

Mayor's Letter



City of Chattanooga
Office of the Mayor

City Hall 101 East 11th Street Chattanooga, Tennessee 37402

November 26, 2014

To the Citizens and City Council of the City of Chattanooga:



Mayor Andy Berke

I am honored to present the City of Chattanooga's annual financial report for the year ended June 30, 2014. Since I took office, I have made sure city government's actions match our community priorities. Safer streets, smarter students and stronger families, a growing economy, stronger neighborhoods, and high performing government – Chattanoogaans tell me these are the areas they want to see addressed. And we are addressing them, every day.

Over the past year, we have made strides in public safety. From the Chattanooga Violence Reduction Initiative to a more proactive and community-focused police department, we are diligently working to ensure our streets are safe for all Chattanoogaans. On top of that, the City successfully reformed an underfunded Police & Fire pension, putting the pension plan on a sustainable path in a fiscally responsible way. That means taxpayers will save a total of \$227 million and, at the same time, we will ensure the fund is able to pay benefits to tomorrow's retirees.

A great city supports its families and students by providing access to opportunity. Throughout the year we have turned our 18 Youth & Family Development Centers into places for learning and growth. Our literacy initiative has resulted in more children reading at grade level and our Chattanooga Ambassador Program is helping young people prepare for success through intense mentorship and training.

To grow our local economy, the City created an Economic Development office, purchased the former Harriet Tubman housing complex to create jobs in East Chattanooga, and refocused The Enterprise Center to capitalize on Chattanooga's emerging reputation as a technology hub. We began pulling together the essential entities for the creation of an innovation district and put the wheels in motion to offer incentives to our small businesses, as well as paved the way for Volkswagen to announce a second line at their existing Chattanooga plant. Volkswagen's announcement, which came in July of 2014, means the creation of 2,000 new jobs in Chattanooga and a total investment of \$900 million.

The City is able to do all of this and more because of the hard work and talent of our employees. Whether it is delivering essential services or innovative policy solutions, city government is more attentive than ever to enhancing quality of life for Chattanoogaans throughout our City.

Sincerely,

A handwritten signature in black ink that reads "Andy Berke".

Mayor Andy Berke
City of Chattanooga



City Council



Chip Henderson
Chair
District 1



Jerry Mitchell
District 2



Ken Smith
District 3



Larry Grohn
District 4



Russell Gilbert
District 5



Carol Berz
Vice Chair
District 6



Chris Anderson
District 7



Moses Freeman
District 8



Yusuf Hakeem
District 9



Letter of Transmittal



City of Chattanooga
Department of Finance and Administration
City Hall
101 East 11th Street
Chattanooga, Tennessee 37402

November 26, 2014

To the Honorable Mayor Andy Berke, Members of the City Council and the Citizens of Chattanooga, Tennessee:

State and local statutes require that the City publish annual audited financial statements for each fiscal year. This Comprehensive Annual Financial Report (CAFR) of the City of Chattanooga for the fiscal year ended June 30, 2014 is submitted in compliance with this requirement.

Management assumes full responsibility for the completeness and reliability of the information contained in this report, based upon a comprehensive framework of internal control that it has established for this purpose. Because the cost of internal control should not exceed anticipated benefits, the objective is to provide reasonable, rather than absolute, assurance that the financial statements are free of any material misstatements.

Henderson, Hutcherson & McCullough, PLLC, Certified Public Accountants, have issued an unqualified ("clean") opinion on the City of Chattanooga's financial statements for the year ended June 30, 2014. The independent auditor's report is presented as the first item in the financial section of this report.

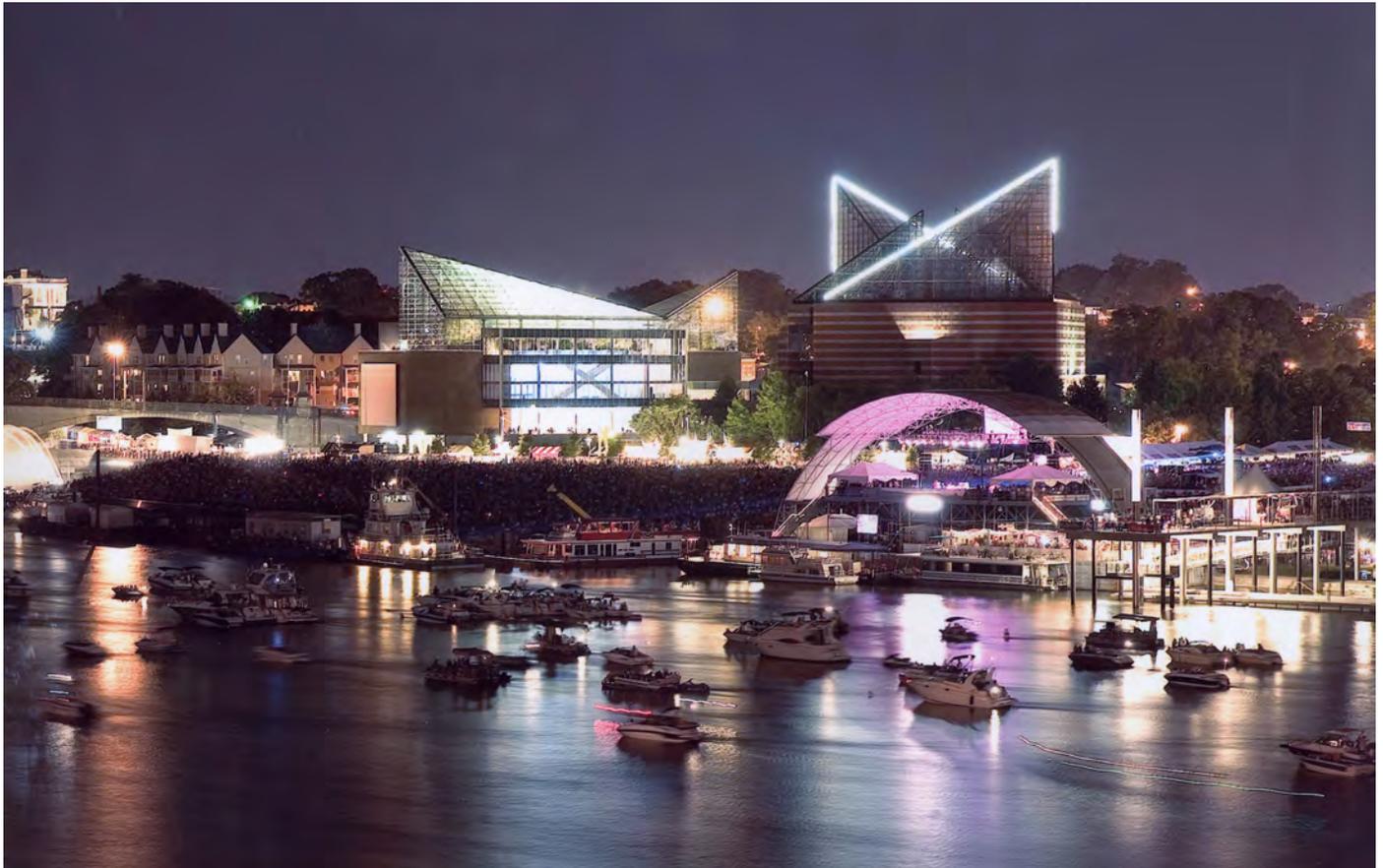
The independent audit of the City's financial statements was part of a broader, federally mandated "Single Audit" designed to meet the special needs of federal grantor agencies. The standards governing Single Audit engagements require the independent auditor to report not only on the fair presentation of the financial statements, but also on the audited government's internal controls and compliance with legal requirements. Special emphasis is placed on internal controls and legal requirements involving the administration of federal awards. These reports are in a separate Single Audit section.

Generally Accepted Accounting Principles 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 City of Chattanooga's MD&A can be found immediately following the financial statement report of the independent auditors.



Daisy W. Madison, City Finance Officer





GOVERNMENTAL STRUCTURE, ECONOMIC CONDITIONS AND MAJOR INITIATIVES

PROFILE OF THE GOVERNMENT

Nestled in a bend of the Tennessee River and surrounded by mountains and lakes, Chattanooga is so beautiful it inspired a community quest to make it the best mid-sized city in America. Living in Chattanooga means that outdoor views and adventures are around every corner, but our city is much more than a pretty playground. Over the last four decades, we've been winning acclaim for our unique way of working together to produce national best practices for cleaning up air pollution, downtown revitalization, affordable housing, and much more.

Founded as a ferry landing and warehouse site in 1815, the City of Chattanooga was incorporated under State of Tennessee Private Acts of 1839. The City is the county seat of Hamilton County and is located near the southeastern corner of the state on the Tennessee-Georgia border. Chattanooga is centrally located in relation to other major population centers of the southeast, being within a 150-mile radius of Knoxville and Nashville, Tennessee; Birmingham, Ala-

bama; and Atlanta, Georgia. Over 11 million people live within a 2 to 2½ hour drive of Chattanooga. It encompasses an area of 148 square miles. Official results of the 2010 U.S. Census show a population of 167,674, a 7.8% growth since the 2000 Census. The City is empowered to levy a property tax on both real and personal property located within its boundaries. Corporate limits may be extended at the request of the property owner or by a referendum of the people in the affected areas that might want to petition to come into the city.

The City Mayor is elected at-large and is not a member of the City Council. The Council is composed of nine members, with each member being elected from one of nine districts within the geographic boundaries of the City. The Mayor and Council are elected on a non-partisan basis for four-year terms. The Mayor is the City's chief executive officer and oversees the operation of all City departments.

The City provides a full range of municipal services including but not limited to fire and police protection; sanita-



tion services and recycling; construction and maintenance of highways, streets and infrastructure; recreation and cultural activities; youth and family development; public library; community development; planning and zoning; neighborhood services; social services; and general administrative services. It also operates a water quality program, a solid waste program and a wastewater system for its residents and for other communities in southeast Tennessee and northwest Georgia. The City's Electric Power Board (EPB) provides electric and fiber-to-home services. Other services are provided through legally separate Chattanooga Downtown Redevelopment Corporation which is reported along with EPB as an enterprise fund. Additional services are provided through the legally separate Metropolitan Airport Authority and the Chattanooga Area Regional Transportation Authority, both of which are reported separately within the City's financial statements. Additional information on all these legally separate entities can be found in the notes to the financial statements.

The annual budget serves as the foundation for the City's financial planning and control. In lieu of the traditional approach, the City develops its annual budget utilizing the Budgeting for Outcomes (BFO) approach. BFO is a process designed to create a government that works better and costs less. It is based on the premise that the percentage of personal income the public is willing to pay for their government through taxes, fees, and charges is fixed. While the "price of government" is fixed, the cost of providing services is increasing. Budgeting for Outcomes focuses on results and priorities, not cost. The budget process shifts from paying for costs to buying results. It puts citizens and their priorities, not status quo, first. It emphasizes accountability, innovation, and partnerships. The City Finance Officer obtains budget offers from all City departments and agencies to address the major results area communicated by the citizens. These results areas are safer streets, a growing economy, stronger neighborhoods, smarter students and stronger families, and high performing government. Offers are evaluated by a Results Team and allocations are recommended by the Mayor based on citizens' priorities and available funding. During the months of April, May and June, advertised public hearings are held by the council whereby taxpayers are given the opportunity to comment prior to final passage. The budget is legally enacted through passage of an ordinance with an operative date of July 1. The appropriated budget is adopted on a departmental basis; the legal level of budgetary control is the fund level. The City Finance Officer is authorized to make intra-fund transfers if necessary and report to council. Budgetary comparison schedules are provided in the budget document for each individual governmental fund for which an appropriated annual budget has been adopted.

FACTORS AFFECTING FINANCIAL CONDITION

The information presented in the financial statements

may be best understood when it is considered from the broader perspective of the specific economic environment within which the City of Chattanooga operates.

The Local Economy: Employment in the Chattanooga area is diverse. The top employment sectors of trades, transportation, and utilities (22%), government (15%), manufacturing (13%), professional and business services (18%), education and health (14%), and leisure and hospitality (10%) comprise 92% of the workforce. Employment in the retail service sector continues to thrive. Hamilton Place Mall, which is in its 28th year of operation, anchors the area's most vibrant retail corridor along I-75. Most recently a new hotel, operated by a major chain, has opened along the south end of the mall's retail campus. Additional retail expansion continues just north of the mall at Waterside, a mixed used development encompassing over 40 acres.

Downtown is continuing to attract new investment as well. The first phase of a proposed \$100 million housing and commercial project on the west side of downtown along the river is taking shape. This will include 39 homes and luxury townhomes along Riverfront Parkway which are expected to range upward from \$319,000 each. Hotel space in the downtown area is continuing to increase as well. A \$19 million hotel, with 140 rooms, is currently under construction. Most recently, another new hotel was announced for the downtown area. This 90-room upscale boutique hotel is slated to open in 2016 near the Tennessee Aquarium. These projects, along with numerous other housing and retail developments under construction or under consideration throughout the city, will guarantee a strong base for growth in the coming years.



Chattanooga enjoys strategic advantages related to its location, strong transportation system, natural resources and competitive cost of doing business. The local unemployment rate of 7.3% for the Metropolitan Statistical Area remains below the state average of 7.4% but higher than the national average of 6.3% as of August, 2014, according to information from

the Tennessee Civilian Labor Force Summary. Fiscally, the City of Chattanooga is well positioned for future growth.

Chattanooga remains a world leader in technology. The Electric Power Board, Chattanooga's municipal power provider, offers a one-gigabit per second internet service. Few other cities in the world offer such lightning-fast service. This puts Chattanooga at 10 times faster and 10 years ahead of the FCC National Broadband Plan, according to EPB officials. The Fiber-to-the-Home (FITH) network has grown to become available to all 170,000 homes, schools, and businesses in the service area, a total of 600 square miles that covers urban, suburban, and rural places and a diverse population of 300,000 people. The system is integrated with Smart Grid, a technology which allows remote monitoring of meters for every customer. A \$111 million federal stimulus grant from the Department of Energy dramatically accelerated the installation of the Smart Grid, shortening the planned five year implementation schedule to two years. A wireless mesh network is piggybacked onto the entire system, enhancing public safety as well. This year, EPB applied to the Federal Communications Commission to become the first utility to provide service outside its existing approved service area, which is regulated by the State of Tennessee. The high-speed internet has attracted competition and international visitors. In 2014, Chattanooga hosted its third GigTank competition, hosting specialists from around the world to develop business ideas. In October, a delegation from New Zealand arrived to take a first-hand look at ways the service can generate economic growth.



Manufacturing has been in the midst of resurgence over the past six years. Since 2008, the Chattanooga area has attracted \$4 billion in foreign direct investment including a Volkswagen auto assembly plant and major investments in alternative energy. The Enterprise South Industrial Park (ESIP), home to Volkswagen AG's U.S. manufacturing headquarters, plant, and supplier park hosting numerous companies, as well as an Amazon distribution center, has essentially been filled or committed for potential expansion of the VW plant.

The most significant manufacturing investment of the past year is the announcement by Volkswagen of a major plant expansion with a total investment of \$900 million from all sources. The \$600 million investment by VW is expected to

bring 2000 jobs directly to the manufacturing plant as well as 3600 jobs to support industries and suppliers. State and local government are providing \$230 million in direct support, including \$26.25 million directly from the City of Chattanooga, and up to \$70 million in incentives and infrastructure improvements over the next decade. The plant's footprint will grow by over 500,000 square feet, or more than twenty five percent. In conjunction with the plant expansion to build a new sport utility vehicle, VW will open a Research and Development (R&D) Center, to employ 200 professionals in engineering and related fields. This R&D facility is a first of its kind for Tennessee. Also included in the new agreement is the decision to locate the \$12 million Volkswagen Visitors Center, envisioned as part of the original 2008 investment, in downtown Chattanooga. Local payroll as a result of these expansions is expected to add \$100 million in payroll to the local economy. As this expansion takes place, additional suppliers have committed to the area. Plastic Omnium Auto Exterior announced a \$65 million factory to furnish parts for the automobiles.

VW retains an option on 900 additional acres adjacent to their 1,300 acre facility, allowing room for significant additional future expansion. This releases 300 acres in the industrial park which would be ideal for other first-tier suppliers to the plant. When this expansion phase is complete, there will still be enough remaining land to enable the size of the assembly plant to be doubled.

Retention of existing jobs can be as important as the addition of new. Not only is the city attracting new industry, it is retaining and expanding historic industry as well. The Chattanooga Coca-Cola Bottling Company, with a presence in our city for 115 years, has broken ground on a new \$62 million distribution center and regional headquarters. The new facility near I-75 will absorb the Dalton, Georgia and Scottsboro, Alabama distribution regions and will bring over 40 jobs in addition to the 270-employee base. Chattem Chemicals Inc., founded here in 1879, will invest \$6 million and add 25 jobs over the next year.

These successes and many more are the result of strong leadership among all the various civic leaders and elected officials. The third phase of the Chattanooga Chamber of Commerce "Chattanooga Can Do" campaign, being conducted from July 2011 – June 2015, has set goals for job growth. These goals include the following benchmarks (with progress as of September 2014 in parentheses):

- Increase regional employment by 15,121 (14,753)
- Increase private investment by \$500 million (\$847 million)
- Create \$427 million in new payroll income (\$705 million)



Quality education is also the centerpiece of a successful community. Chattanooga State Technical Community College maintains five training partnerships with local manufacturers or groups to provide industry-specific training to students, allowing flexibility so programs can be tailored to current needs. This approach to educational and training support to industry will serve to attract additional new manufacturing and technical jobs to the area. The Hamilton County Public School System has established a Science, Technology, Engineering and Math (STEM) school, located on the Chattanooga State campus, which provides coursework based on hands-on training and offers internships or apprenticeships to the students.

Transportation is another key to a vibrant economy. The Chattanooga area is served by three interstate highways, seven U.S. highways, two railways, airlines, bus service, and the Tennessee River system. Direct flights are available to ten major cities. Chattanooga is home to three major air cargo facilities, three public use port terminals, and four major industrial parks. Railway service is provided by four divisions of the Norfolk Southern Railway System and two divisions of the CSX Transportation System, all with switching service throughout the entire area. Modern “piggyback” service is provided by both lines.



Another contribution to the local economy is the level of support we enjoy from several national events held here. Among those which took place over the past year were the Head of the Hooch rowing competition, the USA Cycling pro championships and Ironman Chattanooga. These and a host of regional tournaments, outdoor events, and recreational activities, bring millions to the local economy and help keep Chattanooga in the forefront.

The fiscal health of Chattanooga City Government remains strong. As outlined in the Management’s Discussion and Analysis on page iv, the City has maintained a healthy financial position through sound fiscal management. We have a history of strong fiscal discipline, healthy reserves, and constant review of operations, being ever vigilant to find new effi-

ciencies and cost reduction measures. Standard and Poor’s Ratings Services raised the City’s bond rating to AAA in November, 2013, which was reaffirmed as AAA Stable in June, 2014. Fitch Ratings affirmed their bond rating for the City at AA+ Stable in June, 2014.

Long-term financial planning: The City takes a long range approach to capital spending by the adoption of a five year capital plan. As part of the strategic plan, the new administration has restructured operations to include a department of economic and community development that focuses intensely on sustainable growth and maintenance of a vibrant community. The City’s ultra-high-speed broadband mesh network will carry the City well into the future. The network was the key factor in Chattanooga being voted among the world’s Top Seven intelligent Communities by the Intelligent Community Forum. The City continues to explore growth opportunities through economic development, regional growth plans, and other strategic initiatives that involve all citizens.

The City began a new approach to budget preparation and management, known as Budgeting for Outcomes, for the Fiscal Year 2014 budget. This approach is designed to measure results against goals and benchmarks used in determining funding levels for all city operations. Budgeting for Outcomes will provide accountability by providing for regular review and monitoring of departmental performance by the Mayor, the City Finance Officer and other senior City officials. The City’s annual performance report to the citizens of Chattanooga gives residents an update on how city services are responding to their needs. It also provides department heads and managers with quantifiable information to assess performance in meeting the City’s goal of efficient and effective management of resources in providing quality services to the citizens of Chattanooga.

Relevant financial policies: The City Council has adopted a Debt Management Policy which is intended to guide current and future decisions related to debt issued by the City. Performance is measured against benchmarks set forth and changes are made as needed to meet the desired goals.

Major initiatives: Over five (5.8) square miles have been annexed since May, 2001. Chattanooga is a major participant in a 40-year regional growth plan, known as the Greater Chattanooga Regional Growth Initiative, or “Thrive 2055”. The participants include sixteen counties and their major cities from southeast Tennessee, northwest Georgia, and northeast Alabama, including the three metropolitan statistical areas. This public-private initiative is a pioneering effort for a new kind of long-term regional plan. It is a continuation of the type of public visioning and community engagement that has transformed Chattanooga and the surrounding area over the past 30 years.



Awards and Acknowledgments

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the City of Chattanooga, Tennessee for its comprehensive annual financial report for the fiscal year ended June 30, 2013. This was the twenty-second consecutive year that the City has received this award. The Certificate of Achievement is a prestigious national award, recognizing conformance with the highest standards for preparation of state and local government financial reports.

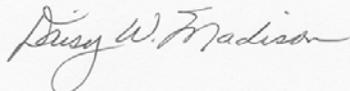
In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized comprehensive annual financial report, whose contents conform to program standards. Such reports must satisfy both Generally Accepted Accounting Principles and applicable legal requirements. A Certificate of Achievement is valid for a period of one year only. We believe our current report continues to conform to the Certificate of Achievement program requirements, and we are submitting it to GFOA to determine its eligibility for another certificate.

The City also received the GFOA Award for Distinguished Budget Presentation for its annual appropriated budget for each of the nineteen fiscal years for which it applied. In order to qualify for the Distinguished Budget Presentation Award, the City's budget document was judged to be proficient in several categories including policy documentation, financial planning and organization.

The GFOA Award for Outstanding Achievement in Popular Annual Financial Reporting was received for the fiscal year ended June 30, 2013. This is the third consecutive year for which the City applied for the award. In order to qualify, a government must publish a Popular Annual Financial Report with contents that conform to program standards of creativity, presentation, understandability, and reader appeal.

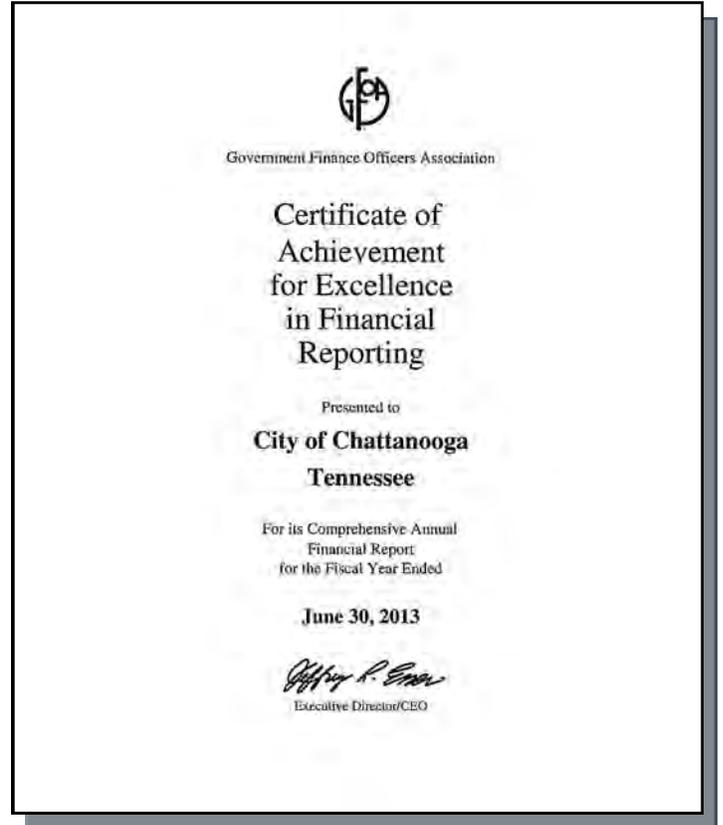
The preparation of this report could not have been accomplished without the professional and dedicated services of the entire staff of the Finance Department and the City's independent public accountants, Henderson, Hutcherson & McCullough PLLC. We would like to express our appreciation to members of various City departments who assisted and contributed to the preparation of this report. Further appreciation is extended to the Mayor and the City Council for their interest and support in planning and conducting the financial affairs of the City in a responsible and progressive manner.

Respectfully submitted,



Daisy W. Madison

City Finance Officer



City Officials as of June 30, 2014



EXECUTIVE BRANCH:

Andy Berke, Mayor
Travis McDonough, Chief of Staff
Jeffery Cannon, Chief Operating Officer

CITY COUNCIL:

Chip Henderson, Chair.....District 1
Carol Berz, Vice Chair.....District 6
Jerry Mitchell.....District 2
Ken Smith.....District 3
Larry Grohn.....District 4
Russell Gilbert.....District 5
Chris Anderson.....District 7
Moses Freeman.....District 8
Yusuf Hakeem.....District 9

COURTS:

Sherry B. Paty.....City Court Judge
Ron Swafford.....City Court Clerk
Russell J. Bean.....City Court Judge

DEPARTMENT ADMINISTRATORS

Legal.....Wade Hinton.....City Attorney
Legislative.....Sandra Freeman.....Clerk of Council
Finance and Administration.....Daisy W. Madison.....Administrator
Vickie C. Haley.....Deputy Administrator
Fire.....Chief Lamar Flint.....Administrator
Economic andDonna Williams.....Administrator
Community Development Anthony Sammons.....Deputy Administrator
Police.....Chief Fred Fletcher.....Administrator
Public Works.....Lee Norris.....Administrator
Youth and Family Development.....Lurone Jennings.....Administrator
Transportation.....Blythe Bailey.....Administrator



Organization Chart

