

MANAGEMENT'S DISCUSSION AND ANALYSIS

As management of the County of Beaver (the "County"), we offer readers of the County's financial statements this narrative overview and analysis of the financial activities of the County for the fiscal year ended December 31, 2003. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our letter of transmittal.

Financial Highlights

- The County's real property tax was maintained at 15.7 mills for a second consecutive year.
- Financial information for the Community College of Beaver County is presented along with the County's financial statements for the first time (Note A). The County helped fund the operations of the College by providing \$2.1 million during the year.
- The County owned nursing facility, Friendship Ridge, incurred a \$4 million loss during the year.
- In the face of continuing economic difficulties, tax revenues increased by approximately \$1.7 million.
- The County maintained an investment grade bond rating of AAA insured from Standard & Poor.
- Operating grants and contributions for governmental activities increased approximately \$7.2 million.
- Investment income for governmental and business-type activities decreased approximately \$0.55 million from the prior year and \$2.55 million from two years ago.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the County's basic financial statements. The County's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains 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 County's finances, in a manner similar to a private-sector business.

The *statement of net assets* provides information showing the status of the County's financial position at year-end. It reports the availability of assets for future use and is

an important management tool in financial planning. The statement distinguishes those assets used exclusively with regards to government operation versus those assets committed to the business operation of government.

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, such as uncollected taxes, earned but unused vacation leave, accrued interest on long-term debt, accrued payroll, and intergovernmental receivables.

Both of the government-wide financial statements distinguish functions of the County that are principally supported by taxes and intergovernmental revenues (*governmental activities*) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*). The governmental activities of the County are general government, judicial, public safety, public works and enterprise, culture, recreation, conservation, and human services. The business-type activities of the County are Friendship Ridge, Emergency Services, and Health Choices.

The government-wide financial statements include not only the County itself (known as the *primary government*), but also two legally separate entities, the Beaver County Transit Authority and the Community College of Beaver County, for which the County provides subsidies and appoints their boards. Financial information for these *component units* are reported separately from the financial information presented for the primary government itself.

The government-wide financial statements can be found on pages 33-36 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 County, 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 County can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

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

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions.

Immediately following both the governmental funds' balance sheet and the governmental funds' statement of revenues, expenditures, and changes in fund balances, a statement is presented that provides a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*.

The County maintains sixteen individual governmental funds. Information is presented separately in the governmental funds' balance sheet and in the governmental funds' statement of revenues, expenditures, and changes in fund balance for the General Fund, Mental Health / Mental Retardation, Children & Youth, and the 1996 Bond Issue, all of which are considered to be major funds. Data from the other twelve 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 schedules elsewhere in this report. The County adopts an annual appropriated budget for its governmental funds.

The basic governmental funds financial statements can be found on pages 37-42 of this report.

Proprietary funds. The County maintains two different types of proprietary funds. *Enterprise funds* are used to report the same functions presented as *business-type activities* in the government-wide financial statements. The County uses enterprise funds to account for Friendship Ridge, Emergency Services, and Health Choices. *Internal service funds* are an accounting device used to accumulate and allocate costs internally among the County's various functions.

The County uses an internal service fund to account for the medical benefits of the County's employees. Because this service predominantly benefits governmental rather than business-type functions, they have been included within governmental activities in the government-wide financial statements.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The proprietary funds' financial statements provide separate information for Friendship Ridge and for Health Choices, both of which are considered to be major funds of the County, and for Emergency Services, which is a non-major fund. The proprietary funds' financial statements also provide separate information for the County's internal service fund.

The basic proprietary funds' financial statements can be found on pages 43-48 of this report.

Fiduciary funds. Fiduciary funds are used to account for resources held for the benefits of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the County's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds.

The basic fiduciary fund financial statements can be found on pages 49-50 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 51-98 of this report.

Other information. In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information concerning the County's progress in funding its obligation to provide pension benefits to its employees and budgetary comparison statements for the general fund and major special revenue funds which have been provided to demonstrate compliance with the budget.

Required supplementary information can be found on pages 99-103 of this report.

The combining schedules referred to earlier in connection with non-major governmental funds are presented immediately following the required supplementary information.

Combining and individual fund schedules can be found on pages 104-147 of this report.

Government-wide Financial Analysis

This analysis focuses on the Primary Government (see above). Separate financial statements for the County's component units, including their management's discussion and analysis, can be obtained from the component units at the addresses disclosed in Note A.

Analysis of Net Assets

Net assets are a useful indicator of a government's financial position. For the County, total assets exceeded liabilities by \$23,902,685 and \$38,860,639 at December 31, 2003 and 2002, respectively.

County of Beaver's Statement of Net Assets
(in thousands)

The following is a summary of the County's Statement of Net Assets as of December 31, 2003 and 2002:

	<u>2003</u>	<u>2002</u>	<u>2003</u>	<u>2002</u>	<u>2003</u>	<u>2002</u>
<i>Assets:</i>						
Current and Other Assets	\$ 24,375	\$ 34,270	\$ 20,174	\$ 28,013	\$44,549	\$ 62,283
Capital Assets	<u>76,077</u>	<u>76,770</u>	<u>13,498</u>	<u>13,436</u>	<u>89,575</u>	<u>90,206</u>
	100,452	111,040	33,672	41,449	134,124	152,489
<i>Liabilities:</i>						
Long-Term Liabilities Outstanding	85,056	86,813	6,019	5,162	91,075	91,975
Other Liabilities	<u>13,394</u>	<u>16,523</u>	<u>5,752</u>	<u>5,130</u>	<u>19,146</u>	<u>21,653</u>
	98,450	103,336	11,771	10,292	110,221	113,628
<i>Net Assets:</i>						
Invested in Capital Assets, net of related debt	1,138	3,204	8,882	8,274	10,020	11,478
Restricted		-	7,128	11,902	7,128	11,902
Unrestricted	<u>864</u>	<u>4,500</u>	<u>5,891</u>	<u>10,981</u>	<u>6,755</u>	<u>15,481</u>
	<u>\$ 2,002</u>	<u>\$ 7,704</u>	<u>\$ 21,901</u>	<u>\$ 31,157</u>	<u>\$ 23,903</u>	<u>\$ 38,861</u>

A significant portion of net assets are largely restricted for specific legal purposes in the HealthChoices program

Changes in Net Assets

The County's net assets decreased by \$14,957,954 and \$9,977,755 for the years ended December 31, 2003 and 2002, respectively. The mix of County revenues remained essentially unchanged from 2002. Approximately 41% of the County's revenue came from grants and contributions, 38% for services provided, and 20% from taxes on real property. The corresponding figures for 2002 were 40%, 39%, and 20% respectively. The County's expenses cover a wide range of services. The largest share of expenses continues to be incurred for human services, HealthChoices and Friendship Ridge.

The following summarizes the County's Statement of Activities for the years ended December 31, 2003 and 2002.

**County of Beaver's Statement of Activities
(in thousands)**

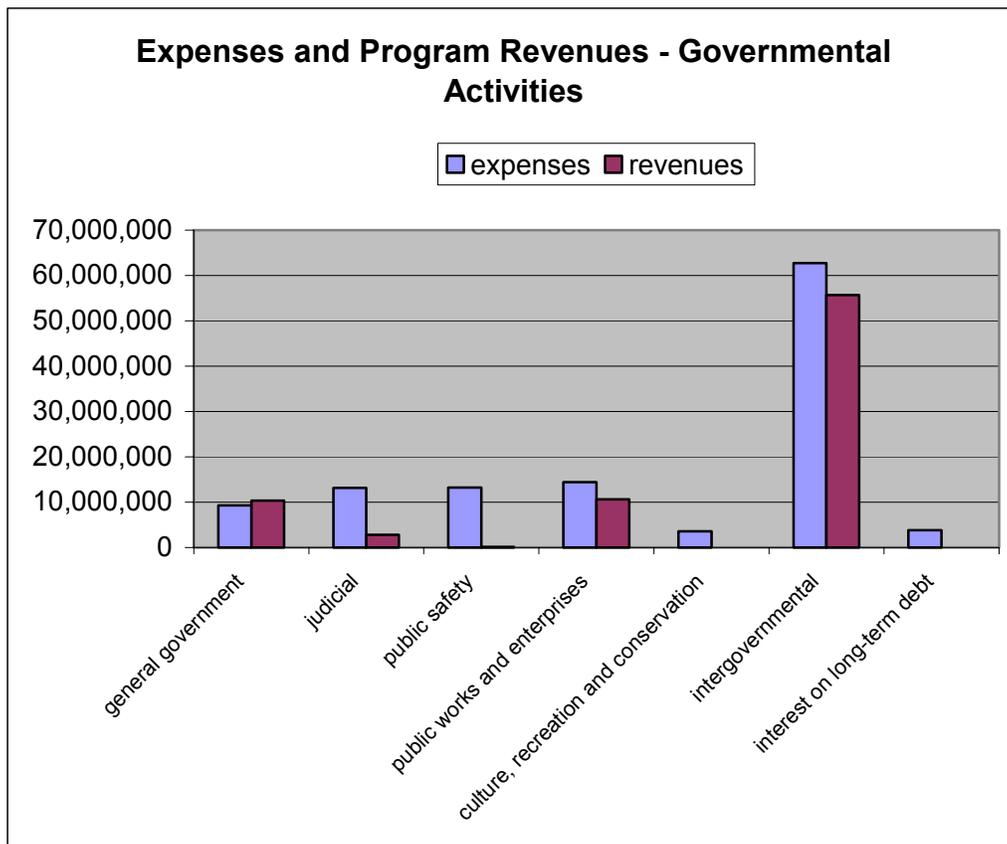
	Governmental Activities		Business-type Activities		Totals	
	<u>2003</u>	<u>2002</u>	<u>2003</u>	<u>2002</u>	<u>2003</u>	<u>2002</u>
<i>Program Revenues:</i>						
Fees and Charges	\$ 10,460	\$ 9,940	\$ 53,300	\$ 51,766	\$ 63,760	\$ 61,706
Operating Grants and Contributions	70,376	63,124	-	-	70,376	63,124
<i>General Revenues:</i>			-			
Real Estate Taxes	32,829	31,173	-	-	32,829	31,173
Investment Income	987	1,344	146	340	1,133	1,684
Unrestricted Gifts	-	-	5	13	5	13
	114,652	105,581	53,451	52,119	168,103	157,700
<i>Program Expenses:</i>						
General Government	9,268	10,109	-	-	9,268	10,109
Judicial	13,136	12,259	-	-	13,136	12,259
Public Safety	13,236	11,841	-	-	13,236	11,841
Public Works and Enterprises	14,429	14,272	-	-	14,429	14,272
Culture, Recreation and Conservation	3,536	3,349	-	-	3,536	3,349
Human Services	61,905	56,843	-	-	61,905	56,843
Miscellaneous	795	593	-	-	795	593
Interest Expense	3,845	3,922	-	-	3,845	3,922
Friendship Ridge	-	-	45,551	41,826	45,551	41,826
Emergency Services	-	-	1,669	1,932	1,669	1,932
Health Choices	-	-	15,595	11,432	15,595	11,432
Total Expenses	120,150	113,188	62,815	55,190	182,965	168,378
Deficiency Before Other Items and Transfers	(5,498)	(7,607)	(9,364)	(3,071)	(14,862)	(10,678)
Gain (Loss) on Disposals	(96)	700	-	-	(96)	700
Transfers Out	(108)	(122)	-	-	(108)	(122)
Transfers In	-	-	108	122	108	122
Change in Net Assets	(5,702)	(7,029)	(9,256)	(2,949)	(14,958)	(9,978)
Net Assets – Beginning	7,704	14,733	31,157	34,106	38,861	48,839
Net Assets – Ending	\$ 2,002	\$ 7,704	\$ 21,901	\$ 31,157	\$ 23,903	\$ 38,861

Analysis of Changes in Net Assets

The County's net assets decreased by \$14,957,954 and \$9,977,755 for the years ended December 31, 2003 and 2002, respectively. This decrease is explained in the governmental and business-type activities discussion below.

Governmental Activities

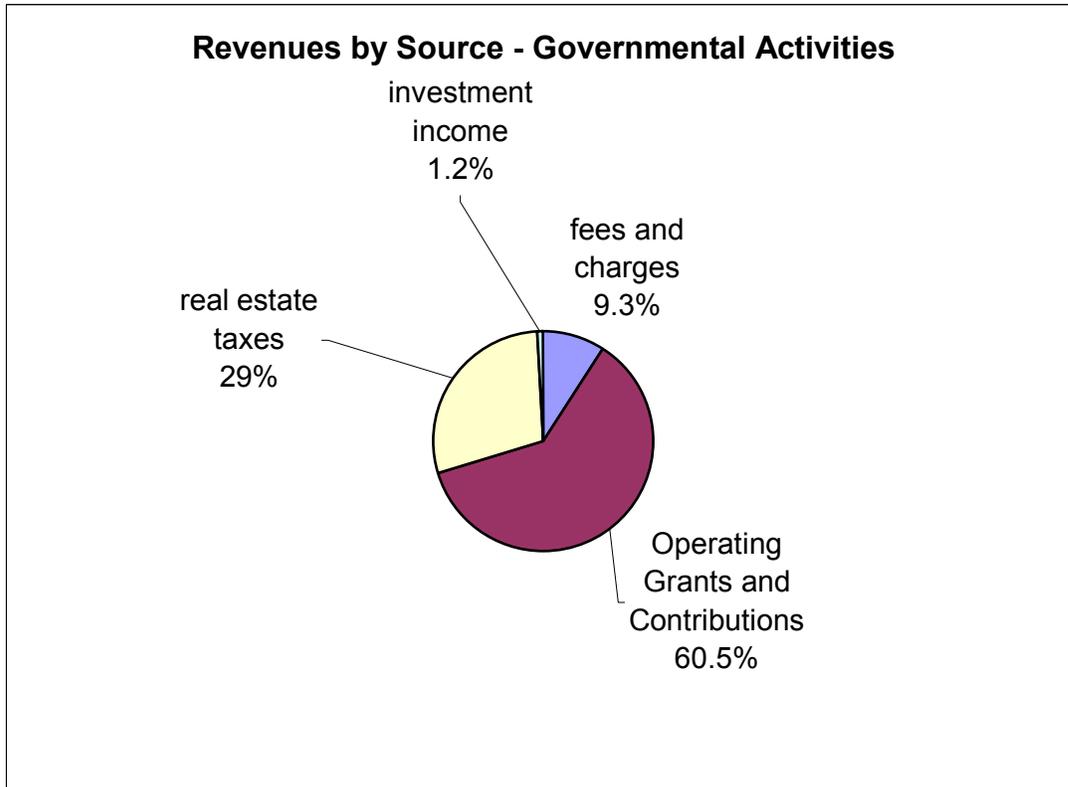
Governmental Activities decreased the County's net assets by \$5,701,847. Key elements of the decrease are a result of lower investment income and higher expenses for providing public safety and human services.



Increased salaries and responsibilities lead to an increase in the expenses net of revenues for the public safety function. Expenditures increased by \$1.39 million while revenues declined slightly.

In the human services function, increases in revenue of \$5.44 million were not enough to cover the increases in expense of \$5.06 million due to increased demand for services.

Due to declining interest rates, investment income fell approximately \$0.4 million during 2003.



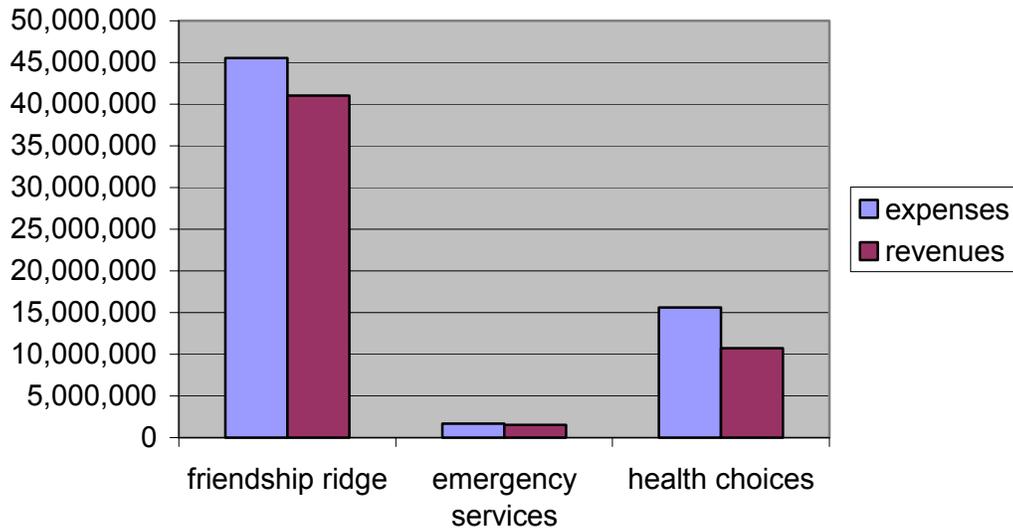
Business-type Activities

Business-type activities decreased the County’s net assets by \$9,256,107 for the year ended December 31, 2003. The two major enterprise funds, HealthChoices and Friendship Ridge, each experienced decreases in net assets of over \$4.3 million.

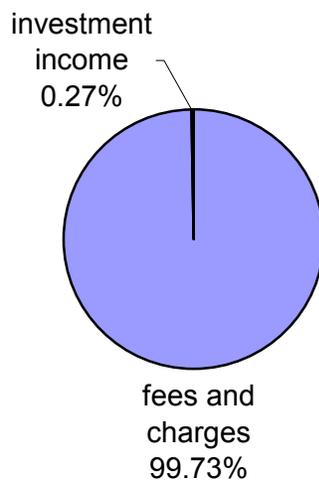
The decrease in net assets for the HealthChoices program is due to an increase in demand for the services of this program without a corresponding increase in revenues and the expenditure of funds within approved reinvestment plans. The Commonwealth of Pennsylvania provides revenue for this program based on fixed rates which are dependent on the number of County residents enrolled in the program. Enrollment was largely unchanged during 2003.

Friendship Ridge incurred a loss for the second year in a row due primarily to continued pressure by the Federal Government to cut back on Medicare/Medicaid costs despite the increasing costs of providing medical services.

Expenses and Program Revenues - Business-type Activities



Revenues by Source - Business-type Activities



Financial Analysis of the County's Individual Funds

Governmental Funds

The focus of the County's Governmental Funds is to provide information on near-term inflows, outflows and balances of expendable resources. Such information is useful in assessing the County'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 year.

At December 31, 2003, the County's Governmental Funds reported a combined ending fund balance of \$12,437,433, a decrease of \$5,440,823 in comparison to the previous year. \$11,735,229 of this total amount or 94% represents unreserved fund balance, which is available for spending at the County's discretion in the coming year.

The General Fund is the main operating fund for the County. Its fund balance decreased by approximately \$1 million during 2003 and \$1.5 million during 2002. This improvement was due to an increase in revenues of \$3.11 million and continuing efforts to control expenditures. The General Fund is discussed in more detail in the General Fund budgetary highlights section (see below).

The Mental Health / Mental Retardation fund decreased by approximately \$.35 million during 2003 and \$0.86 million during 2002. Intergovernmental revenues were less than budgeted amounts and it failed to keep pace with service costs. The County anticipates that the fund's current decrease will be recaptured during the coming year once the County is able to recognize revenues currently deferred.

The Children & Youth fund increased by \$0.5 million during 2003 as compared to a decrease of \$0.76 million during the prior year. This increase was primarily due to timing differences in intergovernmental revenues. The Children & Youth fund had a fund balance of \$0.81 million at December 31, 2003.

During 2003, the County continued to spend down the balance of the 1996 Bond Issue fund. The fund decreased by \$4.76 million during 2003 as compared to \$4.87 million during the prior year. The County had \$3.73 million in unreserved fund balance to spend on capital projects as of December 31, 2003.

The County's numerous nonmajor funds experienced a decrease in fund balance of \$0.46 million and \$0.69 million during 2003 and 2002, respectively. The main source of this decrease during the current year was the continued spending of the balances in the nonmajor capital project funds.

Proprietary Funds

The County's Proprietary Funds provide the same type of information found in the government-wide financial statements, but in more detail. Please refer to the analysis of the changes in net assets for business-type activities for a discussion of Friendship Ridge and the Health Choices program.

Fiduciary Funds

The County maintains Fiduciary Funds for the Pension Trust Fund and several agency funds. Net assets of the Pension Trust Fund increased by \$23,791,435 as compared to a decrease of \$7,265,002 during 2002. The increase during the current year was due in large part to increases in the fair value of investments and the County's contribution pursuant to its fiduciary responsibilities.

General Fund Budgetary Highlights

During any given year there are many factors that may change a budget from the *original* approved version to the *final* ending version. There may be changes in policies, revenue sources or unexpected events that have a financial impact upon the county and require that the budget be adjusted to reflect those circumstances.

The General Fund's budgeted revenues were increased by \$0.96 million from the original budget primarily due to an increase in intergovernmental revenues. These changes in intergovernmental revenues were due to grant awards that were received but not anticipated at the time the original budget was approved.

The General Fund's budgeted expenses were increased by \$3.15 million from the original budget during the year. The main explanation for this increase was the increase in health costs. As explained more fully in Note L, the County pays most medical expenses for its employees directly. As medical costs rise, the County must increase the budget to reflect the increased cost of this employee benefit. The following table summarizes the difference in Salaries and Benefits by function between the original and final budget.

<i>Function</i>	<i>Original Budget</i>	<i>Final Budget</i>	<i>Difference</i>
General Government	\$ 6,626,175	\$ 7,015,955	\$ 389,780
Judicial	8,004,201	8,577,344	573,143
Public Safety	11,576,418	12,449,847	873,429
Public Works	2,448,612	2,620,045	171,433
Culture, Recreation and Conservation	1,633,013	1,796,184	163,171
Human Services	-	-	-
TOTAL	\$ 30,288,419	\$ 32,459,375	\$ 2,170,956

While the Human Services function has no expenditures for salaries, the original budget for this function was increased by \$0.8 million due to additional amounts due for the required County match of certain Federal and State grants and additional amounts paid to the Beaver County Transit Authority.

In reviewing the General Fund budget, there are differences between actual amounts and those budgeted that are due to various business and economic factors within the County. General Fund expenses ended approximately \$4.1 million under budget. The County had operated fiscally prudent with each department manager monitoring employee expenses (overtime, travel), delaying major purchases, and imposing a freeze on job creation. The net result was a savings which enabled the County not to raise taxes for 2003. The current millage for Beaver County is 15.7.

County of Beaver's Capital Assets
(in thousands and net of depreciation)

What follows is a summary of the County's capital assets as of December 31, 2003 and 2002.

	<u>Governmental Activities</u>		<u>Business-type Activities</u>		<u>Totals</u>	
	<u>2003</u>	<u>2002</u>	<u>2003</u>	<u>2002</u>	<u>2003</u>	<u>2002</u>
Land	\$ 1,874	\$ 1,874	\$ 42	\$ 42	\$ 1,916	\$ 1,916
Buildings and Improvements	68,322	68,981	4,724	3,516	73,046	72,497
Vehicles	415	259	-	-	415	259
Furniture and Equipment	3,980	4,387	8,732	9,878	12,712	14,265
Infrastructure	<u>1,486</u>	<u>1,269</u>	<u>-</u>	<u>-</u>	<u>1,486</u>	<u>1,269</u>
Total	<u>\$76,077</u>	<u>\$76,770</u>	<u>\$ 13,498</u>	<u>\$ 13,436</u>	<u>\$ 89,575</u>	<u>\$ 90,206</u>

Additional information on the County's capital assets can be found in Note F on pages 76-79 of this report.

Outstanding Debt, at Year End

The County continued to make principal and interest payments on its existing long-term debt as scheduled. During 2003, the County issued two bond issues, \$5,375,000 in General Obligation Refunding Notes, Series A of 2003 and \$1,405,000 in General Obligation Bonds, Series B of 2003. The Series A Notes were issued for the purpose of refunding a prior bond issue. By refunding the prior bond issue, the County was available to obtain a lower interest rate on its debt and improve cash flow during 2003. The Series B Bonds were issued for the purpose of making capital improvements at Friendship Ridge. Refer to Note J for further details.

Here is a summary of the County's long-term debt at December 31, 2003 and 2002:

	<u>2003</u>	<u>2002</u>
Governmental activities		
General obligation debt	\$70,463,893	\$70,876,859
Other long-term debt	<u>4,180,000</u>	<u>4,325,000</u>
Governmental activities	74,643,893	75,201,859
Business-type activities	<u>6,018,792</u>	<u>5,170,000</u>
Total	<u>\$ 80,662,685</u>	<u>\$ 80,371,859</u>

The County's general obligation bond rating is 'AAA' insured from Standard and Poor. More detailed information about the County's long-term liabilities can be found in Note J on pages 86-94 of this report.

Economic Factors

The County has suffered significant losses in employment with the downsizing of USAirways. USAirways is the largest employer for Beaver County residents and is becoming a regional carrier. USAirways will no longer have Pittsburgh International as a HUB. Therefore, we are expecting further job losses for County residents.

Beaver County has been able to maintain a steady millage rate for two consecutive years and still maintain a positive fund balance without curtailing services to County residents. The Commissioners and elected officials continue to market Beaver County to entice tourists to visit the area and businesses to locate within the area.

Requests for Information

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

Office of the Controller
 Beaver County Courthouse
 810 Third Street
 Beaver, Pennsylvania, 15009-2196