

March 30, 2007

The Honorable Mayor, Councilmembers,
and Citizens of the City of Clearwater:

The City of Clearwater Charter (Section 2.01(c)3), Florida Statutes, and various covenants relating to debt and pension obligations of the City require an annual audit of the City's financial statements of all funds of the City by a firm of licensed certified public accountants. These statements must be presented in conformity with generally accepted accounting principles (GAAP) and audited in accordance with generally accepted auditing standards. Pursuant to these requirements we hereby issue the comprehensive annual financial report of the City of Clearwater for the fiscal year ended September 30, 2006.

This report consists of management's representations concerning the finances of the City. 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 the City 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 the City's financial statements in conformity with GAAP. Because the cost of internal controls should not outweigh their benefits, the City'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.

Cherry, Bekaert & Holland L.L.P., a firm of licensed certified public accountants, has audited the City's financial statements. The goal of the independent audit was to provide reasonable assurance that the financial statements of the City for the fiscal year ended September 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 that there was a reasonable basis for rendering an unqualified opinion that the City's financial statements for the fiscal year ended September 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 the report.

The independent audit of the financial statements of the City was part of a broader, federally mandated "Single Audit" designed to meet the special needs of federal and state 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, with special emphasis on internal controls and legal requirements involving the administration of federal and state awards. These reports are in the Single Audit section of this report.

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

Profile of the City of Clearwater, Florida

Clearwater is located on the Pinellas Peninsula on Florida's west coast. It is directly located on the Gulf of Mexico, 20 miles west of Tampa and 20 miles north of St. Petersburg. Clearwater is the county seat of Pinellas County and one of the largest cities in the Tampa Bay area. The Clearwater area offers a semitropical climate and 28 miles of beautiful beaches. Consequently, tourism is an important component of the economy. In addition to tourism, Clearwater enjoys a diversity of manufacturing businesses, service industries, high-tech companies, and a large retirement population.

The City operates under the council/manager form of government. Policymaking and legislative authority are vested in the City Council, which consists of a mayor and four members elected at large on a non-partisan basis. The City Council is responsible for adopting ordinances, adopting the budget, and hiring the City Manager and City Attorney. The City Manager is responsible for carrying out the policies and ordinances of the City Council, for overseeing the day-to-day operations of the City, and for appointing the heads of the City's departments.

The City provides police and fire protection; construction and maintenance of streets, bridges, sidewalks, storm drainage, public parks, and recreation facilities; planning, zoning, subdivision, and building code regulation and enforcement; redevelopment of commercial and residential neighborhoods; supervised recreation programs; public libraries; water supply and distribution; waste water collection, treatment, and disposal; natural gas distribution; solid waste collection and recycling; stormwater management; marina, airpark, convention center, and public fishing pier operations; and operation of the city-wide parking system.

The annual budget serves as the foundation for the City's financial planning and control. Per the City Code of Ordinances, the City Manager is required to provide to the City Council an operating budget for the ensuing fiscal year, a capital improvement budget, and a five-year capital improvement program, along with an accompanying budget message no later than 60 days prior to the end of the fiscal year. The Council is required to hold public hearings on the budget and to adopt a final operating budget and capital improvement budget no later than September 30, the last day of the City's fiscal year. The appropriated budget is prepared by fund and by department within fund.

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 City operates.

Local Economy

The Tampa Bay metropolitan area economy continues to improve. The unemployment rate improved from 3.7 percent for September 2005 to 3.2 percent for September 2006. The national average for September 2006 was 4.6 percent unemployment versus 5.1% for September 2005. Business development interest in the City's downtown and beach areas has continued to increase significantly in recent years as property valuation increases reflect. We are also seeing a continued interest in the City's markets for multi-family and residential housing.

Long-term Financial Planning

A major project completed during fiscal 2006 was \$15.8 million of stormwater drainage and roadway improvements to downtown's Myrtle Avenue. The improvements will significantly improve stormwater drainage and help relieve traffic congestion in the downtown area. Additionally, fiscal 2006 saw the continuation of \$7.5 million of Glen Oaks stormwater improvements, to include a lakefront community park and soccer fields while removing approximately 100 homes from the Stevenson Creek floodplain. Fiscal 2006 also marked the beginning of construction of the new downtown streetscape, an important step in the redevelopment and revitalization of downtown. Finally, the year also welcomed the beginning of construction of Beach Walk, a \$30 million project that promises to redefine the face of Clearwater Beach. The project includes winding promenades, lush landscaping, and amenities such as whimsical showers, cool places to relax, and distinctive artistic touches that will reinvent the Clearwater tourist experience. The Beach Walk project is expected to be completed during fiscal 2009.

An important future City initiative is construction of proposed boat slips for the downtown waterfront. The \$11 million project will include up to 140 boat slips, over 2,500 feet of "side-tie" moorings for overnight and day visits, and will coordinate with a pedestrian promenade. The project is an important component of downtown and beach redevelopment efforts and will enhance community access to Clearwater's waterfront. Construction is forecast to begin in fiscal 2008 with project completion expected during fiscal 2009.

Cash Management Policies and Practices

As more completely described in Note I (D)(1) of the notes to the financial statements, the City employs a consolidated cash pool to facilitate short-term investment of liquid assets for all City funds. The City believes that a conservative investment philosophy best serves the residents of Clearwater, and that the return of the investment principal is more important than the return on the principal. However, the City attempts to maximize the return, while maintaining a conservative philosophy, via accurate cash flow forecasting and competitive selection of investments. The cash pool earned an average rate of return of 4.15% on its investments during fiscal year 2006.

Risk Management

The City is self-insured within certain parameters for losses arising from claims for general liability, auto liability, police professional liability, public officials' liability, property damage, and workers' compensation. The transactions relating to the self-insurance program are accounted for in the Central Insurance Fund, and are reported as an Internal Service Fund. The City is not self-insured with respect to major medical coverage. Management believes that the amounts showing as claims payable and the unreserved retained earnings are adequate to cover all reasonable projected losses arising from events occurring on or prior to September 30, 2006. Additional information on the City's risk management activity can be found in Note IV (A) of the notes to the financial statements.

Pension

The Employees' Pension Plan and the Firemen's Pension Plan are single-employer defined benefit pension plans that are self-administered by the City. Each year, independent actuaries engaged by the pension plans calculate the amount of the minimum required contributions that the City must make to each of the plans to ensure that the plans will be able to fully meet their obligations to retired employees on a timely basis. City contributions for the year were in accordance with actuarially determined funding requirements.

In addition, supplemental pensions exist for certified Police Officers and Firefighters under the provisions of Florida Statutes Sections 175 and 185. These plans are funded solely from excise taxes on certain insurance premiums covering property in Clearwater. The excise taxes are collected by the state and remitted to the City. Both plans require benefits to be adjusted to equal fund assets provided by the defined contributions.

Additional information on the City's pension plans can be found in Note IV (D) of the notes to the financial statements.

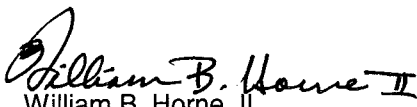
Awards and Acknowledgements

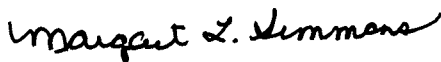
The Government Finance Officers Association (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the City for its comprehensive annual financial report (CAFR) for the fiscal year ended September 30, 2005. This was the twenty-seventh consecutive year that the City received 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.

In addition, the City received the GFOA's Distinguished Budget Presentation Award for the fiscal year 2007 Budget document, the twenty-first consecutive year that this award has been received. In order to qualify, the City's Budget document was judged to be proficient in several categories including as a policy document, a financial plan, an operations guide, and a communications device.

We wish to thank the many members of the Citywide Annual Financial Reporting (CAFR) team, which is composed of individuals in the Finance Department and other financial staff throughout the City, for their professionalism and dedication in producing this report. In addition, we thank the Graphic Communications Division for the professional printing of this report. Sincere appreciation is also extended to the City's external auditors, Cherry, Bekaert & Holland, L.L.P., for their advice and assistance in the preparation of this report. Finally, we would like to thank the City Council for their interest, continued support, and leadership in planning and conducting the financial operations of the City in a progressive and responsible manner.

Sincerely,


William B. Horne, II
City Manager



Margaret L. Simmons, CPA
Finance Director