

County of Durham, North Carolina

A Comprehensive

Annual



Financial Report

For year ended June 30, 2006

County of Durham, North Carolina



Comprehensive Annual Financial Report for the fiscal year ended June 30, 2006

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Prepared by the Durham County Finance Department

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INTRODUCTORY SECTION



Letter of Transmittal

November 30, 2006

Honorable Chairman and Members of the Board of County Commissioners
Durham County
Durham, North Carolina

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 accepted auditing standards (GAAS) by a firm of licensed certified public accountants. Pursuant to that requirement, we hereby issue the comprehensive annual financial report of Durham County for the fiscal year ended June 30, 2006.

This report consists of management's representations concerning the finances of Durham County. 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, management of Durham County has established a comprehensive internal control framework that is designed both to protect the government's assets from loss, theft, or misuse and to compile sufficient reliable information for the preparation of Durham County's financial statements in conformity with GAAP. Because the cost of internal controls should not outweigh their benefits, Durham County's comprehensive framework of internal controls has been designed to provide reasonable rather than absolute assurance that the financial statements are 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 County of Durham's financial statements have been audited by Cherry, Bekaert & Holland, LLP, a firm of licensed certified public accountants. The goal of the independent audit was to provide reasonable assurance that the financial statements of the County of Durham for the fiscal year ended 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 and that the County of Durham's financial statements for the fiscal year ended June 30, 2006 are fairly presented in conformity with GAAP. The independent auditors' report is presented as the first component of the financial section of this report.

The County is required to undergo an annual single audit in conformity with the provisions of the Single Audit Act, the US Office of Management and Budget Circular A-133, "*Audits of State and Local Governments*," and North Carolina state law for state funds. Information related to this single audit, including the schedule of financial assistance, findings and questioned costs, and the independent auditor's report on the internal control structure and compliance with applicable laws and regulations, are presented in a separate document.

GAAP requires 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 County of Durham's MD&A can be found immediately following the report of the independent auditors.

Profile of the Government

Durham County, incorporated in 1881, is located in the piedmont part of the state, which is considered to be the top growth area in the State, and one of the top growth areas in the country. Durham County currently occupies a land area of 299 square miles and serves a population of 249,654. Durham County is empowered to levy a property tax on both real and personal properties located within its boundaries.

Durham County has operated under the commissioner-manager form of government since 1930. Policy-making and legislative authority are vested in a governing board consisting of the chairman, vice-chairman and three other members. The governing board is responsible, among other things, for passing ordinances, adopting the budget, appointing committees, and hiring the government's manager (county manager), attorney and tax administrator. The county manager is responsible for carrying out the policies and ordinances of the governing board, for overseeing the day-to-day operations of the government, and for hiring the heads of the various departments. Effective with the 2004 election, the board members currently serve four-year terms. The chairman and the vice-chairman of the board are voted upon by the board in their first meeting which is in December after being sworn into office.

Durham County provides a full range of services, including sheriff and fire protection, emergency medical, human services (public health, mental health and social services), elections, register of deeds, animal control, youth home, criminal justice and cultural and recreational. Funding is provided for educational services of the Durham Public Schools and Durham Technical Community College. Also, the County funds services provided in conjunction with the City of Durham through interlocal agreements including economic and physical development, emergency communications, environmental engineering and inspections. Solid waste services are provided through contracting with a private company.

In accordance with standards of the Governmental Accounting Standards Board (GASB) defining the governmental reporting entity, this report includes all funds and component units (except as noted below) that are controlled by or are dependent on the County's governing body. Component units are legally separate entities for which Durham County is financially accountable. The Durham County Board of Alcoholic Beverage Control (ABC Board) is a component unit of Durham County. The ABC Board is presented as a proprietary fund. Additional information on the ABC Board can be found in Note A.1 in the notes to the financial statements. The Durham County Industrial Facility and Pollution Control Financing Authority (the "Authority") exists to issue and service revenue bond debt for private businesses for economic development purposes. The Authority is governed by a seven-member board, all of whom are appointed by the County Commissioners. The County can remove any board member of the Authority with or without cause. The Authority has no financial transactions or account balances; therefore, it is not presented in the financial statements. The Authority does not issue separate financial statements. Other governmental type entities within the County which have substantial autonomy and separate governmental characteristics are the Durham Public School Administrative Unit, Durham Technical Community College, Raleigh-Durham Airport Authority, the Special Airport District of Durham and Wake Counties, Triangle J Council of Governments, Triangle Transit Authority, Durham and Wake Counties Research and Production Service District and Advisory Committee, Durham Convention and Visitors Bureau and the Durham Civic Center Authority. These entities have not met the established criteria for inclusion in the reporting entity, and accordingly are excluded from this report.

The annual budget serves as the foundation for Durham County's financial planning and control. All agencies of Durham County are required to submit requests for appropriation to the county manager on or before March 15th of each year. The county manager uses these requests as the starting point for developing a proposed budget. The county manager then presents this proposed budget to the commissioners for review prior to May 31st of each year. The board is required to hold public hearings on the proposed budget and to adopt a final budget no later than June 30, the close of Durham County's fiscal year. The adopted budget is prepared by fund, function (e.g., public safety), and department (e.g., sheriff). However, the appropriations are formally budgeted and approved on a functional basis. The county manager is authorized to transfer budget amounts within a function up to 15% cumulatively without reporting to the Board of County Commissioners (BOCC). The county manager is authorized to transfer budget amounts between functions of the same fund up to \$20,000 with an official report of such transfer being made at the next regular meeting of the BOCC. Budget-to-actual comparisons are provided for each individual governmental fund for which an appropriated annual budget has been adopted. For the general fund, this comparison is presented on page 33 as part of the basic financial statements for the governmental funds. For nonmajor governmental funds, with appropriated annual budgets, this comparison is presented in the governmental fund subsection of this report, which starts on page 99.

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 specific environment within which the County of Durham operates.

Local Economy

Economic Development

Durham County has an expanding, diversified economy with a strong foundation in electronics, metallurgy, telecommunications, health care, and medical related industries. The City of Durham, the County's only municipality, is known as the City of Medicine because of the significant impact that biotechnology, health care and other medical related industries have on the economic base.

The County possesses a variety of technical resources and intellectual assets such as three nationally renowned doctoral based research universities with a strong entrepreneurial focus located in the region, state funded research centers in biotechnology and microelectronics, and a strong business support system. Close collaboration between the academic and business communities fosters a free flowing exchange of information and ideas beneficial to both groups.

Research and Development

Durham is located at the pinnacle of North Carolina's famous Research Triangle Park, formed in 1959 by business leaders, government officials and leaders from Duke University of Durham, North Carolina State University in Raleigh and the University of North Carolina at Chapel Hill. The Research Triangle Park (RTP) consists of 7,000 acres of land, 95% of its corporate enterprises are located in Durham County. RTP is the nation's largest and most successful research and development-oriented business park. The companies and organizations located in the Park represent some of the world's largest and most prestigious corporate and government organizations in scientific and technological research. There are an estimated 39,000 full-time employees working in the park, earning an average annual salary of \$56,000.

The employee population and average annual salary remained constant this past year. The number of research and development companies in the Park continues to grow. Recent locates to RTP include Fidelity Investments, Credit Suisse First Boston, Stiefel Laboratories, Network Appliance and Cree. Between these five companies, 3,091 initial new jobs with salaries averaging over \$80,000 were created this year alone. Initial capital investment stemming from these projects exceeds \$240,000,000.

The recuperation of the Park is happening gradually. In the meantime, research being conducted in Durham County continues to cover a broad range of high tech fields such as biotechnology, medical instrumentation, metallurgy, electronic hardware and software development, health care products, digital switching and transmission systems, telecommunication and microelectronics. There also continues to be an abundance of highly skilled graduates from the region's powerhouse research universities and prestigious law, business and medical schools. Perhaps the most striking indication of talent in the area is the large number of patents for inventions developed or discovered by the residents and/or companies of the County.

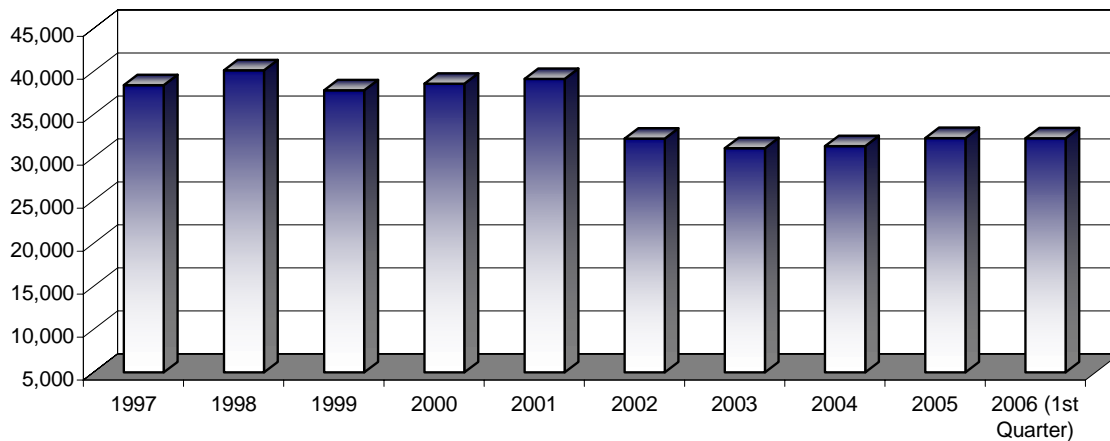
Durham's economy is certainly not limited to development of the Research Triangle Park. New construction is ubiquitous, a testimony to the fact that Durham is a nurturing environment for start-up companies. In addition, many companies from various regions of the US as well as other countries have moved their headquarters here to capture great cost savings. Quintiles Transitional Corporation, a Durham pharmaceutical-testing company, announced its expansion with an investment of approximately \$60 million along with the creation of 1,000 new jobs. Other new companies that announced their location and investment in the County this past year were Stiefel Labs, Kennedy Covington, Empire Distributors, United Therapeutics, Alba Bioscience USA, Abraxis Bioscience, Godfrey Group, RTI, Wavecome and Darchem TIP Corporation. Existing companies that are either expanding or have announced expansions to begin in the County are AW North Carolina, Fedelity, Blue Cross Blue Shield, DRI, Parata Systems, Eisai, Cormetech, Time Warner, EMC, Square One Bank, Duke Corporation Education, Quill Medial Raindrop Geomagic, LED Lighting Systems, Synthon, Ajilon, Tecan, Biogen and West Brothers. Eisai, a pharmaceutical company, has announced an expansion with an investment of approximately \$105 million along with the creation of 85 jobs. *National Policy Research Council*, ranked Durham-Raleigh the #3 best large metro for new business and entrepreneurs.

Health care

Durham Health Partners, Inc. (DHP) was formed in fiscal year 1999 – 2000 in a merger of three community-based health nonprofits – the City of Medicine Program, the Durham Healthy Carolinians Partner and the Foundation for Better Health of Durham. The consolidated organization's mission was to "promote effective solutions that remove barriers to improved community health." It strived to accomplish this mission through collaboration with many local health-related agencies, organizations, and resident groups. With these partners, DHP assessed community needs, facilitated the development of innovative solutions to Durham's public health issues, and identified resources necessary to implement and evaluate these solutions. Durham Health Partners served as an important resource for community health planning, coordination and facilitation at the local level. DHP also collaborated with regional, state, and national resources on these issues.

Durham Health Partners ceased operations as of June 30, 2004, in order to redefine DHP's mission and purpose for the Durham community. Durham Health Partners continues to focus on the community health needs of Durham County through a smaller, six person interim board. This interim board is exploring the design and implementation of a rational system of providing specialty medical care to Durham County's at risk/uninsured population. Currently, the Durham Health Partners board has received some planning grant monies to design and implement a pilot program of specialty access program initially focusing on Lincoln Community Health Center's patients. An advisory board of community members, providers and City/County government representatives was created, and it has begun collecting data and developing a health benefits plan for the specialty access program in order to seek three to five years funding from various public sources and private foundations. The Durham Health Partners board will seek ongoing financial support for the specialty access program.

Manufacturing



Source: Employment Security Commission (ESC)

Note: The ESC changed from using the SIC codes to the newer NAICS codes for counting employment. Therefore, the annual numbers have changed slightly from the fiscal year 2001-2002 report to reflect the new numbers for each year.

Durham County is not only a center for technology development; the County is also a strong manufacturing center. In 2005, the manufacturing sector employment increased from 31,302 in 2004 to 32,251 in 2005, an increase of 949 (3.03%). In the 1st quarter of calendar year 2006 the manufacturing sector employment slightly decreased to 32,218, a decrease of 33 (0.10%). Also, Eisai, a pharmaceutical company, has announced an expansion with an investment of approximately \$105 million along with the creation of 84 jobs.

Telecommunications

The telecommunications industry is making its presence known. The North Carolina information highway is the most advanced statewide telecommunications infrastructure in the nation, providing high-speed multimedia transmission. Verizon is the incumbent provider of phone service to Durham County. Verizon has in place one of the largest operational fiber optic networks in the world providing digital switching and high bandwidth options to virtually all Durham business centers. Intel Wireless Internet Accessibility survey ranked the Raleigh – Durham – Chapel Hill area as #8 in Wireless Internet Accessibility in the United States.

Quality of Life

Durham is in many ways comparable to a much larger city, but with a down-home charm. In July 2005, *CNN Money* ranked Durham one of the nation's 100 Best Places to live in 2005. In September 2006 *Silicon Valley Leadership Groups 2007 Projections Report* ranked Durham-Raleigh #1 in High Tech Region and in July 2006 *Forbes* ranked Durham-Raleigh #6 Best Cities for Singles. In November 2005 *Homebuilder.com* ranked Raleigh-Durham-Chapel Hill Top 20 Places to Live, Work and Play. In addition, Durham boasts nationally acclaimed restaurants and Broadway shows (which rehearse here prior to their Broadway premiers) as well as distinctive history and culture. Durham's advantageous location, climate and lifestyle draw companies from around the world to a place that has a dynamic business environment and a beautiful setting in the Piedmont region of North Carolina. In May of 2006, *Forbes* ranked Durham in Top Ten Metros for Business and Careers. Also, in June of 2005, *Milken Institute* ranked Raleigh-Durham-Chapel Hill #1 for Biotechnology, #2 for Life Sciences Human Capital, #4 for Life Sciences Workforce and #5 US Life Sciences Clusters.

Major Employers

Listed below are the largest business and institutional employers in Durham County.

Company or Institution

Duke University & Medical Center
IBM (International Business Machines)
Glaxo SmithKline
Durham Public Schools
Nortel Networks
Lenovo Group, Ltd.
Durham City Government
Veterans Administration Medical Center
Research Triangle Institute
Durham County Government
National Institute of Environmental Health Sciences
Blue Cross Blue Shield of North Carolina
North Carolina Central University
Cree, Inc.
Sterling Healthcare
US Environmental Protection Agency
AW North Carolina, Inc.
Quintiles Transnational
Verizon
Measurement Incorporated

Source: Durham Chamber of Commerce

Capital Investment

Many companies are either locating to Durham County or expanding their already existing operations in the County. Economic development announcements for 2005 were \$224,732,585. Economic development announcements occurring through the third quarter of 2006 amounted to over \$338 million.

Economic Development Statistics

Per Capita Income

Per capita income data for the last seven calendar years for Triangle MSA, Durham MSA, Raleigh/Cary MSA, North Carolina, and the United States are presented in the following table.

	1999	2000	2001	2002	2003	2004	2005
Triangle MSA	\$ 29,320	\$ 32,382	\$ 32,360	\$ 33,490	\$ 34,605	\$ -	\$ -
Durham MSA	-	-	-	-	-	32,482	33,505
Raleigh/Cary MSA	-	-	-	-	-	36,309	37,270
North Carolina	26,256	27,129	26,910	28,215	29,219	29,541	30,429
United States	28,938	29,676	29,561	31,065	32,209	33,127	34,212

Source: Bureau of Economic Analysis

As of 2004, Durham was no longer considered part of the Triangle Metropolitan Statistical Area.
Prior to 2004, Durham was considered a part of the Triangle Metropolitan Statistical Area.

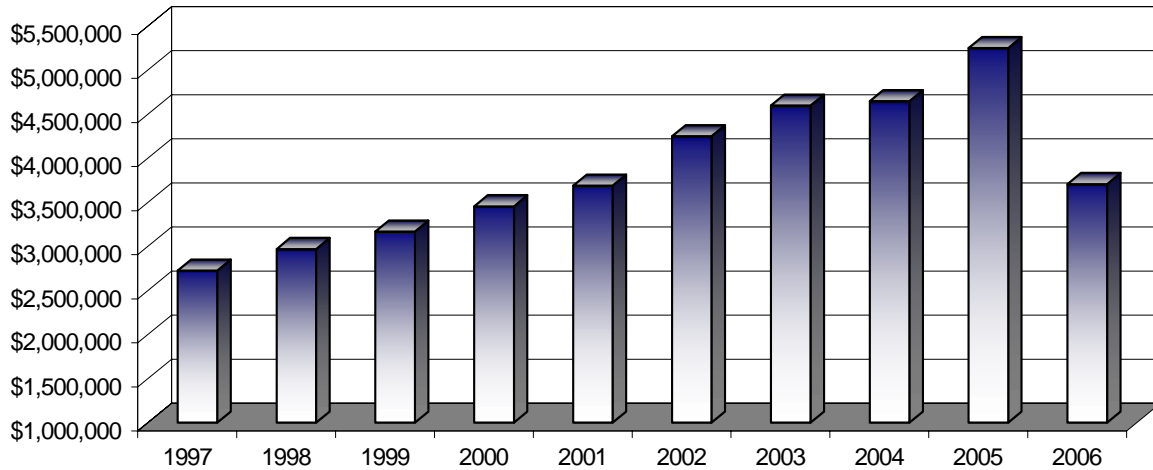
Retail Sales

Total retail sales in the County for the past ten fiscal years are shown in the following table.

Year Ended June 30,	Total Retail Sales (000's)	Total Taxable Sales (000's)	Percent Growth Over Previous Year
1997	\$ 2,725,364		5.6%
1998	2,969,822		9.0%
1999	3,167,577		6.7%
2000	3,455,668		9.1%
2001	3,688,799		6.7%
2002	4,057,352		10.0%
2003	4,597,853		13.3%
2004	4,646,891		1.1%
2005	5,085,956		9.50%
2006 (Through 1st Quarter)	n/a	3,707,314	*

Note: The NC Department of Revenue made an administrative rule change to report Retail sales, beginning in Fiscal Year 2006, based on total taxable sales reported on sales and use tax returns by July of the Fiscal Year in question, rather than gross retail sales. Therefore, 2006 Retail sales total is based on total taxable sales reported on sales and use tax returns submitted during July 2005. Data for total gross retail sales is no longer available due to the change made by the NC Department of Revenue. The calculation of

the “Percent Growth Over Previous Year” will be calculated beginning next year and every year thereafter.

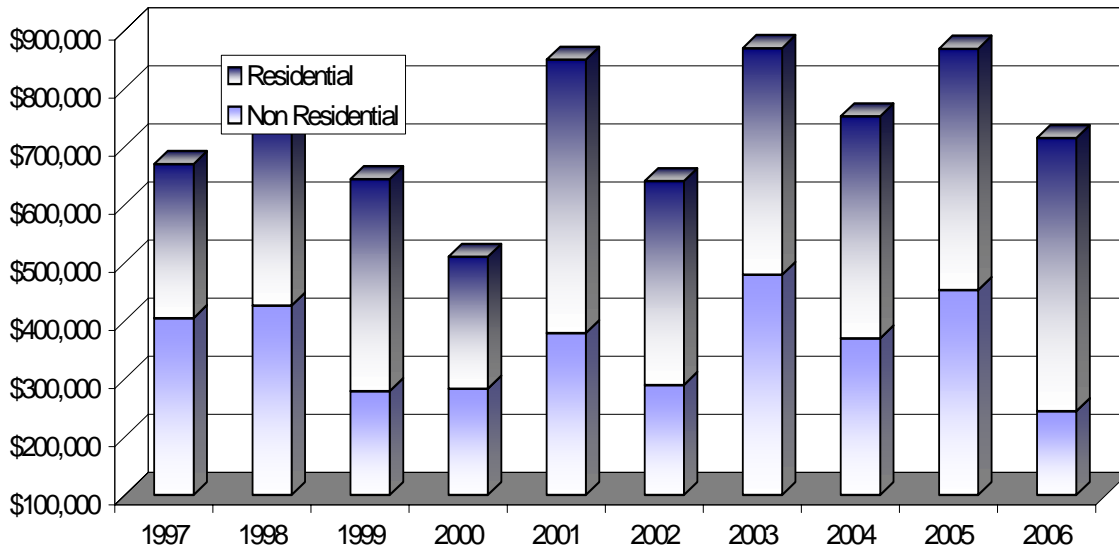


For fiscal years 2002, 2003, and 2004, Durham exceeded \$4.0 billion in gross retail sales activity. In fiscal year 2005, the County surpassed \$5.0 billion. Durham’s retail sales continue to grow as new shopping centers are built and older ones are renovated. Northgate Mall (an older mall) is turning shopping inside out through renovating the mall to include outside shopping, restaurants and an open plaza for year round entertainment as well as indoor shopping. Construction continues as Northgate makes this bold move in the marketplace providing the best of both worlds with shopping inside as well as shopping outside, food and entertainment. The continued growth is primarily because of the continued success of The Streets of Southpoint Mall, the success of Northgate Mall and the success of North Pointe Shopping Center.

Construction Activity

The following table illustrates construction activity in Durham County for the past ten calendar years by reference to the value of all building permits issued in the County.

	Non Residential		Residential		Total
	(000's)		(000's)		(000's)
1997	\$	404,749	\$	265,188	\$ 669,937
1998		426,382		313,702	740,084
1999		279,085		364,835	643,920
2000		283,104		227,067	510,171
2001		378,866		470,722	849,588
2002		289,707		350,767	640,474
2003		479,414		389,954	869,368
2004		369,602		382,513	752,115
2005		453,194		415,152	868,346
2006 (first 10 months)		244,653		469,848	714,501

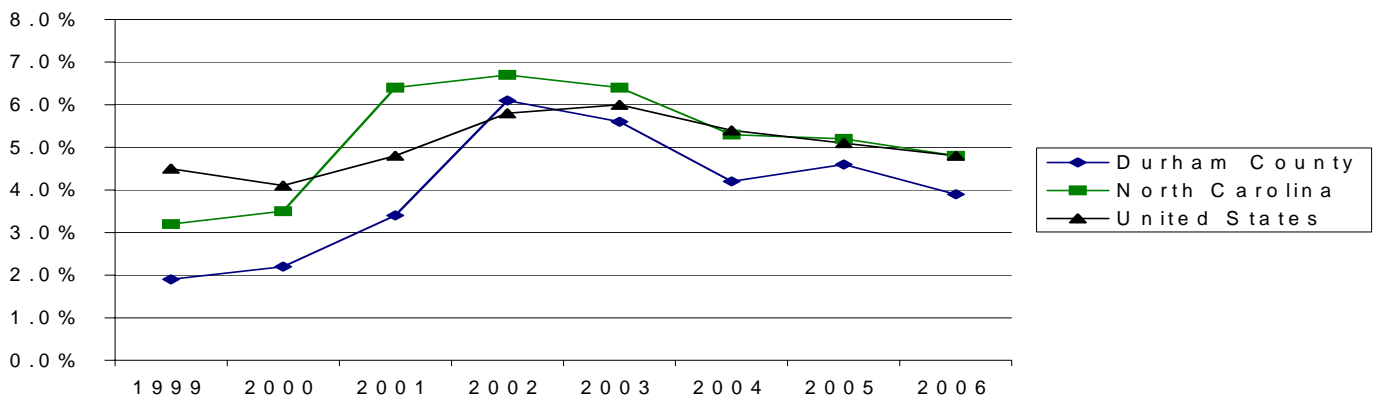


As of July 2006, the total number of occupied dwelling units in Durham County was 107,267. Also, for the first ten months of 2006, 3,303 residential permits have been issued for new residences and for improvements, repairs and expansions of existing residences. There was an increase in the value of construction activity in 2006 from 2005 for residential and non-residential. During the fiscal year 2006, the majority of growth was once again in the southern area of the County.

Unemployment

The percentage of unemployment in the County, State and the United States for the past eight fiscal years (as of June 30) as follows.

	Durham County	North Carolina	United States
1999	1.9%	3.2%	4.5%
2000	2.2%	3.5%	4.1%
2001	3.4%	6.4%	4.8%
2002	6.1%	6.7%	5.8%
2003	5.6%	6.4%	6.0%
2004	4.2%	5.3%	5.4%
2005	4.6%	5.2%	5.1%
2006	3.9%	4.8%	4.8%



As of October 2006, the County's unemployment rate has decreased to 3.6%. The County's rate is .90% less than the State's while the nation's percentage is at 4.7%. This is primarily because of the County's drive to create more jobs within the County and maintain a strong economy.

Long-term Financial Planning

The Board of County Commissioners continues to reaffirm the County's financial stability as one of its highest priorities. The Board recognizes that it is difficult to execute short- and long-term plans if the focus is on day-to-day viability. Consequently, the County's annual budget and financial decisions made throughout the fiscal year support an underlying philosophy to maintain a strong fund balance and the planned expansion of programs and services. Listed below are several of the County's major accomplishments for the year.

Facility Master Plan

The Facility Master Plan that was approved in fiscal year 1999 – 2000 laid the groundwork for the future building needs of the County and was centered on sound planning and solid financial research. The Master Plan was amended in fiscal year 2002 – 2003 to reflect the changes in facility needs for the Human Services Agencies, particularly Mental Health, and to analyze several potential options for meeting the facility needs of Social Services, Public Health and Mental Health. The Facility Master Plan as currently amended serves as the basis for the facility projects included in the Capital Improvement Plan. The two major projects currently in progress are the new court facilities (Justice Building) and the Human Services Complex to accommodate Public Health, Mental Health and Social Services. The status of these projects along with the minor projects of the Master Plan is included within the Capital Improvement Plan.

Capital Improvement Plan

The County maintains a 10-year Capital Improvement plan (CIP), which is fully updated every two years. The major update of the plan has been completed for the period fiscal year 2006-2015. The next update is scheduled to be completed for the period fiscal year 2008-2017. The plan itself provides a blueprint which the County uses to meet the growing facility needs of the schools, libraries, museum, court system, public safety, human service agencies, and open space. The CIP also provides a financial overview of the financing options for the existing capital projects as well as those capital projects not yet implemented projected in the 10-year plan. Annually, the financing options are reviewed, as well as the projects and their estimated costs. Accomplishments during the past fiscal year include the following: completed construction of the East Regional Library, completed construction of the Durham Center for Senior Life; completed renovations and additions to the Stanford L. Warren Library; completed Durham County Detention Center Breathalyzer addition and fingerprinting facility renovations; awarded construction contract for Emergency Medical Services Station No. 2; awarded design contracts for the Animal Control Offices, Judicial Building Elevator Modernization, Human Services Complex, and Justice Building; and acquired property for the Human Services Complex and Justice Building. The 2001 Bond Project accomplishments during the fiscal year are as follows: completed construction of the East Regional Branch Library, Durham Center for Senior Life, Stanford L. Warren Library and began

construction of EMS Station No. 2 and North Regional Library. The 2003 Bond Project accomplishments included demolition of existing buildings on the site of the South Regional Branch Library.

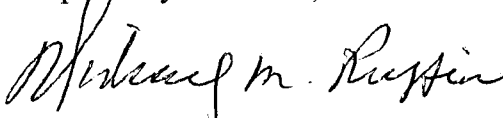
Awards and Acknowledgements

The Government Finance Officers Association (GFOA) awarded the Certificate of Achievement for Excellence in Financial Reporting to Durham County for its comprehensive annual financial report (CAFR) for the fiscal year ended June 30, 2005. This was the eighth consecutive year that the government has received this prestigious award. In order to be awarded a Certificate of Achievement, the government published an easily readable and efficiently organized CAFR. This report satisfied both GAAP and applicable legal requirements.

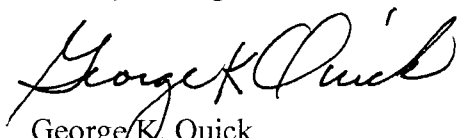
A Certificate of Achievement is valid for a period of one year only. We believe that our current CAFR continues to meet the Certificate of Achievement Program's requirements, and we are submitting it to the GFOA to determine its eligibility for another certificate.

The preparation of this report would not have been possible without the efficient and dedicated services of the entire staff of the Finance Department. We would like to express our appreciation to all members of the department who assisted and contributed to the preparation of this report. Credit also must be given to the Manager and the Board of County Commissioners for their unfailing support for maintaining the highest standards of professionalism in the management of Durham County's finances.

Respectfully submitted,



Michael M. Ruffin
County Manager



George K. Quick
Finance Director

Durham County Board of County Commissioners



Ellen W. Reckhow
Chairman



Becky M. Heron
Vice Chairman



Philip R. Cousin, Jr.



Lewis A. Cheek



Michael D. Page

Durham County Administration



Mike Ruffin
County Manager



George K. Quick
Finance Director

