreciation)	14,359,411	14,944,654	531,044	600,604	33,948,130
Total noncurrent assets	14,426,968	15,039,963	531,044	600,604	34,315,246
Total Assets	17,021,658	16,566,345	814,636	911,632	61,726,756
Liabilities					
Current liabilities					
Accounts payable	58,659	1,314	6,180	7,589	1,013,683
Accrued interest payable	17,838	23,800	-	-	75,044
General obligation bonds - current	276,733	387,431	-	-	553,467
Total current liabilities	353,230	412,545	6,180	7,589	1,642,194
Noncurrent liabilities					
Customer deposits payable	-	-	-	-	169,329
Compensated absences	98,833	107,808	24,321	29,490	257,033
General obligation bonds payable	1,664,145	1,940,878	-	-	13,643,289
Premium on general obligation bonds payable	-	-	-	-	259,073
Total noncurrent liabilities	1,762,978	2,048,686	24,321	29,490	14,328,724
Total Liabilities	2,116,208	2,461,231	30,501	37,079	15,970,918
Net Assets					
Invested in capital assets, net of related debt	12,418,532	17,279,238	531,045	600,604	19,751,368
Unrestricted	2,486,918	(3,174,124)	253,090	273,949	26,004,470
Total Net Assets	\$ 14,905,450	\$ 14,105,114	\$ 784,135	\$ 874,553	\$ 45,755,838

The notes to the financial statements are an integral part of this statement.

TOWN OF FRONT ROYAL, VIRGINIA
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS
FOR THE YEAR ENDED JUNE 30, 2006

	Business-type Activities - Enterprise Funds			
	Electric	Electric	Water	Water
	Current Year	Prior Year	Current Year	Prior Year
Operating revenues				
Charges for sales and services				
Electric sales	\$ 11,407,870	\$ 11,296,186	\$ -	\$ -
Water and sewer sales	-	-	2,820,345	2,458,133
Installation and connection charges	105,058	38,643	363,983	383,880
Refuse service fees	-	-	-	-
Miscellaneous revenues	(5,690)	11,932	14,363	14,316
Total operating revenues	<u>11,507,238</u>	<u>11,346,761</u>	<u>3,198,691</u>	<u>2,856,329</u>
Operating expenses				
Personal service	609,963	577,054	673,430	676,253
Contractual service	432,379	299,968	104,018	103,374
Electric power	7,816,545	7,506,632	-	-
Depreciation	310,003	304,249	419,580	417,089
Other charges	650,033	533,551	715,821	1,146,891
Operating expenses capitalized	(301,798)	(146,801)	(69,208)	(112,154)
Total operating expenses	<u>9,517,125</u>	<u>9,074,653</u>	<u>1,843,641</u>	<u>2,231,453</u>
Operating income	<u>1,990,113</u>	<u>2,272,108</u>	<u>1,355,050</u>	<u>624,876</u>
Nonoperating revenues (expenses)				
Investment earnings	270,768	98,840	150,210	41,201
Interest expense	(6,238)	(7,956)	(114,466)	(91,130)
Bond issuance costs	-	-	(5,916)	(5,916)
Total nonoperating revenue (expenses)	<u>264,530</u>	<u>90,884</u>	<u>29,828</u>	<u>(55,845)</u>
Income before contributions and transfers	<u>2,254,643</u>	<u>2,362,992</u>	<u>1,384,878</u>	<u>569,031</u>
Transfers and contributions				
Capital contributions	-	-	62,127	226,919
Transfers in	-	-	-	-
Transfers (out)	(1,454,999)	(1,797,300)	(606,170)	(129,300)
Change in net assets	<u>799,644</u>	<u>565,692</u>	<u>840,835</u>	<u>666,650</u>
Total net assets - beginning of year	<u>13,676,698</u>	<u>13,111,006</u>	<u>14,749,076</u>	<u>14,082,426</u>
Total net assets - end of year	<u>\$14,476,342</u>	<u>\$13,676,698</u>	<u>\$15,589,911</u>	<u>\$14,749,076</u>

The notes to the financial statements are an integral part of this statement.

TOWN OF FRONT ROYAL, VIRGINIA
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS
FOR THE YEAR ENDED JUNE 30, 2006

	Business-type Activities - Enterprise Funds				
	Sewer	Sewer	Refuse	Refuse	Totals
	Current Year	Prior Year	Current Year	Prior Year	Current Year
Operating revenues					
Charges for sales and services					
Electric sales	\$ -	\$ -	\$ -	\$ -	\$11,407,870
Water and sewer sales	2,770,865	2,388,442	-	-	5,591,210
Installation and connection charges	240,864	285,302	-	-	709,905
Refuse service fees	-	-	806,968	779,275	806,968
Miscellaneous revenues	250	405	-	-	8,923
Total operating revenues	<u>3,011,979</u>	<u>2,674,149</u>	<u>806,968</u>	<u>779,275</u>	<u>18,524,876</u>
Operating expenses					
Personal service	795,936	833,024	580,419	483,571	2,659,748
Contractual service	275,004	40,487	29,642	6,338	841,043
Electric power	-	-	-	-	7,816,545
Depreciation	663,245	661,295	83,287	82,448	1,476,115
Other charges	495,792	1,064,413	135,235	166,775	1,996,881
Operating expenses capitalized	(25,024)	(60,082)	-	-	(396,030)
Total operating expenses	<u>2,204,953</u>	<u>2,539,137</u>	<u>828,583</u>	<u>739,132</u>	<u>14,394,302</u>
Operating income	<u>807,026</u>	<u>135,012</u>	<u>(21,615)</u>	<u>40,143</u>	<u>4,130,574</u>
Nonoperating revenues (expenses)					
Investment earnings	69,107	29,419	7,097	3,781	497,182
Interest expense	(75,097)	(91,130)	-	-	(195,801)
Bond issuance costs	(5,916)	(5,916)	-	-	(11,832)
Total nonoperating revenue (expenses)	<u>(11,906)</u>	<u>(67,627)</u>	<u>7,097</u>	<u>3,781</u>	<u>289,549</u>
Income before contributions and transfers	<u>795,120</u>	<u>67,385</u>	<u>(14,518)</u>	<u>43,924</u>	<u>4,420,123</u>
Transfers and contributions					
Capital contributions	9,579	-	-	-	71,706
Transfers in	-	-	-	-	-
Transfers (out)	(4,363)	(129,300)	(75,900)	(71,500)	(2,141,432)
Change in net assets	<u>800,336</u>	<u>(61,915)</u>	<u>(90,418)</u>	<u>(27,576)</u>	<u>2,350,397</u>
Total net assets - beginning of year	<u>14,105,114</u>	<u>14,167,029</u>	<u>874,553</u>	<u>902,129</u>	<u>43,405,441</u>
Total net assets - end of year	<u>\$14,905,450</u>	<u>\$14,105,114</u>	<u>\$ 784,135</u>	<u>\$ 874,553</u>	<u>\$45,755,838</u>

The notes to the financial statements are an integral part of this statement.

**TOWN OF FRONT ROYAL, VIRGINIA
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE YEAR ENDED JUNE 30, 2006**

	Business-type Activities - Enterprise Funds				Totals
	Electric	Water	Sewer	Refuse	
Cash Flows from Operating Activities					
Receipts from customers and users	\$ 11,579,539	\$ 3,133,620	\$ 2,965,360	\$ 801,810	\$ 18,480,329
Payments to suppliers	(8,461,994)	(926,269)	(644,169)	(166,286)	(10,198,718)
Payments to employees	(599,841)	(681,572)	(804,911)	(585,588)	(2,671,912)
Net cash provided by operating activities	2,517,704	1,525,779	1,516,280	49,936	5,609,699
Cash Flows from Noncapital Financing Activities					
Transfers to other funds	(1,454,999)	(606,170)	(4,363)	(75,900)	(2,141,432)
Repayment of interfund advances	125,000	76,950	76,950	-	278,900
Net cash provided (used) by capital and related financing activities	(1,329,999)	(529,220)	72,587	(75,900)	(1,862,532)
Cash Flows from Capital and Related Financing Activities					
Debt issuance	-	10,574,072	-	-	10,574,072
Capital contributions	-	62,127	9,579	-	71,706
Acquisition and construction of capital assets	(336,172)	(133,913)	(78,002)	(13,728)	(561,815)
Principal paid on capital debt	-	(387,431)	(387,431)	-	(774,862)
Interest paid on capital debt	(6,238)	(86,976)	(86,975)	-	(180,189)
Net cash provided (used) by capital and related financing activities	(342,410)	10,027,879	(542,829)	(13,728)	9,128,912
Cash Flows from Investing Activities					
(Purchases)/sale of investments	3,354,263	(595,700)	(1,075,013)	32,595	1,716,145
Interest and dividends received	270,768	150,210	69,107	7,097	497,182
Net cash provided (used) by investing activities	3,625,031	(445,490)	(1,005,906)	39,692	2,213,327
Net increase in cash and cash equivalents	4,470,326	10,578,948	40,132	-	15,089,406
Cash and cash equivalents July 1, 2005	798,111	973,926	969,375	-	2,741,412
Cash and cash equivalents June 30, 2006	\$ 5,268,437	\$ 11,552,874	\$ 1,009,507	\$ -	\$ 17,830,818
Reconciliation of operating income to net cash provided (used) by operating activities					
Operating income	\$ 1,990,113	\$ 1,355,050	\$ 807,026	\$ (21,615)	\$ 4,130,574
Adjustments to reconcile operating income to net cash provided (used) by operating activities:					
Depreciation expense	310,003	419,580	663,245	83,287	1,476,115
(Increase) decrease in accounts receivable	70,131	(66,161)	(55,971)	(5,006)	(57,007)
(Increase) decrease in other receivables	2,170	1,090	9,353	(152)	12,461
(Increase) decrease in inventories	(11,290)	16,532	16,532	-	21,774
(Increase) decrease in deferred charges	-	(58,756)	11,126	-	(47,630)
(Increase) decrease in escrow deposit	-	-	16,600	-	16,600
Increase (decrease) in customer deposits	(31,824)	1,025	-	-	(30,799)
Increase (decrease) in accounts payable	178,279	(134,439)	57,345	(1,409)	99,776
Increase (decrease) in compensated absences	10,122	(8,142)	(8,976)	(5,169)	(12,165)
Total adjustments	527,591	170,729	709,254	71,551	1,479,125
Net cash provided by operating activities	\$ 2,517,704	\$ 1,525,779	\$ 1,516,280	\$ 49,936	\$ 5,609,699
Noncash investing, capital, and financing activities					
Capital assets contributed by developers	\$ -	\$ 62,127	\$ 9,579	\$ -	\$ 71,706

The notes to the financial statements are an integral part of this statement.

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

I. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Town of Front Royal, Virginia (the Town) have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The following summary of the more significant policies is presented to assist the reader in interpreting the financial statements and other data contained in this report. These policies, as presented, should be viewed as an integral part of the accompanying financial statements.

In June 1999, GASB issued Statement No. 34 *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*. This statement, known as the "Reporting Model" statement, affects the way the Town prepares and presents financial information. State and local governments traditionally have used a financial reporting model substantially different from the one used to prepare private sector financial reports.

GASB Statement No. 34 established requirements and a reporting model for the annual financial reports of state and local governments. The Statement was developed to make annual reports easier to understand and more useful to the people who use governmental financial information to make decisions. The significant reporting changes are summarized as follows:

Management's Discussion and Analysis - GASB Statement No. 34 requires that financial statements be accompanied by a narrative introduction and analytical overview of the government's financial activities in the form of "management's discussion and analysis" (MD&A). This analysis is similar to analysis the private sector provides in their annual reports.

Government-wide financial statements - The reporting model includes financial statements prepared using full accrual accounting for all the government's activities. This approach includes not just current assets and liabilities (such as cash and accounts payable) but also capital assets and long-term liabilities (such as buildings and infrastructure, including bridges and road, and general obligations debt). Accrual accounting also reports all of the revenues and cost of providing services each year, not just those received or paid in the current year or soon thereafter.

Schedule of Net Assets - The Schedule of Net Assets is designed to display the financial position of the primary government (government and business-type activities) and its directly presented component units. Governments will report all capital assets, including infrastructure, in the government-wide Schedule of Net Assets and will report depreciation expense - the cost of "using up" capital assets - in the Schedule of Activities. The net assets of a government will be broken down into three categories - 1) invested in capital assets, net of related debt; 2) restricted; and 3) unrestricted.

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

Schedule of Program Activities - The new government-wide statement of activities reports expenses and revenues in a format that focuses on the cost of each of the government's functions. The expense of individual functions is compared to the revenues generated directly by the function (for instance, through user charges or intergovernmental grants).

Budgetary Comparison Schedules - Demonstrating compliance with the adopted budget is an important component of a government's accountability to the public. Many citizens participate in one way or another in the process of establishing the annual operating budgets of state and local governments, and have a keen interest in following the actual financial progress of their governments over the course of the year. Many governments revise their original budgets over the course of the year for a variety of reasons. Under the new reporting model, governments will continue to provide budgetary comparison information in their annual reports. An important change, however, is a requirement to add the government's original budget to the current comparison of final budget and actual results.

A. Reporting Entity

The Town is an incorporated municipal government governed by an elected mayor and six-member council. As required by generally accepted accounting principles, these financial statements present the Town and its component units, entities for which the Town is considered to be financially accountable. Financial accountability is defined as appointment of a voting majority of the component unit's board and either (A) the ability to impose will by the primary government, or (B) the possibility that the component unit will provide a financial benefit to or impose a financial burden on the primary government.

Based upon the above, all potential component units were evaluated for inclusion in the reporting entity and it was determined there are no material component units requiring inclusion reporting.

B. Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e. the statement of net assets and the statement of changes in net assets) report information on all of the nonfiduciary activities of the primary government. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

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

Separate financial statements are provided for governmental funds and proprietary funds. Major individual governmental funds and major individual proprietary funds are reported as separate columns in the fund financial statements.

C. Measurement Focus, Basis of Accounting and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund and fiduciary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be *available* when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 45 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes, franchise taxes, licenses, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. Only the portion of special assessments receivable due within the current fiscal period is considered to be susceptible to accrual as revenue of the current period. All other revenue items are considered to be measurable and available only when cash is received by the government.

The government reports the following major governmental funds:

The *general fund* is the Town's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

The *debt service fund* accounts for the resources accumulated and payments made for principal and interest on long-term general obligation debt of governmental funds.

Additionally, the government reports the following non-major government funds:

The *special revenue fund* accounts for revenue sources that are legally restricted to expenditures for specific purposes (not including major capital projects).

The *capital projects fund* accounts for the acquisition of fixed assets or construction of major capital projects not being financed by proprietary or non-expendable trust funds.

The government reports the following major proprietary funds:

The *water and sewer funds* account for the activities of the Town's water and sewer operations.

The *electric fund* accounts for the activities of the Town's electric production and distribution operations.

The *refuse fund* accounts for the activities of the Town's refuse collection and processing operation.

Private-sector standards of accounting and financial reporting issued prior to December 2, 1989, generally are followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The government has elected to follow subsequent private-sector guidance.

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are payments-in-lieu of taxes and other charges between the government's water and sewer function and various other functions of the government. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

Amounts reported as program revenues include 1) charges to customers or applicants for goods, services, or privileges provided, 2) operating grants and contributions, and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes.

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the water and sewer enterprise funds, electric enterprise fund, and refuse enterprise fund are charges to customers for sales and services. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the government's policy to use restricted resources first, then unrestricted resources as they are needed.

D. Assets, Liabilities and Net Assets or Equity

1. Deposits and Investments

The Town's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition. Investments are stated at fair value, which approximates cost due to the short-term nature of the investment maturities.

2. Receivables and Payables

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" or "advances to/from other funds." All other outstanding balances between funds are reported as "due to/from other funds." Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances."

Advances between funds, as reported in the fund financial statements, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

The trade and property tax receivables are shown net of an allowance for doubtful accounts. The allowance for doubtful accounts is determined using historical collection data and account analysis.

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

Real estate and personal property taxes are assessed annually by Warren County, Virginia for all property of record as of January 1. The Town bills and collects its own property taxes based on the assessed values provided by the County. Real estate taxes are levied annually on January 1 and are due on December 5. Personal property taxes are levied annually on January 1 and are due December 5 with proration of personal property taxes throughout the year.

Collections of real and personal property taxes between July 1 and August 15 of the subsequent fiscal year, classified as delinquent at June 30, are recorded as revenue for the fiscal year then ended, in accordance with the standards established by the Auditor of Public Accounts of the Commonwealth of Virginia. Liens attach to the property when the tax remains unpaid after July 1 of the following year. The billings are considered past due after the respective tax billing date at which time the applicable property is subject to a 10% penalty and interest is assessed 30 days therefrom.

3. Inventories and Other Assets

Inventory is valued at the lower of cost (first-in, first-out) or market. Inventory in the general fund consists of expendable supplies held for consumption. The cost is recorded as an expenditure at the time individual inventory items are purchased. Reported inventories are equally offset by a fund balance reserve, which indicates that they do not constitute "available spendable resources" even though they are a component of net current assets.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

4. Restricted Assets

Customer Deposits - Cash funds of the enterprise funds are restricted for customer deposits held.

Surety Bonds - Cash held in general fund for performance guarantees are held as a restricted cash asset.

5. Capital Assets

Capital assets, which include property, plant, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Such assets are recorded at cost or estimated historical cost if purchased or constructed. Donated fixed assets are recorded at their estimated fair value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized.

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets of business-type activities is included as part of the capitalized value of the assets constructed. The town has adopted the GFOA Capitalization Threshold recommendation of \$5,000.

Property, plant and equipment of the primary government are depreciated using the straight-line method over the following estimated useful lives:

Type of Asset	Years
Buildings	35 - 50
Improvements other than buildings	10 - 50
Equipment and vehicles	5 - 10
Infrastructure	30 - 50

In accordance with GASB 34, infrastructure has been capitalized retroactively effectively July 1, 2002. A summary of capitalized infrastructure is as follows:

Asset Classification	Asset Value		7/1/2002 Accumulated Depreciation	7/1/2002 Net Book Value
	Current Replacement	Deflated Current Replacement		
Roads	\$ 117,918,554	\$ 98,686,367	\$ 21,324,664	\$ 77,361,703
Sidewalks	11,019,780	7,158,924	3,340,831	3,818,093
Bridges	2,342,111	758,272	335,068	423,204
Road Land	21,508,812	2,846,581	-	2,846,581
	<u>\$ 152,789,257</u>	<u>\$ 109,450,144</u>	<u>\$ 25,000,563</u>	<u>\$ 84,449,581</u>

Roads and road land value were determined utilizing VDOT provided replacement cost and related valuation methods and information. Sidewalks were valued utilizing measured information and cost data provided by the Town's public works department. Bridges were valued by inspection reports and VDOT's valuation methods.

6. Compensated Absences

It is the Town's policy to permit employees to accumulate earned but unused vacation and sick pay benefits. The liability for unpaid accumulated sick leave is limited since the government does not have a full obligation when an employee separates from service. All vacation pay is accrued when incurred in the government-wide and proprietary fund financial statements.

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

7. Long-term Obligations

In the government-wide financial statements, and proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as an other financing source. Premiums received on debt issuances are reported as other financing sources, while discounts of debt issuances are reported as other financing uses. Issuance costs, even if withheld from the actual net proceeds received, are reported as debt service expenditures.

8. Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

9. Comparative Data/Reclassifications

Comparative total data for the prior year have been presented only for individual enterprise funds in the fund financial statements in order to provide an understanding of the changes in the financial position and operations of these funds. Certain amounts presented in prior year data has been reclassified to be consistent with current year's presentation.

II. RECONCILIATION OF GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

A. Explanation of certain differences between the governmental fund balance sheet and the government-wide statement of net assets

The governmental fund balance sheet includes a reconciliation between *fund balance - total governmental funds* and *net assets - governmental activities* as reported in the government-wide statement of net assets. One element of that reconciliation explains that "long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds." The details of this \$1,122,244 are as follows:

Description	Amount
Bonds/notes payable	\$ 568,496
Compensated absences	553,748
Net adjustment to reduce <i>fund balance - total governmental funds to arrive at net assets - governmental activities</i>	<u>\$ 1,122,244</u>

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

B. Explanation of certain differences between the governmental fund statement of revenues, expenditures, and changes in fund balances and the government-wide statement of activities

The governmental statement of revenues, expenditures, and changes in fund balances includes a reconciliation between *net changes in fund balances - total governmental funds and changes in net assets of governmental activities* as reported in the government-wide statement of activities. One element of that reconciliation explains that "Governmental funds report capital outlays as expenditures. However, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. The details of this \$3,650,190 difference is as follows:

Description	Amount
Capital outlay	\$ 223,407
Depreciation expense	(3,873,597)
Net adjustment to increase <i>net changes in fund balances -total governmental funds</i> to arrive at changes in net assets of governmental activities	<u>\$ (3,650,190)</u>

Another element of that reconciliation states that "the issuance of long-term debt (e.g., bonds, leases) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets." The details of this \$75,410 difference are as follows:

Description	Amount
Principal debt retirements of bonded/note debt	\$ 75,410
Net adjustment to decrease <i>net changes in fund balances - total governmental funds</i> to arrive at changes in net assets of governmental activities	<u>\$ 75,410</u>

III. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgetary Information

Annual budgets are adopted on a basis consistent with generally accepted accounting principles for all governmental funds except the capital project and debt service funds. All annual appropriations lapse at fiscal year end.

On or before April 1 of each year, all agencies of the government submit requests for appropriations to the government's manager so that a budget may be prepared. Before June 1 the proposed budget is presented to the government's council for review. The council holds public hearings and a final budget must be prepared and adopted no later than June 30.

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

The appropriated budget is prepared by fund, function, and department. The government's department heads may make transfers of appropriations within a department. Transfers of appropriations between departments require the approval of the council. The legal level of budgetary control (i.e., the level at which expenditures may not legally exceed appropriations) is the department level. The council made several general fund budgetary appropriations throughout the year, totaling \$883,671.

Encumbrance accounting is employed in governmental funds. Encumbrances (e.g., purchase orders, contracts) do not constitute expenditures or liabilities because the commitments will be reappropriated and honored during the subsequent year.

B. Excess of Expenditures over Appropriations

For the year ended June 30, 2006, expenditures exceeded appropriations in the following general fund department:

Department	Excess Expenditures Over Appropriations
Fire protection	\$ 38,073

C. Deficit Fund Equity

At June 30, 2006 Special Revenue Fund - Downtown Service District had a deficit fund balance as noted below:

Fund	Deficit
Downtown Service District	\$ 2,875

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

IV. DETAILED NOTES ON ALL FUNDS

A. Deposits and Investments

Deposits

As of June 30, 2006, the carrying amount of the Town's deposits with banks and savings institutions was \$2,677,570 and the bank balance was \$2,986,340. All of the Town's deposits are covered by federal depository insurance and collateralized in accordance with the Virginia Security for Public Deposits Act. Under the Act, banks holding public deposits in excess of the amounts insured by FDIC must pledge collateral in the amount of 50% of excess deposits to a collateral pool in the name of the State Treasury Board. Savings and loan institutions are required to collateralize 100% of deposits in excess of FDIC limits. The State Treasury Board is responsible for monitoring compliance by banks and savings and loans. The funds deposited in accordance with the requirements of the Act are considered fully secured and thus are not categorized below as to credit risk.

Investments

Statutes authorize local governments and other public bodies to invest in obligations of the United States or agencies thereof, obligations of the Commonwealth of Virginia or political subdivisions thereof, obligations of the International Bank for Reconstruction and Development (World Bank), the Asian Development Bank, the African Development Bank, "prime quality" commercial paper and certain corporate notes, banker's acceptances, repurchase agreements, and the State Treasurer's Local Government Investment Pool (LGIP).

As of June 30, 2006, the government had the following investments:

Investment Type	Fair Value	Maturity	
		1 Year	Over 1 Year
SunTrust US Government MM Fund	\$ 3,261,310	\$ 3,261,310	\$ -
Commercial Paper	5,165,470	5,165,470	-
Government and agency bonds/notes	6,417,924	6,417,924	-
Repurchase agreements	110,333	110,333	-
LGIP Pool	2,601,348	2,601,348	-
SNAP Pool	10,537,765	10,537,765	-
SunTrust US Government Fund	1,438,738	1,438,738	-
Total	\$ 29,532,888	\$ 29,532,888	\$ -

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

C. Receivables

Receivables as of year end for the government's individual major and nonmajor funds in the aggregate, including the applicable allowances for uncollectible accounts, are as follows:

	General	Electric	Water	Sewer	Refuse	Nonmajor	Total
Receivables:							
Delinquent taxes	\$ 280,935	\$ -	\$ -	\$ -	\$ -	\$ (45,241)	\$ 235,694
Accounts	-	1,242,928	254,995	212,991	76,012	-	1,786,926
Interest	1,300	200	2,250	-	-	-	3,750
Intergovernmental	51,116	-	-	-	-	-	51,116
Unbilled	-	707,049	186,304	161,627	53,570	-	1,108,550
Other	23,127	8,475	2,738	5,459	190	-	39,989
Less: allowance for uncollectibles	(3,704)	(689,176)	(101,537)	(69,818)	(34,682)	-	(898,917)
Net total receivables	\$ 352,774	\$ 1,269,476	\$ 344,750	\$ 310,259	\$ 95,090	\$ (45,241)	\$ 2,327,108

Governmental funds reported deferred revenue in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period. Governmental funds also defer revenue recognition in connection with resources that have been received, but not yet earned. At the end of the current fiscal year, the various components of the unearned revenue reported in the governmental funds were as follows:

Fund/Type	Unavailable	Unearned
General Fund - Property Taxes	\$ 287,014	\$ -
Special Revenue Fund - Property Taxes	4,233	-
	\$ 291,247	\$ -

D. Due from Other Governments

At June 30, 2006 amounts due from other governments were as follows:

Description/Payer	General
Commonwealth of Virginia	
Warren County, Virginia - Sales Tax	\$ 51,116

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

E. Capital Assets

Capital asset activity for the year ended June 30, 2006 was as follows:

Primary Government

	Beginning Balance	Increases	Decreases	Ending Balance
Governmental activities:				
Capital assets, not being depreciated				
Land	\$ 1,117,508	\$ -	\$ -	\$ 1,117,508
Construction in progress	77,927	-	-	77,927
Total capital assets, not being depreciated	1,195,435	-	-	1,195,435
Capital assets, being depreciated				
Buildings and improvements	3,345,446	-	-	3,345,446
Vehicles	1,289,788	102,666	-	1,392,454
Equipment	2,570,581	120,741	(28,889)	2,662,433
Infrastructure	109,527,139	-	-	109,527,139
Total capital assets being depreciated	116,732,954	223,407	(28,889)	116,927,472
Less accumulated depreciation for				
Buildings and improvements	(793,011)	(86,644)	-	(879,655)
Vehicles	(878,170)	(139,397)	-	(1,017,567)
Equipment	(1,647,800)	(56,502)	28,889	(1,675,413)
Infrastructure	(35,766,129)	(3,591,054)	-	(39,357,183)
Total accumulated depreciation	(39,085,110)	(3,873,597)	28,889	(42,929,818)
Net capital assets being depreciated	77,647,844	(3,650,190)	-	73,997,654
Governmental capital assets, net	\$ 78,843,279	\$ (3,650,190)	\$ -	\$ 75,193,089

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

	Beginning Balance	Increases	Decreases	Ending Balance
Business-type activities:				
Capital assets, not being depreciated				
Land	\$ 1,368,968	\$ -	\$ -	\$ 1,368,968
Total capital assets not being depreciated	1,368,968	-	-	1,368,968
Capital assets, being depreciated				
Buildings and improvements	6,986,463	-	-	6,986,463
Utility Distribution Systems	47,407,058	467,736	(151,745)	47,723,049
Vehicles	2,365,435	-	-	2,365,435
Equipment	1,848,986	94,078	-	1,943,064
Total capital assets, being depreciated	58,607,942	561,814	(151,745)	59,018,011
Less accumulated depreciation for				
Buildings and improvements	(2,960,851)	(199,429)	-	(3,160,280)
Utility Distribution Systems	(19,575,463)	(1,115,705)	151,745	(20,539,423)
Vehicles	(1,452,486)	(94,752)	-	(1,547,238)
Equipment	(1,125,679)	(66,229)	-	(1,191,908)
Total accumulated depreciation	(25,114,479)	(1,476,115)	151,745	(26,438,849)
Net capital assets being depreciated	33,493,463	(914,301)	-	32,579,162
Business-type activities	\$ 34,862,431	\$ (914,301)	\$ -	\$ 33,948,130

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

Depreciation expense was charged to functions/programs of the primary government as follows:

Activity	Depreciation
Governmental activities:	
General government	\$ 77,951
Public safety	106,159
Public works	81,443
Planning, zoning, and community development	15,315
Culture and recreation	1,675
Infrastructure depreciation	3,591,054
Total depreciation expense - governmental activities	<u>\$ 3,873,597</u>
Business-type activities:	
Electric	\$ 310,003
Water	419,580
Sewer	663,245
Refuse	83,287
Total depreciation expense - business-type activities	<u>\$ 1,476,115</u>

F. Interfund Advances/Transfers

The composition and activity of interfund advances/transfers for 2006 is as follows:

Advanced to	Advanced from	Amount
General Fund	Electric	\$ 625,000
Special Revenue	Water	46,265
Special Revenue	Sewer	46,265
		<u>\$ 717,530</u>

G. Long-Term Debt

General Obligation Bonds. The Town issues general obligation bonds to provide funds for the acquisition and construction of major capital facilities and for refunding of general obligation bonds. General obligation bonds have been issued for both general government and proprietary activities. These bonds are reported in the proprietary funds if they are expected to be repaid from proprietary fund revenues. General obligation bonds are direct obligations and pledge the full faith and credit of the Town. These bonds generally are issued as serial bonds with amounts of principal maturing each year.

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

General obligation bonds and notes outstanding at June 30, 2006 are as follows:

\$5,655,523 2002 series general obligation refunding bond, issued November 14, 2002 due in increasing annual maturities starting with \$135,131 in 2002 and increasing to \$502,674 in 2013, with interest at 3.22%.	\$ 3,881,756
\$2,275,000, 1998 series public improvement bonds, issued June 30, 1998, due in annual installments of \$547,966 through June 30, 2001, and \$97,031 from June 30, 2002 through June 30, 2013 including interest at 4.27% and 4.67%.	568,496
\$10,315,000, 2006 series general obligation bonds, issued June 8, 2006 due in increasing annual maturities starting with \$330,000 in 2007 and increasing to \$780,000 in 2026, with interest at 3.63% to 4.95%.	<u>10,315,000</u>
Total General Obligation Debt	<u>\$ 14,765,252</u>

Annual debt service requirements to maturity for general obligation debt are as follows:

Year ending June 30,	Governmental Activities		Business-type Activities	
	Principal	Interest	Principal	Interest
2007	\$ 70,495	\$ 26,537	\$ 553,467	\$ 553,526
2008	73,787	23,244	887,189	578,800
2009	77,233	19,799	906,030	548,601
2010	80,839	19,192	919,996	517,208
2011	84,615	12,417	939,089	485,017
Thereafter	181,527	12,794	9,990,985	3,943,926
Total	<u>\$ 568,496</u>	<u>\$ 113,983</u>	<u>\$ 14,196,756</u>	<u>\$ 6,627,078</u>

The legal debt limit mandated by the Commonwealth of Virginia is \$78,458,758.

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

The Town issued \$5,655,523 of 2002 series of general obligation refunding bonds to provide resources to purchase U.S. Governmental State and Local Government Series securities that were placed in an irrevocable trust for the purpose of generating resources for all future debt service payments of \$5,467,202 of general obligation water and sewer bonds. As a result, the refunded bonds are considered to be defeased and the liability has been removed from the business type activities column of the statement of net assets. The reacquisition price exceeded the net carrying amount of the old debt by \$104,200. This amount is being amortized over the remaining life of the refunded debt, which is the same as the life of the new debt issued. This advance refunding was undertaken to reduce total debt service payments over the next 10 years by \$393,867 and resulted in an economic gain of \$358,124.

Long-term liability activity for the year ended June 30, 2006 was as follows:

	June 30, 2005	Additions	Retirements	June 30, 2006	One Year
Governmental activities:					
Bonds payable:					
General obligation bonds	\$ 635,834	\$ -	\$ (67,338)	\$ 568,496	\$ 70,495
Demand note	8,072	-	(8,072)	-	-
Compensated absences	512,369	41,379	-	553,748	-
Governmental activity					
Long-term liabilities	<u>\$ 1,156,275</u>	<u>\$ 41,379</u>	<u>\$ (75,410)</u>	<u>\$ 1,122,244</u>	<u>\$ 70,495</u>
Business-type activities:					
Bonds payable:					
General obligation bonds	\$ 4,656,618	\$ 10,315,000	\$ (774,862)	\$ 14,196,756	\$ 553,467
Unamortized premium	-	259,073	-	259,073	-
Compensated absences	269,197	-	(12,164)	257,033	-
Business-type activity					
Long-term liabilities	<u>\$ 4,925,815</u>	<u>\$ 10,574,073</u>	<u>\$ (787,026)</u>	<u>\$ 14,712,862</u>	<u>\$ 553,467</u>

Compensated absences due within one year disclosed by individual fund is estimated as follows:

Individual Fund	Due Within	
	1 Year	Long-term
General	\$ -	\$ 553,748
Electric	-	35,485
Water	-	98,394
Sewer	-	98,833
Refuse	-	24,321
	<u>\$ -</u>	<u>\$ 257,033</u>

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

V. OTHER INFORMATION

A. Risk Management

The Town is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. To reduce insurance costs and the need for self-insurance, the Town has joined together with other municipalities in the Commonwealth of Virginia in several public entity risk pools (not self-insured) that operate as common risk management and insurance programs for member municipalities. The risk pools include:

VMGSIA: The Town has workers' compensation coverage with the Virginia Municipal Group Self Insurance Association (VMGSIA). During the fiscal year 2006 the Town paid premiums of approximately \$205,193 to VMGSIA.

VMLP: The Town has general and excess liability, automobile, property, boiler and machinery, law enforcement liability, public officials, legal liability, and commercial crime insurance with the Virginia Municipal Liability Pool (VMLP). During the fiscal year 2006, the Town paid contributions of approximately \$265,357 to the VMLP.

Settled claims have not exceeded commercial insurance coverage in any of the past three fiscal years.

B. Surety Bonds

The Town maintains a \$100,000 blanket surety bond on all employees through the Virginia Municipal Liability Pool Insurance Program.

C. Commitments and Contingent Liabilities

Litigation: The Town is a defendant in various lawsuits. Although the outcome of these lawsuits is not presently determinable, in the opinion of the Town, through discussion with its legal counsel, these matters will not have a material adverse effect on the financial condition of the Town.

Contingent Liability: Federal programs in which the Town participates were audited in accordance with the provisions of the Federal Program. Pursuant to the provisions of A-133, all major programs and certain other programs were tested for compliance with applicable grant requirements. While no matters of non-compliance were disclosed by audit, the Federal government may subject grant programs to additional compliance tests which may result in disallowed expenditures. In the opinion of management, any future disallowance of grant program expenditures would not have a material effect on the Town's financial condition.

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

IDA Bond Debt Support Agreement: The Industrial Development Authority (IDA) of Warren County issued \$4,125,000 series 1996 bonds dated November 1, 1996. The IDA issued the bonds to develop a water/sewer project along U.S. Route 340/522. March 1, 2005 the IDA issued Refunding Bonds to provide resources to pay off the 1996 bond issue by placing funds in an irrevocable trust to meet all future debt service and payoff. As a result, the 1996 bond series is considered to be defeased. The advance refunding was undertaken to reduce total debt service payments over the next 12 years by \$270,019 and resulted in an economic gain of \$97,615.

The Town of Front Royal, Virginia and the County of Warren, Virginia have agreed to provide the funds to repay the debt and interest expense obligation and have each executed a support agreement. The County has agreed to provide funding to support 80% of the debt and interest, subject to annual appropriation, and the Town of Front Royal, Virginia has agreed to fund 20% of the debt and interest. The Town's support agreement is backed by the full faith and credit and taxing power of the Town. Details of the IDA bond with the Town's related support obligation are as follows:

Description	Balance
\$3,300,000 2005 Series Industrial Development Authority Revenue Refunding Bond issued March 1, 2005 in increasing annual maturities starting with \$225,000 in 2005 and increasing to \$330,000 in 2016 with interest at 3.59%	<u>\$ 3,075,000</u>
Town of Front Royal support agreement obligation – 20%	<u>\$ 615,000</u>

Year	IDA Debt		20% Support Agreement		
	Principal	Interest	Principal	Interest	Total
2007	\$ 235,000	\$ 106,174	\$ 47,000	21,235	\$ 68,235
2008	240,000	97,648	48,000	19,530	67,530
2009	250,000	88,853	50,000	17,771	67,771
2010	260,000	79,698	52,000	15,940	67,940
2011	270,000	70,185	54,000	14,037	68,037
Thereafter	1,820,000	202,476	364,000	40,495	404,495
	<u>\$ 3,075,000</u>	<u>\$ 645,034</u>	<u>\$ 615,000</u>	<u>\$ 129,008</u>	<u>\$ 744,008</u>

D. Other Post-employment Benefits

In addition to providing pension benefits, the Town Personnel Policies allow the Town to provide certain health care insurance benefits for retired public employees. Substantially all of the Town's public employees may become eligible for those benefits at varying levels dependent on years of service and employment. The cost of retiree health care insurance benefits is recognized as an expenditure as premiums are paid. For 2006 those costs totaled approximately \$25,000 covering approximately 30 employees.

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

E. Defined Benefit Pension Plan

Plan Description

The Town contributes to the Virginia Retirement System (VRS), an agent and cost-sharing multiple-employer defined benefit pension plan administered by the Virginia Retirement System (System). All full-time, salaried permanent employees of participating employers must participate in the VRS. Benefits vest after five years of service. Employees are eligible for an unreduced retirement benefit at age 65 with five years of service (age 60 for participating law enforcement officers and firefighters) and at age 50 with 30 years of service for participating employees (age 50 with 25 years for participating law enforcement officers and firefighters). Employees who retire with a reduced benefit at age 55 (age 50 for participating law enforcement officers and firefighters) with at least five years of credited service are entitled to an annual retirement benefit payable monthly for life in an amount equal to 1.7 percent of their average final salary (AFS) for each year of credited service. Benefits are actuarially reduced for retirees who retire prior to becoming eligible for retirement benefits.

In addition, retirees qualify for annual cost-of-living increases beginning in their second year of retirement. AFS is defined as the highest consecutive 36 months of salary. Participating law enforcement officers and firefighters may receive a monthly benefit supplement if they retire prior to age 65. The VRS also provides death and disability benefits. Title 51.1 of the Code of Virginia (1950), as amended, assigns the authority to establish and amend benefit provisions to the General Assembly of Virginia.

The System issues a publicly available comprehensive annual financial report that includes financial statements and required supplementary information for VRS. A copy of that report may be obtained by writing the System at P. O. Box 2500, Richmond, VA, 23218-2500.

Funding Policy

Plan members are required by Title 51.1 of the *Code of Virginia* (1950), as amended, to contribute 5% of their annual salary to the VRS. The Town assumed this 5% member contribution. In addition, the Town is required to contribute the remaining amounts necessary to fund its participation in the VRS using the actuarial basis specified by the statute and approved by the VRS Board of Trustees. The Town's total contribution rate (employee and employer) for the fiscal year ended 2006 was 13.5% of annual covered payroll.

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

Annual Pension Cost

For 2006, the Town's annual pension cost of \$695,723 was equal to the Town's and employee's required and actual contributions. The required contribution was determined as part of the June 30, 2003 actuarial valuation using the entry age normal actuarial cost method. The actuarial assumptions included (a) 8% investment rate of return, (b) projected salary increases that range between 4.25% and 6.10% per year, and (c) 3.00% per year cost-of-living adjustments. Both (a) and (b) included an inflation component of 4%. The actuarial value of the Town's assets is equal to the modified market value of assets. This method was determined using techniques that smooth the effects of short-term volatility in the market value of assets over a five-year period. The Town's unfunded actuarial accrued liability is being amortized as a level percentage of payroll on an open basis within a period of 30 years or less.

Five-year historical trend information for annual premium costs is as follows:

Fiscal Year Ended	Annual	% APC	Net Pension
2006	\$ 695,723	100	None
2005	677,061	100	None
2004	501,074	100	None
2003	484,692	100	None
2002	559,531	100	None

Required Supplementary Information

Five-year historical trend information about the funding process is presented below as required supplementary information. This information is intended to help users assess the System's funding status on an on-going concern basis, assess progress made in accumulating assets to pay benefits when due, and make comparisons with other public employee retirement systems.

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded Actuarial Accrued Liability (UAAL)		Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage Of Covered Payroll ((b-a)/c)
			Actuarial Accrued Liability (UAAL) (b-a)				
June 30, 2005	\$ 17,855,882	\$ 20,383,018	\$ 2,527,138		87.60%	\$ 4,945,591	51.10%
June 30, 2004	17,485,601	19,325,038	1,839,437		90.48%	4,929,451	37.32%
June 30, 2003	17,324,257	17,999,823	675,566		96.25%	4,810,582	14.04%
June 30, 2002	17,131,301	16,906,356	(224,945)		101.33%	4,487,067	-5.01%
June 30, 2001	16,438,001	15,262,536	(1,175,465)		107.70%	4,232,311	-27.77%

TOWN OF FRONT ROYAL, VIRGINIA

NOTES TO THE FINANCIAL STATEMENTS

F. Deferred Compensation Plan

The Town offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all Town employees at their option, permits participants to defer a portion of their salary until future years. The deferred compensation is not available to participants until termination, retirement, death, or unforeseeable emergency.

The Town implemented GASB Statement No. 32 requiring changes to the accounting and financial reporting for the deferred compensation plans created in accordance with Internal Revenue Code 457. The plans are administered by independent plan administrators through administrative service agreements. The Town's administrative involvement is limited to transmitting amounts withheld from payroll to the plan administrator who performs investing functions. Amendments to the laws governing Section 457 plans substantially became effective January 1, 1997. The Town approved plan amendments such that plan assets are held in trust for the benefit of the plan participants and their beneficiaries. The financial activity of these plans is no longer reported in the Town's Agency Fund.

TOWN OF FRONT ROYAL, VIRGINIA
GENERAL FUND
SCHEDULE OF REVENUES AND OTHER FINANCING SOURCES - BUDGET AND ACTUAL
FOR THE YEAR ENDED JUNE 30, 2006

	Original Budget	Final Budget	Actual	Variance Positive (Negative)
Source of Revenues				
General Property Taxes				
Real estate taxes				
Current taxes, including penalties	\$ 729,240	\$ 729,240	\$ 708,251	\$ (20,989)
Delinquent taxes, including penalties	19,000	19,000	(6,978)	(25,978)
Personal property taxes				
Current taxes, including penalties	283,250	283,250	327,078	43,828
Delinquent taxes, including penalties	-	-	(27,379)	(27,379)
Machinery and tools taxes				
Current taxes, including penalties	-	-	-	-
Mobile home taxes				
Current taxes, including penalties	-	-	-	-
Public service corporation taxes	23,000	23,000	33,911	10,911
Interest on delinquent taxes	17,000	17,000	18,443	1,443
Total General Property Taxes	<u>1,071,490</u>	<u>1,071,490</u>	<u>1,053,326</u>	<u>(18,164)</u>
Other Local Taxes				
Warren County sales tax	534,886	534,886	586,133	51,247
Business and occupational taxes and penalties	668,500	668,500	740,268	71,768
Franchise taxes	190,000	190,000	213,601	23,601
Consumer taxes - electric deregulation	180,300	180,300	191,554	11,254
Vehicle licenses	245,140	245,140	246,458	1,318
Bank stock taxes	150,000	150,000	197,212	47,212
Lodging taxes	296,000	296,000	298,916	2,916
Meal taxes	896,300	896,300	960,333	64,033
Payment in lieu of taxes	75,000	75,000	80,200	5,200
Total Other Local Taxes	<u>3,236,126</u>	<u>3,236,126</u>	<u>3,514,675</u>	<u>278,549</u>
Permits, Fees and Licenses				
Zoning income	23,200	23,200	47,086	23,886
Building maintenance fees	15,750	15,750	(200)	(15,950)
Public ROW use fees	48,000	48,000	30,362	(17,638)
Sign permits	400	400	610	210
Total Permits, Fees and Licenses	<u>87,350</u>	<u>87,350</u>	<u>77,858</u>	<u>(9,492)</u>
Fines and Forfeitures				
Town prosecutions	52,000	52,000	99,820	47,820
Fines and forfeitures - county	63,300	63,300	176,264	112,964
Fines and forfeitures - town	20,000	20,000	31,191	11,191
Total Fines and Forfeitures	<u>135,300</u>	<u>135,300</u>	<u>307,275</u>	<u>171,975</u>
Revenues from Use of Money and Property				
Interest on bank deposits	48,000	48,000	198,986	150,986
Interest on accounts receivable	1,000	1,000	1,083	83
Rental - general property	-	-	600	600
Rental - Adelphia property	8,400	8,400	8,800	400
Total Revenues from Use of Money and Property	<u>\$ 57,400</u>	<u>\$ 57,400</u>	<u>\$ 209,469</u>	<u>\$ 152,069</u>

**TOWN OF FRONT ROYAL, VIRGINIA
GENERAL FUND**

**SCHEDULE OF REVENUES AND OTHER FINANCING SOURCES - BUDGET AND ACTUAL
FOR THE YEAR ENDED JUNE 30, 2006**

	Original Budget	Final Budget	Actual	Variance Positive (Negative)
Charges for Services				
Curb and gutter charges	\$ 45,000	\$ 45,000	\$ 18,142	\$ (26,858)
Street & walk assessment	2,000	2,000	617	(1,383)
Credit card fees	2,000	2,000	(1,000)	(3,000)
Sales at Visitors' Center	56,700	56,700	65,662	8,962
Sales of publications	1,200	1,200	942	(258)
Total Charges for Services	<u>106,900</u>	<u>106,900</u>	<u>84,363</u>	<u>(22,537)</u>
Miscellaneous Revenue				
Miscellaneous	<u>38,000</u>	<u>38,000</u>	<u>115,343</u>	<u>77,343</u>
Recovered Costs				
Warren County Fire Department	<u>50,000</u>	<u>50,000</u>	<u>75,552</u>	<u>25,552</u>
Intergovernmental				
ABC profits	7,960	7,960	7,966	6
Wine tax distribution	8,350	8,350	8,350	-
Rolling stock tax	12,000	12,000	12,482	482
Animal friendly plates	-	-	108	108
Virginia personal property tax reduction	270,000	270,000	280,041	10,041
Rental tax vehicles	40,000	40,000	47,576	7,576
State aid for police and fire	330,000	330,000	415,047	85,047
Highway maintenance	1,500,000	1,500,000	1,032,943	(467,057)
Grants	<u>111,707</u>	<u>117,162</u>	<u>43,416</u>	<u>(73,746)</u>
Total Intergovernmental	<u>2,280,017</u>	<u>2,285,472</u>	<u>1,847,929</u>	<u>(437,543)</u>
Total General Fund Revenues	<u>7,062,583</u>	<u>7,068,038</u>	<u>7,285,790</u>	<u>217,752</u>
Other Financing Sources				
Transfers from other funds	<u>2,298,932</u>	<u>2,298,932</u>	<u>2,141,432</u>	<u>(157,500)</u>
Total Other Financing Sources	<u>2,298,932</u>	<u>2,298,932</u>	<u>2,141,432</u>	<u>(157,500)</u>
Total General Fund Revenues and Other Financing Sources	<u>\$ 9,361,515</u>	<u>\$ 9,366,970</u>	<u>\$ 9,427,222</u>	<u>\$ 60,252</u>

**TOWN OF FRONT ROYAL, VIRGINIA
GENERAL FUND
SCHEDULE OF EXPENDITURES COMPARED WITH APPROPRIATIONS
FOR THE YEAR ENDED JUNE 30, 2006**

	Original Budget	Final Budget	Actual Expenditures	Variance Positive (Negative)
Legislative				
Town Council				
Personal service	\$ 53,433	\$ 53,686	\$ 53,696	\$ (10)
Contractual service	37,000	37,050	21,472	15,578
Materials and supplies	1,000	1,800	1,780	20
Travel and communications	14,700	11,587	8,198	3,389
Total Town Council	106,133	104,123	85,146	18,977
Clerk of Council				
Personal service	56,750	52,100	41,531	10,569
Contractual service	7,250	8,150	6,291	1,859
Materials and supplies	1,500	1,790	1,683	107
Travel and communications	3,450	2,260	488	1,772
Dues and memberships	300	300	240	60
Total Clerk of Council	69,250	64,600	50,233	14,367
Total Legislative	175,383	168,723	135,379	33,344
Executive				
Town Manager				
Personal service	164,222	214,122	213,384	738
Contractual service	4,500	5,424	5,352	72
Materials and supplies	3,500	6,310	5,549	761
Travel and communications	8,300	7,350	6,647	703
Dues and memberships	1,400	876	876	-
Capital outlays	250	-	-	-
Total Town Manager	182,172	234,082	231,808	2,274
Management Services				
Personal service	94,059	94,059	93,890	169
Contractual service	33,840	33,840	24,313	9,527
Materials and supplies	1,900	1,900	1,523	377
Travel and communications	3,000	3,250	2,702	548
Dues and memberships	500	500	305	195
Total Management Services	133,299	133,549	122,733	10,816
Office of the Town Engineer				
Personal service	68,229	68,229	66,130	2,099
Contractual service	5,000	5,000	272	4,728
Materials and supplies	1,750	2,010	953	1,057
Travel and communications	1,400	1,140	616	524
Dues and memberships	500	500	212	288
Capital outlays	17,000	17,000	18,020	(1,020)
Total Office of the Town Engineer	93,879	93,879	86,203	7,676
Auto/Motorpool				
Personal service	247,336	251,036	259,776	(8,740)
Contractual service	(141,300)	(112,940)	(155,814)	42,874
Materials and supplies	220,750	197,500	174,387	23,113
Travel and communications	2,500	1,200	1,019	181
Utilities	2,500	2,500	982	1,518
Dues and memberships	-	140	136	4
Capital outlays	10,000	6,600	6,604	(4)
Total Auto/Motorpool	341,786	346,036	287,090	58,946

SCHEDULE 2
(Continued)

**TOWN OF FRONT ROYAL, VIRGINIA
GENERAL FUND
SCHEDULE OF EXPENDITURES COMPARED WITH APPROPRIATIONS
FOR THE YEAR ENDED JUNE 30, 2006**

	Original Budget	Final Budget	Actual Expenditures	Variance Positive (Negative)
Office of Information Technology				
Personal service	3,768	3,768	3,768	-
Contractual service	109,392	109,392	99,850	9,542
Materials and supplies	3,250	3,250	2,137	1,113
Travel and communications	81,500	80,650	41,141	39,509
Dues and memberships	500	500	-	500
Capital outlays	87,350	146,759	59,989	86,770
Total Office of Information Technology	<u>\$ 285,760</u>	<u>\$ 344,319</u>	<u>\$ 206,885</u>	<u>\$ 137,434</u>
Office of Tourism				
Personal service	\$ 89,842	\$ 92,215	\$ 103,656	\$ (11,441)
Contractual service	93,900	107,900	71,041	36,859
Materials and supplies	44,400	45,900	45,741	159
Utilities	100	100	108	(8)
Travel and communications	14,400	14,900	15,457	(557)
Dues and memberships	2,000	2,000	1,600	400
Contributions to other entities	2,900	2,900	1,511	1,389
Capital outlays	32,750	32,977	7,929	25,048
Total Office of Tourism	<u>280,292</u>	<u>298,892</u>	<u>247,043</u>	<u>51,849</u>
Board of Elections				
Contractual service	6,200	6,200	6,665	(465)
Total Executive	<u>1,323,388</u>	<u>1,456,957</u>	<u>1,188,427</u>	<u>268,530</u>
Legal				
Town Attorney				
Personal service	173,915	175,915	171,582	4,333
Contractual service	42,075	37,975	33,366	4,609
Materials and supplies	6,350	7,750	4,273	3,477
Travel and communications	4,800	5,400	4,273	1,127
Dues and memberships	1,200	1,400	1,365	35
Capital outlays	-	4,356	1,132	3,224
Total Legal	<u>228,340</u>	<u>232,796</u>	<u>215,991</u>	<u>16,805</u>
Finance				
Finance Department				
Personal service	655,797	656,997	574,366	82,631
Contractual service	39,950	46,633	25,696	20,937
Materials and supplies	15,900	18,200	15,067	3,133
Travel and communications	48,375	51,772	41,571	10,201
Dues and memberships	350	350	70	280
Capital outlays	23,000	30,952	16,806	14,146
Total Finance Department	<u>783,372</u>	<u>804,904</u>	<u>673,576</u>	<u>131,328</u>
Total General Government	<u>2,510,483</u>	<u>2,663,380</u>	<u>2,213,373</u>	<u>450,007</u>
Planning, Zoning and Community Development				
Planning and Zoning				
Personal service	235,236	195,386	146,625	48,761
Contractual service	101,350	220,637	69,087	151,550
Materials and supplies	1,800	1,800	1,721	79
Travel and communications	2,750	2,580	396	2,184
Dues and memberships	400	400	389	11
Capital outlays	-	100,170	167	100,003
Total Planning and Zoning	<u>341,536</u>	<u>520,973</u>	<u>218,385</u>	<u>302,588</u>

TOWN OF FRONT ROYAL, VIRGINIA
GENERAL FUND
SCHEDULE OF EXPENDITURES COMPARED WITH APPROPRIATIONS
FOR THE YEAR ENDED JUNE 30, 2006

	Original Budget	Final Budget	Actual Expenditures	Variance Positive (Negative)
Property Maintenance Inspection				
Personal service				-
Contractual service				-
Materials and supplies				-
Travel and communications				-
Total Property Maintenance	-	-	-	-
Boards and Commissions				
Contractual service	13,360	13,360	11,468	1,892
Materials and supplies	250	210	466	(256)
Travel and communications	4,320	4,360	3,672	688
Dues and memberships	200	200	25	175
Joint operations	7,415	7,415	7,415	-
Total Boards and Commissions	25,545	25,545	23,046	2,499
Economic Development				
Contractual service	-	8,377	-	8,377
Contributions to other entities	66,900	66,900	64,855	2,045
Capital outlays	-	-	-	-
Total Economic Development	66,900	75,277	64,855	10,422
Total Planning, Zoning and Community Development	\$ 433,981	\$ 621,795	\$ 306,286	\$ 315,509
Police				
Police Department				
Personal service	\$ 2,637,524	\$ 2,637,524	\$ 2,620,181	\$ 17,343
Contractual service	27,740	29,340	24,530	4,810
Materials and supplies	162,495	153,371	145,043	8,328
Travel and communications	27,650	36,650	32,314	4,336
Dues and memberships	4,750	2,800	1,460	1,340
Joint operations	26,310	28,465	24,077	4,388
Capital outlays	75,000	83,515	78,677	4,838
Total Police Department	2,961,469	2,971,665	2,926,282	45,383
Fire Protection				
Fire Department				
Personal service	-	-	57,259	(57,259)
Materials and supplies	50,000	50,000	30,814	19,186
Total Fire Department	50,000	50,000	88,073	(38,073)
Total Public Safety	3,011,469	3,021,665	3,014,355	7,310
Engineering and Public Works				
Engineering				
Personal service	87,822	93,502	114,053	(20,551)
Contractual service	2,900	7,016	1,067	5,949
Materials and supplies	5,725	2,645	10,712	(8,067)
Travel and communications	3,075	2,675	1,772	903
Dues and memberships	300	35	32	3
Capital outlays	-	647	664	(17)
Total Engineering	99,822	106,520	128,300	(21,780)

SCHEDULE 2
(Continued)

**TOWN OF FRONT ROYAL, VIRGINIA
GENERAL FUND
SCHEDULE OF EXPENDITURES COMPARED WITH APPROPRIATIONS
FOR THE YEAR ENDED JUNE 30, 2006**

	Original Budget	Final Budget	Actual Expenditures	Variance Positive (Negative)
Streets and Sidewalks				
Personal service	837,801	837,801	765,175	72,626
Contractual service	94,700	852,699	502,399	350,300
Materials and supplies	577,150	500,948	388,561	112,387
Travel and communications	2,750	2,750	712	2,038
Utilities	22,500	22,500	22,503	(3)
Dues and memberships	300	300	-	300
Capital outlays	527,500	372,097	251,463	120,634
Total Streets and Sidewalks	2,062,701	2,589,095	1,930,813	658,282
General Properties				
Personal service	39,850	41,850	41,214	636
Contractual service	52,000	114,564	57,068	57,496
Materials and supplies	23,050	29,480	30,457	(977)
Travel and communications	1,850	2,185	1,242	943
Utilities	33,600	40,475	42,839	(2,364)
Capital outlays	-	-	-	-
Total General Properties	150,350	228,554	172,820	55,734
Horticulture				
Personal service	57,178	57,178	51,339	5,839
Contractual service	2,300	2,300	1,943	357
Materials and supplies	15,175	15,175	12,089	3,086
Travel and communications	1,050	1,050	874	176
Capital outlays	10,000	14,922	14,376	546
Total Horticulture	85,703	90,625	80,621	10,004
Total Engineering and Public Works	2,398,576	3,014,794	2,312,554	702,240
Parks and Recreation				
Library	47,596	47,596	47,596	-
Total Parks and Recreation	\$ 47,596	\$ 47,596	\$ 47,596	\$ -
Nondepartmental				
Fringe Benefits	\$ 301,752	\$ 289,500	\$ 245,794	\$ 43,706
Insurance	275,800	275,800	265,357	10,443
Contractual services	100,600	94,648	53,551	41,097
Bad debt	-	-	10,079	(10,079)
Joint operations	10,250	10,250	10,000	250
Reserves	126,008	60,758	-	60,758
Leases	-	-	-	-
Total Nondepartmental	814,410	730,956	584,781	146,175
Subtotal	9,216,515	10,100,186	8,478,945	1,621,241
Transfers to Other Funds				
Transit System Fund	20,000	20,000	-	20,000
Debt Service Fund	125,000	125,000	-	125,000
Total Transfers	145,000	145,000	-	145,000
Total General Fund Encumbrances and Expenditures	\$ 9,361,515	\$ 10,245,186	\$ 8,478,945	\$ 1,766,241

TOWN OF FRONT ROYAL, VIRGINIA
 COMBINING BALANCE SHEET
 NONMAJOR GOVERNMENTAL FUNDS
 JUNE 30, 2006

	Special Revenue				Capital Project		Total Nonmajor Governmental Funds
	Downtown Service District	Asset Forfeitures	Economic Development	Community/ Neighborhood	Total	Town Facilities	
Assets							
Cash and cash equivalents	\$ -	\$ 54,464	\$ 72,882	\$ 1,478,404	\$ 1,605,750	\$ 388	\$ 1,606,138
Accounts receivable - real estate taxes	4,233	-	-	(49,474)	(45,241)	-	(45,241)
Interfund advances	-	-	4,500	-	4,500	-	4,500
Total Assets	4,233	54,464	77,382	1,428,930	1,565,009	388	1,565,397
Liabilities							
Accounts payable	-	-	1,498	(1,548)	(50)	-	(50)
Deferred revenue	4,233	-	-	-	4,233	-	4,233
Interfund advances	-	-	-	97,031	97,031	-	97,031
Cash advances	2,875	-	-	-	2,875	-	2,875
Total Liabilities	7,108	-	1,498	95,483	104,089	-	104,089
Fund Balances							
Unreserved, undesignated	(2,875)	54,464	75,884	1,333,447	1,460,920	388	1,461,308
Total Fund Balances	(2,875)	54,464	75,884	1,333,447	1,460,920	388	1,461,308
Total Liabilities and Fund Balances	\$ 4,233	\$ 54,464	\$ 77,382	\$ 1,428,930	\$ 1,565,009	\$ 388	\$ 1,565,397

**TOWN OF FRONT ROYAL, VIRGINIA
 COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
 NONMAJOR GOVERNMENTAL FUNDS
 FOR THE YEAR ENDED JUNE 30, 2006**

	Special Revenue					Capital Project		Total Nonmajor Governmental Funds
	Downtown Service District	Asset Forfeitures	Economic Development	Community/ Neighborhood	Total	Town Facilities	Total	
Revenues								
Real estate taxes	\$ 19,811	\$ -	\$ 205,989	\$ 70,102	\$ 295,902	\$ -	\$ -	\$ 295,902
Meal taxes	-	-	-	319,661	319,661	-	-	319,661
Asset Forfeitures	-	23,254	-	-	23,254	-	-	23,254
Miscellaneous	-	-	-	3,324	3,324	-	-	3,324
Total revenues	19,811	23,254	205,989	393,087	642,141	-	-	642,141
Expenditures								
Current								
Payment in support of EDA debt issue	-	-	72,379	-	72,379	-	-	72,379
Contributions to other entities	12,379	-	43,832	-	56,211	-	-	56,211
Capital outlays	-	-	-	-	-	7,246	7,246	7,246
Total expenditures	12,379	-	116,211	-	128,590	7,246	7,246	135,836
Excess (deficiency) of revenues over (under) expenditures	7,432	23,254	89,778	393,087	513,551	(7,246)	(7,246)	506,305
Other Financing Sources (Uses)								
Transfers in	-	-	-	-	-	-	-	-
Transfers (out)	-	-	(6,559)	(97,031)	(103,590)	-	-	(103,590)
Total other financing sources (uses)	-	-	(6,559)	(97,031)	(103,590)	-	-	(103,590)
Net change in fund balances	7,432	23,254	83,219	296,056	409,961	(7,246)	(7,246)	402,715
Fund balances - beginning	(10,307)	31,210	(7,335)	1,037,391	1,050,959	7,634	7,634	1,058,593
Fund balances - ending	\$ (2,875)	\$ 54,464	\$ 75,884	\$ 1,333,447	\$ 1,460,920	\$ 388	\$ 388	\$ 1,461,308

**TOWN OF FRONT ROYAL, VIRGINIA
DOWNTOWN SERVICE DISTRICT SPECIAL REVENUE FUND
SCHEDULE OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL
FOR THE YEAR ENDED JUNE 30, 2006**

	Original and Final Budget	Actual Amounts	Variance Positive (Negative)
Revenues			
Real estate taxes	\$ 6,875	\$ 19,811	\$ 12,936
Expenditures			
Contributions to other entities	6,875	12,379	(5,504)
Excess (deficiency) of revenues over (under) expenditures	-	7,432	7,432
Fund balances - beginning	(10,307)	(10,307)	-
Fund balances - ending	<u>\$ (10,307)</u>	<u>\$ (2,875)</u>	<u>\$ 7,432</u>

**TOWN OF FRONT ROYAL, VIRGINIA
 ASSET FORFEITURES SPECIAL REVENUE FUND
 SCHEDULE OF REVENUES, EXPENDITURES,
 AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL
 FOR THE YEAR ENDED JUNE 30, 2006**

	Original and Final Budget	Actual Amounts	Variance Positive (Negative)
Revenues			
Asset forfeitures	\$ 10,000	\$ 23,254	\$ 13,254
Expenditures			
Capital outlays	10,000	-	10,000
Excess (deficiency) of revenues over (under) expenditures	-	23,254	23,254
Fund balances - beginning	31,210	31,210	-
Fund balances - ending	<u>\$ 31,210</u>	<u>\$ 54,464</u>	<u>\$ 23,254</u>

**TOWN OF FRONT ROYAL, VIRGINIA
ECONOMIC DEVELOPMENT SPECIAL REVENUE FUND
SCHEDULE OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL
FOR THE YEAR ENDED JUNE 30, 2006**

	Original and Final Budget	Actual Amounts	Variance Positive (Negative)
Revenues			
Real estate taxes	\$ 121,053	\$ 205,989	\$ 84,936
Expenditures			
Payments in support of EDA debt issue	68,996	72,379	(3,383)
Contributions to other entities	43,832	43,832	-
Total Expenditures	112,828	116,211	(3,383)
Excess (deficiency) of revenues over (under) expenditures	8,225	89,778	81,553
Other Financing Sources (Uses)			
Transfers (out)	(8,225)	(6,559)	1,666
Net change in fund balances	-	83,219	83,219
Fund balances - beginning	(7,335)	(7,335)	-
Fund balances - ending	<u>\$ (7,335)</u>	<u>\$ 75,884</u>	<u>\$ 83,219</u>

**TOWN OF FRONT ROYAL, VIRGINIA
 CAPITAL ASSETS USED IN THE OPERATION OF GOVERNMENTAL FUNDS
 COMPARATIVE SCHEDULES BY SOURCE
 JUNE 30, 2006 AND 2005**

	<u>2006</u>	<u>2005</u>
Governmental funds capital assets		
Land	\$ 1,117,508	\$ 1,117,508
Construction in progress	77,927	77,927
Buildings and improvements	3,345,446	3,345,446
Vehicles	1,392,454	1,289,788
Machinery and equipment	2,662,433	2,570,581
Infrastructure	<u>109,527,139</u>	<u>109,527,139</u>
Total governmental funds capital assets	<u><u>118,122,907</u></u>	<u><u>117,928,389</u></u>
Investments in governmental funds capital assets by source		
General fund	<u>118,122,907</u>	<u>117,928,389</u>
Total governmental funds capital assets	<u><u>\$ 118,122,907</u></u>	<u><u>\$ 117,928,389</u></u>

This schedule presents capital assets without provisions for depreciation.

**TOWN OF FRONT ROYAL, VIRGINIA
CAPITAL ASSETS USED IN THE OPERATION OF GOVERNMENTAL FUNDS
SCHEDULE BY FUNCTION AND ACTIVITY
JUNE 30, 2006**

Function and Activity	Land	Buildings and Improvements	Vehicles	Machinery and Equipment	Infrastructure	Total
General Government						
Executive	\$ 83,155	\$ 738,857	\$ 14,668	\$ 166,781	\$ -	\$ 1,003,461
Finance	-	-	37,101	245,533	-	282,634
Economic development	354,345	16,695	14,705	27,647	-	413,392
General government buildings	276,808	602,545	55,041	64,568	-	998,962
Total general government	714,308	1,358,097	121,515	504,529	-	2,698,449
Public Safety	23,300	439,986	550,030	442,962	-	1,456,278
Public Works and Engineering	379,900	1,625,291	716,166	1,719,684	-	4,441,041
Infrastructure	-	-	-	-	109,527,139	109,527,139
Total governmental funds capital assets	\$ 1,117,508	\$ 3,423,374	\$ 1,387,711	\$ 2,667,175	\$ 109,527,139	\$ 118,122,907

This schedule presents capital assets without provisions for depreciation.

TOWN OF FRONT ROYAL, VIRGINIA
CAPITAL ASSETS USED IN THE OPERATION OF GOVERNMENTAL FUNDS
SCHEDULE OF CHANGES BY FUNCTION AND ACTIVITY
JUNE 30, 2006

Function and Activity	Governmental Funds Capital Assets			Governmental Funds Capital Assets
	July 1, 2005	Additions	Dispositions	June 30, 2006
General Government				
Executive	\$ 940,852	\$ 62,609	\$ -	\$ 1,003,461
Finance	266,438	16,196	-	282,634
Economic development	413,392	-	-	413,392
General government buildings	998,962	-	-	998,962
Total general government	<u>2,619,644</u>	<u>78,805</u>	<u>-</u>	<u>2,698,449</u>
Public Safety	1,390,474	65,804	-	1,456,278
Public Works and Engineering	4,391,132	78,798	28,889	4,441,041
Infrastructure	<u>109,527,139</u>	<u>-</u>	<u>-</u>	<u>109,527,139</u>
Total governmental funds capital assets	<u>\$ 117,928,389</u>	<u>\$ 223,407</u>	<u>\$ 28,889</u>	<u>\$ 118,122,907</u>

**TOWN OF FRONT ROYAL, VIRGINIA
 SCHEDULE OF DIRECTOR OF FINANCE'S ACCOUNTABILITY
 JUNE 30, 2006**

Assets held by the Director of Finance

Cash on hand		\$	1,488
Cash in Banks			
Checking - SunTrust			2,122,042
Certificates of Deposit			
BB&T Bank	\$	350,000	
Greater Atlantic Bank		106,600	
Wachovia Bank		79,547	
Virginia Savings Bank		19,382	
Total Certificates of Deposit			555,529
Virginia Local Government Investment Pool			2,601,348
Repurchase Agreements - Wachovia			110,333
Suntrust Government & Agency Fund			1,438,738
SNAP Pool			10,537,765
Suntrust Investment Account			14,844,704
			<u>14,844,704</u>
Total Assets			<u><u>\$32,211,947</u></u>

At June 30, 2006, Greater Atlantic Bank was not a qualified depository in accordance with the Virginia Security for Public Deposits.

TOWN OF FRONT ROYAL, VIRGINIA
 SCHEDULE OF DIRECTOR OF FINANCE'S ACCOUNTABILITY TO THE TOWN
 FOR THE YEAR ENDED JUNE 30, 2006

	Governmental Funds					2006 Totals (Memorandum Only)	2005 Totals (Memorandum Only)
	General	Debt Service	Special Revenue	Capital Projects	Proprietary Funds		
Balance July 1, 2005	\$ 5,296,328	\$ -	\$ 1,351,338	\$ 11,163	\$ 10,843,061	\$ 17,501,890	\$ 15,376,461
Revised Totals	5,296,328	-	1,351,338	11,163	10,843,061	17,501,890	15,376,461
Receipts (net)							
Interfund advances/receipts	-	-	-	-	278,900	278,900	194,163
General property taxes	1,050,267	-	289,879	-	-	1,340,146	1,371,300
Other local taxes	3,446,239	-	319,661	-	-	3,765,900	3,500,457
Permits, fees and licenses	77,858	-	-	-	-	77,858	93,957
Fines and forfeitures	307,275	-	-	-	-	307,275	219,713
Revenues from use of money and property	209,469	-	-	-	497,182	706,651	274,830
Charges for services	84,363	-	-	-	18,471,406	18,555,769	17,794,112
Capital contributed	-	-	-	-	71,706	71,706	-
Miscellaneous	115,343	-	3,324	-	8,923	127,590	43,562
Recovered costs	75,552	-	23,254	-	-	98,806	84,251
Payment in lieu of taxes	80,200	-	-	-	-	80,200	-
Intergovernmental	2,197,878	-	-	-	-	2,197,878	2,241,813
Debt issuance	-	-	-	-	10,574,073	10,574,073	-
Sale of property	-	-	-	-	-	-	58,417
Total Receipts	7,644,444	-	636,118	-	29,902,190	38,182,752	25,876,575
Total Available	12,940,772	-	1,987,456	11,163	40,745,251	55,684,642	41,253,036
Disbursements (net)							
Warrants (checks) issued	8,564,843	-	127,092	10,775	13,432,445	22,135,155	22,373,457
Retirement of indebtedness	125,000	73,580	-	-	774,862	973,442	1,100,274
Interfund advance payments	-	-	153,899	-	-	153,899	-
Interest on other debt costs	-	30,010	-	-	180,189	210,199	277,415
Total Disbursements	8,689,843	103,590	280,991	10,775	14,387,496	23,472,695	23,751,146
Interfund Transfers							
Transfers in	2,141,432	103,590	-	-	-	2,245,022	2,348,709
Transfers (out)	-	-	(103,590)	-	(2,141,432)	(2,245,022)	(2,348,709)
Total Transfers In (Out)	2,141,432	103,590	(103,590)	-	(2,141,432)	-	-
Balance June 30, 2006	\$ 6,392,361	\$ 76	\$ 1,602,875	\$ 388	\$ 24,216,323	\$ 32,211,947	\$ 17,501,890

**TOWN OF FRONT ROYAL, VIRGINIA
COMPUTATION OF LEGAL DEBT MARGIN
JUNE 30, 2006**

Taxable assessed value of real property	<u>\$ 788,661,561</u>
Debt limit (10 percent of assessed value)	78,458,758
Amount of debt applicable to debt limit:	
Bonded debt	<u>14,765,254</u>
Total amount of debt applicable to debt limitation	<u>(14,765,254)</u>
Legal debt margin	<u>\$ 63,693,504</u>

Note: Section 15.1-176 of 1950 Code of Virginia, as amended, limits to 10% of the assessed valuation of the section real estate subject to taxation as the amount of debt which can be issued by the Town. Debt includes any bonds or other interest bearing obligations including existing indebtedness.

STATISTICAL SECTION

PART III

TOWN OF FRONT ROYAL, VIRGINIA
NET ASSETS BY COMPONENT
Last Four Fiscal Years
(accrual basis of accounting)
(Unaudited)

	Fiscal Year			
	2003	2004	2005	2006
Governmental Activities				
Invested in capital assets, net of related debt	\$ 85,759,208	\$ 80,842,973	\$ 78,199,373	\$ 74,624,593
Restricted	-	-	-	-
Unrestricted	2,280,133	5,304,430	5,450,254	6,691,369
Total Governmental Activities Net Assets	<u>\$ 88,039,341</u>	<u>\$ 86,147,403</u>	<u>\$ 83,649,627</u>	<u>\$ 81,315,962</u>
Business-type Activities				
Invested in capital assets, net of related debt	\$ 85,759,208	\$ 39,613,187	\$ 39,531,599	\$ 19,751,368
Restricted	-	-	-	-
Unrestricted	2,280,133	2,649,403	3,873,842	26,004,470
Total Business-type Activities Net Assets	<u>\$ 88,039,341</u>	<u>\$ 42,262,590</u>	<u>\$ 43,405,441</u>	<u>\$ 45,755,838</u>
Primary Government				
Invested in capital assets, net of related debt	\$ 125,180,698	\$ 120,456,160	\$ 117,730,972	\$ 94,375,961
Restricted	-	-	-	-
Unrestricted	3,936,229	7,953,833	9,324,096	32,695,839
Total Primary Government Net Assets	<u>\$ 129,116,927</u>	<u>\$ 128,409,993</u>	<u>\$ 127,055,068</u>	<u>\$ 127,071,800</u>

Source: Comprehensive Annual Financial Report

TOWN OF FRONT ROYAL, VIRGINIA
CHANGES IN NET ASSETS, LAST FOUR FISCAL YEARS
(accrual basis of accounting)
(Unaudited)

	Fiscal Year			
	2003	2004	2005	2006
Expenses				
Governmental Activities:				
General government and administration	\$ 2,139,086	\$ 2,213,302	\$ 2,493,723	\$ 2,326,711
Public safety	2,951,792	2,857,066	3,150,426	3,276,981
Public works	1,851,599	2,103,729	2,086,799	2,574,487
Planning, zoning, and community development	609,091	501,250	652,296	484,132
Culture and recreation	95,770	43,625	45,142	52,985
Interest on long term debt	41,299	3,788	69,567	28,180
Infrastructure depreciation	3,588,522	3,588,522	3,588,522	3,591,054
Total Governmental Activities Expenses	11,277,159	11,311,282	12,086,475	12,334,530
Business-Type Activities:				
Electric	6,631,457	9,173,662	9,082,609	9,523,363
Water	1,581,502	1,851,233	2,328,499	1,964,023
Sewer	2,228,065	2,061,542	2,636,183	2,285,966
Refuse	685,242	649,323	739,132	828,583
Total Business-Type Activities Expenses	11,126,266	13,735,760	14,786,423	14,601,935
Total Primary Government Expenses	22,403,425	25,047,042	26,872,898	26,936,465
Program Revenues				
Governmental Activities:				
Charges for services:				
General government	7,397	88,891	71,572	131,037
Public safety	251,882	308,337	235,282	406,081
Public works	50,918	46,761	45,371	18,759
Planning, zoning, and community development	73,943	80,864	93,957	77,858
Culture and recreation	50,189	-	-	-
Operating grants and contributions	1,634,435	1,618,991	1,704,613	1,447,990
Capital grants and contributions	-	64,156	80,484	43,416
Total Governmental Activities Program Revenues	2,068,764	2,208,000	2,231,279	2,125,141
Business-Type Activities:				
Charges for services:				
Electric	9,617,905	10,959,143	11,346,761	11,507,238
Water	2,241,254	2,450,850	2,856,329	3,198,691
Sewer	2,153,905	2,330,077	2,674,149	3,011,979
Refuse	730,938	770,344	779,275	806,968
Operating grants and contributions	-	-	-	-
Capital grants and contributions	396,743	316,543	226,919	71,706
Total Business-Type Activities Program Revenues	15,140,745	16,826,957	17,883,433	18,596,582
Total Primary Government Program Revenues	17,209,509	19,034,957	20,114,712	20,721,723

(continued)

TOWN OF FRONT ROYAL, VIRGINIA
CHANGES IN NET ASSETS, LAST FOUR FISCAL YEARS
(accrual basis of accounting)
(Unaudited)

	Fiscal Year			
	2003	2004	2005	2006
Net (Expense) Revenue				
Governmental Activities	\$ (9,208,395)	\$ (9,103,282)	\$ (9,855,196)	\$ (10,209,389)
Business-Type Activities	4,014,479	3,091,197	3,097,010	3,994,647
Total Primary Government Net Expense	<u>(5,193,916)</u>	<u>(6,012,085)</u>	<u>(6,758,186)</u>	<u>(6,214,742)</u>
General Revenues and Other Changes in Net Assets				
Governmental Activities:				
Property taxes	1,029,043	1,258,013	1,213,101	1,280,730
Sales taxes	448,086	507,804	570,926	586,133
Business and occupational taxes	539,916	611,617	624,511	740,268
Franchise taxes	179,371	309,497	211,544	213,601
Consumer taxes	182,303	178,879	178,423	191,554
Alcoholic beverage taxes	31,668	33,569	16,317	16,316
Meals and lodging taxes	1,238,298	1,378,666	1,433,420	1,578,910
Virginia personal property tax reduction	254,979	285,334	262,457	280,041
Other general taxes	495,708	507,664	559,315	583,928
Unrestricted investment earnings	77,910	73,089	101,589	209,469
Gain on sale of capital assets and other recoveries	100,711	46,162	58,417	53,342
Transfers	1,957,860	2,021,050	2,127,400	2,141,432
Total Governmental Activities	<u>6,535,853</u>	<u>7,211,344</u>	<u>7,357,420</u>	<u>7,875,724</u>
Business-Type Activities:				
Unrestricted investment earnings	219,843	114,857	173,241	497,182
Transfers	(1,957,860)	(2,021,050)	(2,127,400)	(2,141,432)
Total Business-Type Activities	<u>(1,738,017)</u>	<u>(1,906,193)</u>	<u>(1,954,159)</u>	<u>(1,644,250)</u>
Total Primary Government	<u>4,797,836</u>	<u>5,305,151</u>	<u>5,403,261</u>	<u>6,231,474</u>
Change in Net Assets				
Governmental Activities	(2,672,542)	(1,891,938)	(2,497,776)	(2,333,665)
Business-Type Activities	2,276,462	1,185,004	1,142,851	2,350,397
Total Primary Government	<u>\$ (396,080)</u>	<u>\$ (706,934)</u>	<u>\$ (1,354,925)</u>	<u>\$ 16,732</u>

(concluded)

Source: Comprehensive Annual Financial Report

TOWN OF FRONT ROYAL, VIRGINIA
FUND BALANCES, GOVERNMENTAL FUNDS
LAST FOUR FISCAL YEARS
(accrual basis of accounting)
(Unaudited)

	Fiscal Year			
	2003	2004	2005	2006
General Fund				
Reserved for other	\$ 2,646,710	\$ 1,552,890	\$ 547,791	\$ 100,975
Unreserved	2,219,482	2,920,690	3,996,494	5,391,587
Total General Fund	<u>\$ 4,866,192</u>	<u>\$ 4,473,580</u>	<u>\$ 4,544,285</u>	<u>\$ 5,492,562</u>
All Other Governmental Funds				
Reserved for:				
Debt service	\$ -	\$ -	\$ -	\$ -
Prepaid items	-	-	-	-
Advances to other funds	-	-	-	-
Unreserved, reported in:				
Special revenue funds	22,792	(22,275)	1,050,959	1,460,920
Capital funds	706,945	974,884	7,634	388
Total all other governmental funds	<u>\$ 729,737</u>	<u>\$ 952,609</u>	<u>\$ 1,058,593</u>	<u>\$ 1,461,308</u>

Source: Comprehensive Annual Financial Report

TOWN OF FRONT ROYAL, VIRGINIA
CHANGES IN FUND BALANCES, GOVERNMENTAL FUNDS
LAST FOUR FISCAL YEARS
(accrual basis of accounting)
(Unaudited)

	Fiscal Year			
	2003	2004	2005	2006
REVENUES:				
Taxes:				
Property	\$ 975,882	\$ 1,301,901	\$ 1,261,184	\$ 1,349,228
Sales	448,086	507,804	570,926	586,133
Business and occupational	539,916	611,617	624,511	740,268
Franchise	179,371	309,497	211,544	213,601
Consumer	182,303	178,879	178,423	191,554
Vehicle licenses	226,033	230,743	236,441	246,458
Bank stock	143,828	143,065	166,904	197,212
Meals and lodging	1,238,298	1,378,666	1,433,420	1,578,910
Permits, fees, and licenses	73,943	80,864	93,957	77,858
Fines and forfeitures	106,882	203,904	219,713	307,275
Revenues from use of money and property	77,910	73,089	101,589	209,469
Charges for services	101,107	111,143	101,343	84,363
Miscellaneous	7,397	16,055	74,017	118,667
Recovered costs	145,000	104,433	15,569	98,806
Payment in lieu of taxes	62,582	66,970	84,251	80,200
Intergovernmental	1,984,347	2,058,357	2,135,390	1,847,929
Total Revenues	<u>6,492,885</u>	<u>7,376,987</u>	<u>7,509,382</u>	<u>7,927,931</u>
EXPENDITURES:				
General government				
Legislative	165,682	188,630	205,523	135,379
Executive	1,010,533	931,212	1,165,197	1,188,427
Legal	187,413	215,643	246,472	215,991
Finance	664,008	779,038	670,026	673,576
Public Safety				
Police	2,553,496	2,807,340	2,937,684	2,926,282
Fire protection	191,125	78,900	100,005	88,073
Planning, zoning, and community development	601,409	471,241	894,911	434,876
Engineering and public works	2,154,147	2,688,013	2,285,996	2,312,554
Parks and recreation	88,131	41,000	41,000	47,596
Nondepartmental	291,714	385,770	621,043	584,781
Debt Service				
Principal	325,927	18,196	144,742	75,410
Interest	41,299	3,788	69,567	28,180
Capital outlay	1,025,638	24,201	77,927	7,246
Total Expenditures	<u>9,300,522</u>	<u>8,632,972</u>	<u>9,460,093</u>	<u>8,718,371</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>(2,807,637)</u>	<u>(1,255,985)</u>	<u>(1,950,711)</u>	<u>(790,440)</u>
OTHER FINANCING SOURCES (USES):				
Transfers in	2,348,562	2,058,450	2,348,709	2,245,022
Transfers (out)	(390,702)	(37,400)	(221,309)	(103,590)
Special revenue	-	8,454	-	-
Interfund borrowing proceeds	1,250,000	-	-	-
Sale of capital assets	100,711	46,162	-	-
Total Other Financing Sources (Uses)	<u>3,308,571</u>	<u>2,075,666</u>	<u>2,127,400</u>	<u>2,141,432</u>
NET CHANGE IN FUND BALANCES	<u>\$ 500,934</u>	<u>\$ 819,681</u>	<u>\$ 176,689</u>	<u>\$ 1,350,992</u>
Debt service as a percentage of noncapital expenditures	<u>4.44%</u>	<u>0.26%</u>	<u>2.28%</u>	<u>1.19%</u>

Source: Comprehensive Annual Financial Report

TOWN OF FRONT ROYAL, VIRGINIA
 ASSESSED VALUE AND ESTIMATED ACTUAL VALUE OF TAXABLE PROPERTY
 LAST TEN FISCAL YEARS
 (Unaudited)

Fiscal Year	Estimated Market Value					Public Utility			Total Taxable Assessed Value			Tax Rates	
	Real Property	Personal Property	Machinery and Tools	Mobile Homes	Real Estate	Real Estate	Personal Property	Real Estate	Real Estate	Real Estate	Personal Property	Real Estate	Personal Property
1997	545,680,800	73,980,786	1,431,480	175,440	13,775,278	314,202	635,357,986	0.16	0.16	0.60	0.16	0.60	
1998	545,854,900	76,226,046	742,810	156,425	13,764,420	280,942	637,025,543	0.16	0.16	0.60	0.16	0.60	
1999	552,343,000	78,468,538	573,395	139,770	13,231,291	221,070	644,977,064	0.14	0.14	0.60	0.14	0.60	
2000	538,807,900	84,523,192	487,990	101,460	13,042,612	101,942	637,065,096	0.13	0.13	0.60	0.13	0.60	
2001	538,299,800	90,970,040	579,930	120,370	13,583,949	137,089	643,691,178	0.13	0.13	0.60	0.13	0.60	
2002	565,683,000	94,753,260	611,990	140,880	11,410,301	117,799	672,717,230	0.13	0.13	0.60	0.13	0.60	
2003	577,812,000	98,300,340	638,350	172,150	14,615,483	58,094	691,596,417	0.13	0.13	0.60	0.13	0.60	
2004	697,130,500	106,727,512	835,030	153,930	16,664,771	-	821,511,743	0.13	0.13	0.60	0.13	0.60	
2005	713,445,100	109,271,685	865,360	159,410	16,664,771	-	840,406,326	0.13	0.13	0.60	0.13	0.60	
2006	719,331,408	103,400,500	916,340	166,370	15,918,461	-	839,733,079	0.13	0.13	0.60	0.13	0.60	

TABLE VII

**TOWN OF FRONT ROYAL, VIRGINIA
PRINCIPAL PROPERTY TAX PAYERS
CURRENT YEAR AND TEN YEARS AGO
(Unaudited)**

Taxpayer	2006		Taxpayer	1997	
	Taxable Assessed Value	Percentage of Total Town Taxable Assessed Value		Taxable Assessed Value	Percentage of Total Town Taxable Assessed Value
Boisseau Family	\$ 15,019,100	1.94%	Rudacille, P W & Bosseau Ltd. Partners	\$ 7,637,300	1.28%
Gateway Plaza	6,271,300	0.81%	Gateway Plaza Shopping Center	5,144,700	0.86%
Shenandoah Square LP	5,722,900	0.74%	Shenandoah Properties	3,447,900	0.58%
Ramsey Inc.	5,287,300	0.68%	Cogil Corporation	3,332,200	0.56%
Corr Family	3,522,900	0.46%	Front Royal Associates	2,850,000	0.48%
Royal Arms Associates	3,340,100	0.43%	James E. Corr	2,843,780	0.48%
Cogil Corp.	3,220,200	0.42%	Royal Hills Limited	2,641,500	0.44%
CCC Enterprises	3,029,900	0.39%	CCC Enterprise Inc. of Virginia	2,524,820	0.42%
Richmond Homes	2,731,000	0.35%	Heritage Hall	2,149,500	0.36%
Shenandoah Properties II	2,142,900	0.28%	Rappawan, Inc.	1,816,470	0.31%
Total	<u>\$ 50,287,600</u>	<u>6.51%</u>		<u>\$ 34,388,170</u>	<u>5.77%</u>

**TOWN OF FRONT ROYAL, VIRGINIA
PROPERTY TAX LEVIES AND COLLECTIONS
LAST TEN FISCAL YEARS
(Unaudited)**

Fiscal Year	Total Tax Levy	Current Tax Collections	Percent of Levy Collected	Delinquent Tax Collections	Total Tax Collections	Total Collection as Percent of Current Levy
1997	\$ 1,312,029	\$ 1,009,583	76.95%	\$ 177,611	\$ 1,187,194	90.49%
1998	1,308,411	1,109,869	84.83%	78,893	1,188,762	90.86%
1999	1,211,775	926,982	76.50%	174,871	1,101,853	90.93%
2000	1,166,611	950,972	81.52%	228,947	1,179,919	101.14%
2001	1,237,319	1,127,655	91.14%	129,307	1,256,962	101.59%
2002	1,265,639	1,175,097	92.85%	115,463	1,290,560	101.97%
2003	1,298,124	1,064,604	82.01%	87,878	1,152,482	88.78%
2004	1,537,321	1,514,244	98.50%	74,239	1,588,483	103.33%
2005	1,523,668	1,493,940	98.05%	40,065	1,534,005	100.68%
2006	1,597,087	1,599,025	100.12%	55,002	1,654,027	103.57%

Note: Penalties and interest are not included in any of the values.

TOWN OF FRONT ROYAL, VIRGINIA
RATIO OF OUTSTANDING DEBT BY TYPE
LAST TEN FISCAL YEARS
(Unaudited)

Fiscal Year	Governmental Activities	Business Type Activities	Total Primary Government	Personal Income (thousands of dollars)	Percentage of Personal Income	Population	Per Capita
	General Obligation Bonds	General Obligation Refunding Bonds					
1997	10,655,545	10,655,545	21,311,090	271,241	DNA	12,750	1,671
1998	12,405,661	11,135,661	23,541,322	299,676	DNA	13,000	1,811
1999	11,285,699	10,123,906	21,409,605	343,884	DNA	13,464	1,590
2000	9,999,807	8,938,816	18,938,623	355,563	DNA	13,500	1,403
2001	8,694,656	7,739,304	16,433,960	343,277	DNA	13,529	1,215
2002	7,784,635	6,901,864	14,686,499	364,469	DNA	13,560	1,083
2003	6,977,236	6,170,392	13,147,628	DNA	DNA	13,584	968
2004	6,206,636	5,417,988	11,624,624	472,533	DNA	13,584	856
2005	5,300,524	4,656,618	9,957,142	472,707	DNA	14,184	702
2006	10,883,496	3,881,756	14,765,252	DNA	DNA	13,720	1,076

TABLE X

**TOWN OF FRONT ROYAL, VIRGINIA
RATIOS OF GENERAL BONDED DEBT OUTSTANDING
LAST TEN FISCAL YEARS**

Fiscal Year	General Obligation Bonds	Debt Payable from Enterprise Revenues	Net Bonded Debt	Assessed Value in \$1,000	Percentage of Actual Taxable Value of Property	Population	Per Capita
1997	10,655,545	10,655,545	-	635,358	0.00%	12,750	-
1998	12,405,661	11,135,661	1,270,000	637,026	0.20%	13,000	97.69
1999	11,285,699	10,123,906	1,161,793	644,977	0.18%	13,464	86.29
2000	9,999,807	8,938,816	1,060,991	637,065	0.17%	13,500	78.59
2001	8,694,656	7,739,304	955,352	643,691	0.15%	13,529	70.62
2002	7,784,635	6,901,864	882,771	672,717	0.13%	13,560	65.10
2003	6,977,236	6,170,392	806,844	691,596	0.12%	13,584	59.40
2004	6,206,636	5,417,988	788,648	821,512	0.10%	13,584	58.06
2005	5,300,524	4,656,618	643,906	840,406	0.08%	13,589	47.38
2006	14,765,252	14,196,756	568,496	839,733	0.07%	13,720	41.44

TOWN OF FRONT ROYAL, VIRGINIA
DIRECT AND OVERLAPPING GOVERNMENTAL ACTIVITIES DEBT
AS OF SEPTEMBER 30, 2006
(Unaudited)

<u>Governmental Unit</u>	<u>Debt Outstanding</u>	<u>Estimated Percentage Applicable</u>	<u>Estimated Share of Overlapping Debt</u>
Debt repaid with property taxes			
Warren County	4,325,000		
Warren County School Board	12,197,682		
Subtotal, overlapping debt	<u>16,522,682</u>	49%	8,096,114
Town of Front Royal (direct debt)	<u>14,765,252</u>	100%	<u>14,765,252</u>
Total direct and overlapping debt			<u><u>22,861,366</u></u>

**TOWN OF FRONT ROYAL, VIRGINIA
 PLEDGED-REVENUE COVERAGE
 LAST TEN FISCAL YEARS
 (Unaudited)**

Fiscal Year	Gross Revenue ¹	Operating Expenses ²	Net Revenue Available for Debt Service	Debt Service Requirements			
				Principal	Interest ³	Total	Coverage
1997	12,659,121	8,855,476	3,803,645	556,840	600,482	1,157,322	3.29
1998	13,250,730	7,690,336	5,560,394	659,884	568,543	1,228,427	4.53
1999	13,190,876	8,585,568	4,605,308	1,011,775	553,927	1,565,702	2.94
2000	14,021,657	8,927,744	5,093,913	1,185,090	473,094	1,658,184	3.07
2001	14,658,305	8,047,406	6,610,899	1,199,512	469,356	1,668,868	3.96
2002	14,556,457	9,487,331	5,069,126	837,440	369,078	1,206,518	4.20
2003	14,963,845	9,434,131	5,529,714	919,792	261,538	1,181,330	4.68
2004	16,625,271	12,054,058	4,571,213	752,404	228,919	981,323	4.66
2005	17,829,755	13,119,294	4,710,461	761,370	202,048	963,418	4.89
2006	19,022,058	12,918,187	6,103,871	553,467	553,526	1,106,993	5.51

¹Gross revenue includes operating revenues and investment earnings

²Total operating expenses exclusive of depreciation

³Interest includes fiscal charges

**TOWN OF FRONT ROYAL, VIRGINIA
 DEMOGRAPHIC AND ECONOMIC STATISTICS
 LAST TEN CALENDAR YEARS
 (Unaudited)**

Year	Estimated Population	Personal Income (thousands of dollars)	Per Capita Personal Income	Median Age	School Enrollment	Unemployment Rate
1997	12,750	271,741	21,313	*	4,858	5.4%
1998	13,000	299,676	23,052	*	4,903	2.4%
1999	13,464	343,884	25,541	*	4,906	2.4%
2000	13,500	355,563	26,338	37	5,012	2.0%
2001	12,589	343,277	27,268	*	5,277	2.8%
2002	13,650	364,469	26,701	*	5,153	3.4%
2003	13,584	DNA	DNA	*	5,112	3.4%
2004	13,584	472,533	34,786	*	5,176	3.4%
2005	13,589	472,707	34,786	*	5,376	3.1%
2006	13,720	DNA	DNA	*	5,173	2.5%

*Median age only available in census years

TOWN OF FRONT ROYAL, VIRGINIA
PRINCIPAL EMPLOYERS
CURRENT YEAR
(Unaudited)

2006

<u>Employer</u>	<u>Employees</u>
Warren County	400
DuPont	400
Family Dollar Stores	325
Town of Front Royal	150
Valley Redi-Mix	80
Toray Plastics, Inc.	75
Tartan Textiles	75
Precision Systems	75
Walden Foods	60
AirPac	50
Ferguson Enterprises	40
CorrecTech	35
GeoDigital Mapping	20
Blue Ridge Prestain	20

TOWN OF FRONT ROYAL, VIRGINIA
FULL-TIME EQUIVALENT TOWN GOVERNMENT EMPLOYEES BY FUNCTION/PROGRAM
LAST FOUR FISCAL YEARS
(Unaudited)

<u>Function/Program</u>	<u>Fiscal Year</u>			
	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
General Government and Administration	153	135	135	135
Fire Protection	5	5	5	5
Police Protection	35	35	35	35

TOWN OF FRONT ROYAL, VIRGINIA
OPERATING INDICATORS BY FUNCTION/PROGRAM
LAST FOUR FISCAL YEARS
(Unaudited)

<u>Function/Program</u>	<u>Fiscal Year</u>			
	<u>2003</u>	<u>2004</u>	<u>2005</u>	<u>2006</u>
Public Safety				
Police				
Number of Employees	35	35	35	35
Number of Stations	1	1	2	2
Fire				
Number of Employees	5	5	5	5
Number of Stations	1	1	1	1
Sewage System				
Number of service connections	4,100	5,180	5,300	5,390
Daily average treatment in gallons	2,100,000	3,490,755	3,523,000	3,523,000
Maximum daily capacity of treatment plant in gallons	4,000,000	4,000,000	4,000,000	4,000,000
Water System				
Number of service connections	4,500	5,500	5,300	5,700
Daily average consumption in gallons	1,750,000	1,678,000	1,708,000	1,708,000
Maximum daily capacity of plant in gallons	2,500,000	2,500,000	2,500,000	2,500,000
Electric Distribution				
Number of distribution stations	3	3	3	3

TOWN OF FRONT ROYAL, VIRGINIA
OPERATING INDICATORS BY FUNCTION/PROGRAM
LAST FOUR FISCAL YEARS
(Unaudited)

Function/Program	Fiscal Year			
	2003	2004	2005	2006
Public Safety				
Police Stations	1	1	2	2
Police Patrol Units	6	6	6	6
Fire Stations	1	1	1	1
Town Facilities and Services				
Miles of streets	143	143	143	143
Number of streetlights	1,430	1,430	1,430	1,430
Community centers	1	1	1	1
Parks	13	13	13	13
Park acreage	165	165	165	165
Swimming pools	1	1	1	1
Tennis courts	9	9	9	9
Sewage System				
Miles of sanitary sewers	117	117	117	117
Miles of storm sewers	27	27	27	27
Number of treatment plants	1	1	1	1
Water System				
Number of facilities	1	1	1	1
Electric Distribution System				
Miles of service	140	140	140	140

COMPLIANCE SECTION

PART IV

MITCHELL & Co., P.C.

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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENTAL AUDITING STANDARDS*

To The Honorable Mayor and Members of Town Council
Town of Front Royal, Virginia

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Town of Front Royal, Virginia, as of and for the year ended June 30, 2006, which collectively comprise the Town of Front Royal, Virginia's basic financial statements and have issued our report thereon dated October 27, 2006. 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, and *Specifications for Audits of Counties, Cities and Towns* issued by the Auditor of Public Accounts of the Commonwealth of Virginia.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Town of Front Royal, Virginia'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 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 Town of Front Royal, Virginia's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants 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* and *Specifications for Audits of Counties, Cities and Towns*.

This report is intended for the information of Town Council, management, others within the Town of Front Royal, Virginia and appropriate state regulatory agencies. However, this report is a matter of public record and its distribution is not limited.

October 27, 2006
Leesburg, Virginia

Mitchell & Company, P.C.

TOWN OF FRONT ROYAL, VIRGINIA

**AUDITOR'S COMMENTS
FOR THE YEAR ENDED JUNE 30, 2006**

SUMMARY OF AUDITOR'S RESULTS

We have audited the financial statements of the Town of Front Royal, Virginia as of and for the year ended June 30, 2006, and have issued an unqualified opinion thereon dated October 27, 2006. 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 and *Specifications for Audits of Counties, Cities and Towns*, issued by the Auditor of Public Accounts of the Commonwealth of Virginia.

Our audit did not disclose any noncompliance which is considered material to the financial statements of the Town of Front Royal, Virginia nor did not disclose any material weaknesses in internal controls.

Findings and Questioned Costs

There are no current year questioned costs or prior year findings requiring follow-up.

SUMMARY OF COMPLIANCE MATTERS

We performed tests of the Town's compliance with certain provisions of the laws, regulations, contracts, and grants shown below.

State Compliance Matters

- Code of Virginia
- Budget and Appropriation Laws
- Cash and Investments Laws
- Conflicts of Interest Act
- Local Retirement Systems
- Debt Provisions
- Procurement Laws
- Uniform Disposition of Unclaimed Property Act
- State Agency Requirements
- Highway Maintenance Funds

Federal Compliance Matters

- Internal Revenue Service
- EEOC

Other Compliance Matters

- Bond Covenants/Support Agreement