CITY OF GRAND MARAIS, MINNESOTA

FINANCIAL STATEMENTS AND SUPPLEMENTARY INFORMATION
Year Ended December 31, 2008

CITY OF GRAND MARAIS, MINNESOTA

TABLE OF CONTENTS
December 31, 2008

	Page
ORGANIZATION	1
FINANCIAL SECTION	
Independent Auditor's Report	2
Management's Discussion and Analysis	4
Basic Financial Statements	
Government-wide Financial Statements	
Statement of Net Assets	11
Statement of Activities	12
Fund Financial Statements	
Governmental Funds	
Balance Sheet	14
Reconciliation of the Balance Sheet of Governmental Funds to the Statement of Net Assets	15
Statement of Revenues, Expenditures and Changes in Fund Balances	16
Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balances of Governmental Funds to the Statement of Activities	17
Proprietary Funds	
Statement of Net Assets	18
Statement of Revenues, Expenses and Changes in Fund Net Assets	19
Statement of Cash Flows	20
Notes to Financial Statements	22
Required Supplementary Information	
General Fund - Schedule of Revenues, Expenditures and Changes in Fund Balance - Budget and Actual	41
Note to Required Supplementary Information	42
Other Supplementary Information	
Nonmajor Governmental Funds	
Combining Balance Sheet	43
Combining Statement of Revenues, Expenditures and Changes in Fund Balances	44
General Fund	
Statement of Revenues, Expenditures and Changes in Fund Balance	45
REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*	47
SCHEDULE OF FINDINGS AND RESPONSES	49
MANAGEMENT LETTER	51

CITY OF GRAND MARAIS, MINNESOTA

ORGANIZATION
December 31, 2008

CITY COUNCIL

Mayor	Evelyn Larsen
Councilmember	Edward Bolstad
Councilmember	Kay Costello
Councilmember	Tim Kennedy
Councilmember	William Lenz

ADMINISTRATION

City Administrator	Michael J. Roth

FINANCIAL SECTION

Walker, Giroux, Hahne LTD

CERTIFIED PUBLIC ACCOUNTANTS & CONSULTANTS

P.O. Box 960 • 225 1st Street North, Suite 2400 • Virginia, Minnesota 55792
218-749-4880 • FAX 218-749-8528

INDEPENDENT AUDITOR'S REPORT

To the City Council
City of Grand Marais, Minnesota

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of City of Grand Marais, Minnesota, as of and for the year ended December 31, 2008, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of City of Grand Marais, Minnesota's, management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Grand Marais, Minnesota, as of December 31, 2008, and the respective changes in financial position, and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 2, 2009, on our consideration of the City of Grand Marais, Minnesota's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and important for assessing the results of our audit.

The management's discussion and analysis and budgetary comparison information, as listed in the table of contents, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Grand Marais, Minnesota's basic financial statements. The combining nonmajor and individual fund financial statements are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Walker, Hirsch + Nelson, Ltd

June 2, 2009

MANAGEMENT'S DISCUSSION AND ANALYSIS

CITY OF GRAND MARAIS, MINNESOTA

MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2008

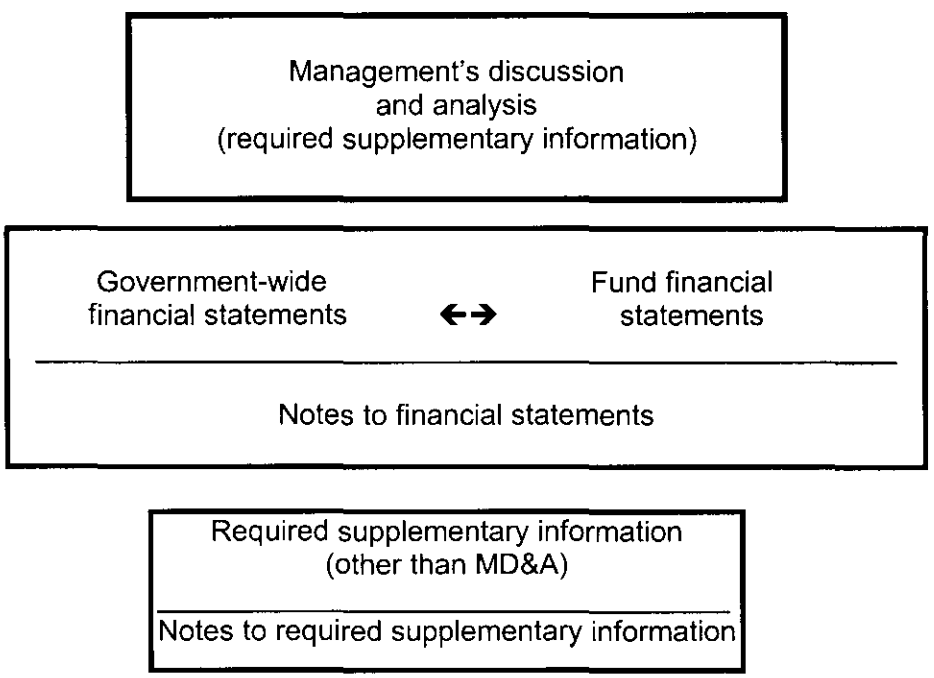
The City of Grand Marais, Minnesota's management's discussion and analysis provides an overview of the City's financial activities for the year ended December 31, 2008. Since this information is designed to focus on the current year's activities, resulting changes, and currently known facts, it should be read in conjunction with the City of Grand Marais, Minnesota's financial statements.

FINANCIAL HIGHLIGHTS

- Governmental activities' total net assets are $5,168,757, of which $2,349,588 is invested in capital assets, net of related debt.
- Business-type activities have total net assets of $11,454,144. Invested in capital assets, net of related debt represents $7,800,496 of the total.
- The City of Grand Marais's net assets increased by $320,226 for the year ended December 31, 2008. Of the increase, an increase of $246,394 was in the governmental activities' net assets and $73,832 represented the increase in business-type activities' net assets.
- The net cost of governmental activities was $842,038 for the current year. The net cost was funded by general revenues and other items totaling $1,088,432.
- Governmental funds' fund balances increased by $185,068.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the basic financial statements. The City of Grand Marais, Minnesota's basic financial statements consist of three parts: government-wide financial statements, fund financial statements, and notes to the financial statements. The management's discussion and analysis (this section) is required to accompany the basic financial statements, and therefore, is included as required supplementary information. The following chart demonstrates how the different pieces are interrelated.



There are two government-wide financial statements. The statement of net assets and the statement of activities provide information about the activities of the City as a whole and present a longer-term view of the City's finances. The fund financial statements explain how governmental activities were financed in the short term as well as what remains for future spending. Fund financial statements also report the City's operations in more detail than the government-wide statements by providing information about the City's most significant funds.

Government-wide Financial Statements

The statement of net assets and the statement of activities report information about the City, as a whole, and about its activities in a way that helps the reader determine whether the City's financial condition has improved or declined as a result of the year's activities. These statements include all assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These government-wide statements report the City's net assets and how they have changed. You can think of the City's net assets — the difference between assets and liabilities—as one way to measure the City's financial health or financial position. Increases or decreases in the City's net assets are one indicator of whether its financial health is improving or deteriorating. However, other nonfinancial factors, such as changes in the City's property tax base and state aid and the condition of City buildings also need to be considered in assessing the overall health of the City.

In the statement of net assets and the statement of activities, all activities are shown in the governmental activities and business-type activities:

- Governmental activities—Most of the City's basic services are reported here, including general government, public safety, streets, culture and recreation, and economic development. Property taxes and state and federal grants and aids finance most of these activities.

- Business-type activities—The City charges a fee to customers to help it cover all or most of the cost of services it provides. The City's liquor store, golf course, electric, water, and sewer services are reported here.

Fund Financial Statements

The fund financial statements provide detailed information about the significant funds—not the City as a whole. Some funds are required to be established by State law and by bond covenants. However, the City establishes some funds to help it control and manage money for a particular purpose or to show that it is meeting legal responsibilities for using certain taxes, grants, and other money. The City's two kinds of funds—governmental and proprietary—use different accounting methods.

- Governmental funds—Most of the City's basic services are reported in governmental funds, which focus on how money flows into and out of those funds and the balances left at year-end that are available for spending. These funds are reported using the modified accrual basis of accounting. This method measures cash and all other

financial assets that can be readily converted to cash. The governmental fund statements provide a detailed short-term view of the City's general government operations and the basic services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs. We describe the relationship (or differences) between governmental activities (reported in the Statement of Net Assets and the Statement of Activities) and governmental funds in a reconciliation statement following each governmental fund financial statement.

- Proprietary funds—When the City charges customers for the services it provides—whether to outside customers or to other units of the City—these services are generally reported in proprietary funds. Proprietary funds are reported in the same way that all activities are reported in the Statement of Net Assets and the Statement of Activities. In fact, the City's enterprise funds (a component of proprietary funds) are the same as the business-type activities we report in the government-wide statements but provide more detail and additional information, such as cash flows.

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

The City's combined net assets increased from $16,302,675 to $16,622,901. During 2008, both the governmental activities and the business-type activities had an increase in net assets. Our analysis below focuses on the net assets (Table 1) and changes in net assets (Table 2) of the City's governmental and business-type activities.

Table 1
Net Assets

	Governmental Activities		Business-Type Activities		Total Primary Government	
	2008	2007	2008	2007	2008	2007
Current and other assets	$ 3,496,162	$ 2,863,413	$ 4,452,305	$ 3,903,544	$ 7,948,467	$ 6,766,957
Capital assets	9,103,588	7,284,604	13,562,496	13,986,464	22,666,084	21,271,068
Total assets	12,599,750	10,148,017	18,014,801	17,890,008	30,614,551	28,038,025
Long-term debt outstanding	6,754,000	5,021,000	5,762,000	5,541,576	12,516,000	10,562,576
Other liabilities	676,993	204,654	798,657	968,120	1,475,650	1,172,774
Total liabilities	7,430,993	5,225,654	6,560,657	6,509,696	13,991,650	11,735,350
Net assets						
Invested in capital assets, net of debt	2,349,588	3,138,604	7,800,496	8,444,888	10,150,084	11,583,492
Restricted	-	-	987,700	942,478	987,700	942,478
Unrestricted	2,819,169	1,783,759	2,665,948	1,992,946	5,485,117	3,776,705
Total net assets	$ 5,168,757	$ 4,922,363	$11,454,144	$11,380,312	$16,622,901	$16,302,675

Net assets of the City's governmental activities increased by 5.01 percent ($5,168,757 compared to $4,922,363) in 2008.

Net assets of the City's business-type activities increased by .65 percent ($11,454,144 compared to $11,380,312) in 2008.

Table 2
Changes in Net Assets

	Governmental Activities		Business-Type Activities		Total Primary Government	
	2008	2007	2008	2007	2008	2007
Revenues						
Program revenues:						
Fees, fines, charges, and other	$ 924,981	$ 907,657	$4,995,450	$4,956,500	$5,920,431	$5,864,157
Operating grants and contributions	194,585	118,475	8,530	-	203,115	118,475
Capital grants and contributions	293,714	795,030	11,698	48,471	305,412	843,501
General revenues:						
Property taxes	628,168	679,576	27,787	-	655,955	679,576
Intergovernmental	205,071	269,287	-	-	205,071	269,287
Other general revenues	55,193	88,390	36,668	56,475	91,861	144,865
Total revenues	2,301,712	2,858,415	5,080,133	5,061,446	7,381,845	7,919,861
Program expenses:						
General government	351,365	356,941	-	-	351,365	356,941
Public safety	251,277	227,718	-	-	251,277	227,718
Streets	372,945	350,728	-	-	372,945	350,728
Culture and recreation	1,067,160	1,016,372	-	-	1,067,160	1,016,372
Interest	212,571	236,395	-	-	212,571	236,395
Liquor store	-	-	1,284,381	1,234,726	1,284,381	1,234,726
Golf course	-	-	169,211	180,668	169,211	180,668
Electric	-	-	2,427,592	2,595,477	2,427,592	2,595,477
Water	-	-	414,807	393,926	414,807	393,926
Sewer	-	-	510,310	509,078	510,310	509,078
Total program expenses	2,255,318	2,188,154	4,806,301	4,913,875	7,061,619	7,102,029
Excess (deficit) before special item and transfers	46,394	670,261	273,832	147,571	320,226	817,832
Special item	-	4,293	-	(80,712)	-	(76,419)
Transfers	200,000	(947,532)	(200,000)	947,532	-	-
Increase (decrease) in net assets	$ 246,394	$ (272,978)	$ 73,832	$1,014,391	$ 320,226	$ 741,413

Governmental Activities

The cost of all governmental activities this year was $2,255,318. As shown in the Statement of Activities, some of the cost was paid by those who directly benefited from the programs ($924,081) or by other governments and organizations that subsidized certain programs with grants and contributions ($488,299). Our taxpayers financed $628,168 of the cost through property taxes.

Table 3 presents the cost of each of the City's five largest programs, as well as each program's net cost (total cost less revenues generated by the activities). The net cost shows the financial burden that was placed on the City's taxpayers by each of these programs.

Table 3
Governmental Activities

	Total Cost of Services		Net Cost (Revenue) of Services	
	2008	2007	2008	2007
Culture and recreation	$ 1,067,160	$ 1,016,372	$ 146,718	$ 107,224
Streets	372,945	350,728	199,231	147,251
General government	351,365	356,941	207,858	235,614
Public safety	251,277	227,718	198,133	175,347
Economic development	-	-	(122,473)	(534,839)
All others	212,571	236,395	212,571	236,395
Totals	$ 2,255,318	$ 2,188,154	$ 842,038	$ 366,992

Business-Type Activities

Revenues of the City's business-type activities were $5,080,133; expenses were $4,806,301 (see Table 2). There was a change in net assets of $73,832 during the year ended December 31, 2008. The factors driving these results include:

- Electric, water, and sewer utility fee rate increases.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

As the City completed the year, its governmental funds reported a combined fund balance of $2,543,591 which is an increase from last year's total of $2,358,523. Included in this year's total fund balance is a surplus of $844,133 in the City's general fund. The general fund had an increase of $242,069. The largest increase of $735,121 was in the Street/Utility Project Capital Projects Fund due to bond issuance. The largest decrease of $760,196 was in the Debt Service Fund due to the payoff of the 2000 GO Improvement Bonds.

GENERAL FUND BUDGETARY HIGHLIGHTS

Over the course of the year, the City did not revise the general fund budget. The actual charges to appropriations (expenditures) were $138,111 below the final budget amounts. Resources available for appropriation were $76,033 above the final budgeted amounts. Although the City received less in property taxes than expected, more intergovernmental aids and charges for services were received.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

At the end of 2008, the City had $22,666,084 invested in a broad range of capital assets (net of accumulated depreciation), including land, construction in progress, buildings, improvements, infrastructure, machinery and equipment, and licensed vehicles. (See Table 4 below.) This amount represents a net increase (including additions and deductions) of $1,395,016 over last year.

Table 4
Capital Assets at Year-end
(Net of Depreciation)

	Governmental Activities		Business-type Activities		Totals	
	2008	2007	2008	2007	2008	2007
Land	$ 630,922	$ 630,922	$ 186,100	$ 186,100	$ 817,022	$ 817,022
Construction in progress	3,988,009	2,001,370	-	236,108	3,988,009	2,237,478
Buildings	1,142,738	1,186,387	4,694,053	4,871,954	5,836,791	6,058,341
Improvements	406,283	423,322	44,095	40,648	450,378	463,970
Infrastructure	2,537,037	2,645,595	8,229,912	8,162,832	10,766,949	10,808,427
Machinery and equipment	133,715	128,407	280,000	336,395	413,715	464,802
Licensed vehicles	264,884	268,601	128,336	152,427	393,220	421,028
Totals	$9,103,588	$7,284,604	$13,562,496	$13,986,464	$22,666,084	$21,271,068

This year's major additions were the EDA Cedar Grove Business Park and street/utility projects in the governmental activities, and a water main replacement on County Road 7 in the Water Enterprise Fund.

More detailed information about the City's capital assets is presented in Note 4 to the financial statements.

Debt

At year-end, the City had $12,516,000 in long-term debt outstanding versus $10,562,576 last year—as shown in Table 5.

Table 5
Outstanding Debt, at Year-end

	Governmental Activities		Business-type Activities		Totals	
	2008	2007	2008	2007	2008	2007
General obligation bonds (backed by the City)	$6,754,000	$5,021,000	$ -	$ -	$ 6,754,000	$ 5,021,000
Electric system revenue bonds	-	-	3,935,000	4,110,000	3,935,000	4,110,000
General obligation sewer revenue bonds	-	-	366,000	372,000	366,000	372,000
General obligation revenue notes	-	-	1,001,000	1,059,576	1,001,000	1,059,576
Water revenue note	-	-	460,000	-	460,000	-
Total	$6,754,000	$5,021,000	$5,762,000	$5,541,576	$12,516,000	$10,562,576

The State limits the amount of net debt that the City can issue to 3 percent of the market value of all taxable property in the City. The City's outstanding qualifying net debt of $0 is significantly below the $4,664,040 state-imposed limit.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS

The City's elected and appointed officials considered many factors when setting the 2009 budget and tax rates.

- The property tax levy increase will be held to 4.5%.
- The City's capital improvement plan anticipates no new projects in 2009 - 2010.
- Electric rates were increased 6% for 2009 in response to increasing fuel costs and wholesale rates.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the City Administrator, Michael J. Roth, City of Grand Marais, P.O. Box 600, Grand Marais, Minnesota 55604.

BASIC FINANCIAL STATEMENTS

CITY OF GRAND MARAIS, MINNESOTA

STATEMENT OF NET ASSETS
December 31, 2008

	Primary Government		
	Governmental Activities	Business-type Activities	Total
ASSETS			
Cash and cash equivalents	$ 3,146,646	$ 2,139,417	$ 5,286,063
Investments	-	135,000	135,000
Taxes receivable	55,894	-	55,894
Special assessments receivable	229,568	235,267	464,835
Accounts receivable	4,097	365,484	369,581
Internal balances	(91,399)	91,399	-
Loans receivable	30,385	-	30,385
Inventories	12,740	428,686	441,426
Prepaid items	45,491	47,928	93,419
Deferred debt issue costs	62,740	114,002	176,742
Temporarily restricted assets			
Cash and cash equivalents	-	895,122	895,122
Capital assets not being depreciated:			
Land	630,922	186,100	817,022
Construction in progress	3,988,009	-	3,988,009
Capital assets, net of accumulated depreciation:			
Buildings	1,142,738	4,694,053	5,836,791
Improvements	406,283	44,095	450,378
Infrastructure	2,537,037	8,229,912	10,766,949
Machinery and equipment	133,715	280,000	413,715
Licensed vehicles	264,884	128,336	393,220
TOTAL ASSETS	12,599,750	18,014,801	30,614,551
LIABILITIES			
Accounts payable	124,464	239,121	363,585
Salaries payable	72,733	94,505	167,238
Contracts payable	410,323	58,366	468,689
Customer deposits	-	13,580	13,580
Deferred revenues	-	338,773	338,773
Accrued interest payable	69,473	54,312	123,785
Noncurrent liabilities			
Due within one year	105,000	268,000	373,000
Due in more than one year	6,649,000	5,494,000	12,143,000
TOTAL LIABILITIES	7,430,993	6,560,657	13,991,650
NET ASSETS			
Invested in capital assets, net of related debt	2,349,588	7,800,496	10,150,084
Restricted for other purposes	-	987,700	987,700
Unrestricted	2,819,169	2,665,948	5,485,117
TOTAL NET ASSETS	$ 5,168,757	$ 11,454,144	$ 16,622,901

The accompanying notes are an integral part of these financial statements.

CITY OF GRAND MARAIS, MINNESOTA

STATEMENT OF ACTIVITIES
Year Ended December 31, 2008

Functions/Programs	Expenses	Program Revenues: Charges for Services	Program Revenues: Operating Grants and Contributions
PRIMARY GOVERNMENT			
Governmental Activities			
General government	$ 351,365	$ 119,325	$ 24,182
Public safety	251,277	35,698	17,446
Streets	372,945	-	-
Culture and recreation	1,067,160	767,485	152,957
Economic development	-	2,473	-
Interest on long-term debt	212,571	-	-
Total Governmental Activities	2,255,318	924,981	194,585
Business-type Activities			
Liquor Store	$ 1,284,381	$ 1,535,043	$ -
Golf Course	169,211	132,353	7,303
Electric	2,427,592	2,445,469	1,227
Water	414,807	349,683	-
Sewer	510,310	532,902	-
Total Business-type Activities	4,806,301	4,995,450	8,530
TOTAL PRIMARY GOVERNMENT	$ 7,061,619	$ 5,920,431	$ 203,115

General Revenues:
Taxes:
Property taxes, levied for general purposes
Property taxes, levied for specific purposes
Franchise taxes
Grants and contributions not restricted to specific programs
Unrestricted investment earnings
Gain on sale of capital assets
Transfers

Total General Revenues and Transfers

CHANGE IN NET ASSETS

NET ASSETS - JANUARY 1

NET ASSETS - DECEMBER 31

The accompanying notes are an integral part of these financial statements.

Capital Grants and Contributions	Net (Expense) Revenue and Changes in Net Assets Primary Government Governmental Activities	Business-type Activities	Total
$ -	$ (207,858)	$ -	$ (207,858)
-	(198,133)	-	(198,133)
173,714	(199,231)	-	(199,231)
-	(146,718)	-	(146,718)
120,000	122,473	-	122,473
-	(212,571)	-	(212,571)
293,714	(842,038)	-	(842,038)
$ -	-	250,662	250,662
-	-	(29,555)	(29,555)
-	-	19,104	19,104
11,698	-	(53,426)	(53,426)
-	-	22,592	22,592
11,698	-	209,377	209,377
$ 305,412	(842,038)	209,377	(632,661)
	508,592	-	508,592
	119,576	27,787	147,363
	6,335	-	6,335
	205,071	-	205,071
	37,683	36,668	74,351
	11,175	-	11,175
	200,000	(200,000)	-
	1,088,432	(135,545)	952,887
	246,394	73,832	320,226
	4,922,363	11,380,312	16,302,675
	$ 5,168,757	$ 11,454,144	$ 16,622,901

CITY OF GRAND MARAIS, MINNESOTA

BALANCE SHEET
GOVERNMENTAL FUNDS
December 31, 2008

	General Fund	Debt Service Fund	Street/Utility Project Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
ASSETS					
Cash and cash equivalents	$ 758,472	$ 284,860	$ 1,231,804	$ 871,510	$ 3,146,646
Taxes receivable	46,616	9,278	-	-	55,894
Special assessments receivable	-	229,568	-	-	229,568
Accounts receivable	2,615	-	-	1,482	4,097
Due from other funds	104,422	69,130	-	-	173,552
Loans receivables	-	-	-	30,385	30,385
Inventories	12,740	-	-	-	12,740
Prepaid items	40,929	-	-	4,562	45,491
TOTAL ASSETS	$ 965,794	$ 592,836	$ 1,231,804	$ 907,939	$ 3,698,373
LIABILITIES AND FUND BALANCES					
LIABILITIES					
Accounts payable	$ 44,460	$ -	$ -	$ 80,004	$ 124,464
Salaries payable	53,041	-	-	19,692	72,733
Contracts payable	-	-	410,323	-	410,323
Due to other funds	1,802	175,566	86,360	1,223	264,951
Deferred revenue	22,358	229,568	-	30,385	282,311
TOTAL LIABILITIES	121,661	405,134	496,683	131,304	1,154,782
FUND BALANCES					
Unreserved, designated	406,680	-	-	60,076	466,756
Unreserved, undesignated, reported in					
General Fund	437,453	-		-	437,453
Special revenue funds	-	-		410,542	410,542
Debt service fund	-	187,702		-	187,702
Capital projects funds	-	-	735,121	306,017	1,041,138
TOTAL FUND BALANCES	844,133	187,702	735,121	776,635	2,543,591
TOTAL LIABILITIES AND FUND BALANCES	$ 965,794	$ 592,836	$ 1,231,804	$ 907,939	$ 3,698,373

The accompanying notes are an integral part of these financial statements.

CITY OF GRAND MARAIS, MINNESOTA

RECONCILIATION OF THE BALANCE SHEET OF GOVERNMENTAL FUNDS TO THE STATEMENT OF NET ASSETS
December 31, 2008

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

TOTAL FUND BALANCES, GOVERNMENTAL FUNDS	$	2,543,591
Unamortized bond issuance costs are susceptible to full accrual on the government-wide statements.		62,740
Capital assets used in governmental activities are not current financial resources and therefore are not reported in the funds.		9,103,588
Deferred revenue in governmental funds is susceptible to full accrual on the government-wide statements.		282,311
Interest payable on long-term debt is susceptible to full accrual on the government-wide statements.		(69,473)
Long-term liabilities, including bonds payable are not due and payable in the current period and therefore not reported in the governmental funds.		(6,754,000)
NET ASSETS OF GOVERNMENTAL ACTIVITIES	$	5,168,757

The accompanying notes are an integral part of these financial statements.

CITY OF GRAND MARAIS, MINNESOTA

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
Year Ended December 31, 2008

	General Fund	Debt Service Fund	Street/Utility Project Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
REVENUES					
Taxes					
Property	$ 544,671	$ 119,576	$ -	$ -	$ 664,247
Franchise	-	-	-	6,335	6,335
Special assessments	13,232	206,121	-	120,000	339,353
Licenses and permits	80,515	-	-	-	80,515
Intergovernmental	268,012	-	-	101,319	369,331
Charges for services	818,404	-	-	20,551	838,955
Fines	1,552	-	-	-	1,552
Gifts and contributions	18,613	-	-	11,712	30,325
Interest	10,386	14,070	1,169	12,058	37,683
Miscellaneous	3,960	-	-	5,769	9,729
TOTAL REVENUES	1,759,345	339,767	1,169	277,744	2,378,025
EXPENDITURES					
Current					
General government	349,817	-	-	-	349,817
Public safety	241,610	-	-	-	241,610
Streets	261,989	-	-	-	261,989
Culture and recreation	752,351	-	-	269,327	1,021,678
Economic development	-	-	-	25,000	25,000
Debt service					
Principal	-	962,000	-	-	962,000
Interest and other charges	-	137,963	-	59,945	197,908
Bond issuance costs	-	-	52,492	-	52,492
Capital outlay					
Streets	-	-	1,908,556	-	1,908,556
Economic development	-	-	-	78,082	78,082
TOTAL EXPENDITURES	1,605,767	1,099,963	1,961,048	432,354	5,099,132
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	153,578	(760,196)	(1,959,879)	(154,610)	(2,721,107)
OTHER FINANCING SOURCES (USES)					
Transfers in	200,000	-	-	122,684	322,684
Transfers out	(122,684)	-	-	-	(122,684)
Bonds issued	-	-	2,695,000	-	2,695,000
Sale of capital assets	11,175	-	-	-	11,175
TOTAL OTHER FINANCING SOURCES (USES)	88,491	-	2,695,000	122,684	2,906,175
NET CHANGE IN FUND BALANCES	242,069	(760,196)	735,121	(31,926)	185,068
FUND BALANCES - JANUARY 1	602,064	947,898	-	808,561	2,358,523
FUND BALANCES - DECEMBER 31	$ 844,133	$ 187,702	$ 735,121	$ 776,635	$ 2,543,591

The accompanying notes are an integral part of these financial statements.

CITY OF GRAND MARAIS, MINNESOTA

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
Year Ended December 31, 2008

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

NET CHANGE IN FUND BALANCES - TOTAL GOVERNMENTAL FUNDS		$ 185,068
Governmental funds report outlays for capital assets as expenditures; however, in the statement of activities, the cost of those assets is depreciated over their estimated useful lives.		
Expenditures for capital assets	2,054,144	
Less current year depreciation	(235,160)	
Net capital assets		1,818,984
Capital assets were contributed to the Water and Sewer Enterprise Funds.		
Some revenues reported in the statement of activities do not require the use of current financial resources and therefore are not reported as revenues in governmental funds.		
Change in deferred revenue - delinquent property taxes	(36,079)	
Change in deferred revenue - special assessments receivable	(45,638)	
Change in deferred revenue - loans receivable	19,231	
		(62,486)
Debt issued provides current financial resources to governmental funds, but issuing debt increases long-term liabilities in the statement of net assets. Repayment of debt principal is an expenditure in the governmental funds, but the repayment reduced long-term liabilites in the statement of net assets.		
Debt issued	(2,695,000)	
Principal repaid	962,000	
		(1,733,000)
Governmental funds report bond discounts and issuance costs as expenditures; however, in the statement of activities, these costs are amortized over the life of the corresponding debt.		41,791
Some expenses reported in the statement of activities do not require the use of current financial resources and these are not reported as expenditures in governmental funds.		
Change in accrued interest payable on long-term debt		(3,963)
CHANGE IN NET ASSETS OF GOVERNMENTAL ACTIVITIES		$ 246,394

The accompanying notes are an integral part of these financial statements.

CITY OF GRAND MARAIS, MINNESOTA

STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
December 31, 2008

	Business-type Activities - Enterprise Funds					
	Liquor Store Enterprise Fund	Golf Course Enterprise Fund	Electric Enterprise Fund	Water Enterprise Fund	Sewer Enterprise Fund	Totals
ASSETS						
CURRENT ASSETS						
Cash and cash equivalents	$ 538,328	$ -	$ 648,591	$ 59,124	$ 893,374	$ 2,139,417
Investments	100,000	-	-	-	35,000	135,000
Accounts receivable	-	194	285,255	30,989	49,046	365,484
Due from other funds	23,373	-	-	218,215	45,513	287,101
Special assessments receivable	-	-	-	235,267	-	235,267
Inventories	130,425	7,334	274,458	16,056	413	428,686
Prepaid items	7,022	5,022	24,714	5,990	5,180	47,928
TOTAL CURRENT ASSETS	799,148	12,550	1,233,018	565,641	1,028,526	3,638,883
NONCURRENT ASSETS						
Restricted cash and cash equivalents						
Revenue bond covenant accounts	-	-	413,200	-	-	413,200
MPCA contract accounts	-	-	-	-	481,922	481,922
Total restricted cash and cash equivalents	-	-	413,200	-	481,922	895,122
Deferred debt issue costs	-	-	104,193	9,809	-	114,002
Capital assets						
Land	-	154,100	25,000	5,000	2,000	186,100
Buildings	24,248	89,466	2,759,697	1,815,454	2,516,190	7,205,055
Improvements	-	310,058	-	-	-	310,058
Infrastructure	-	-	3,307,936	4,454,416	2,769,512	10,531,864
Machinery and equipment	139,018	161,566	159,127	432,367	1,306,699	2,198,777
Licensed vehicles	-	500	279,808	33,754	72,485	386,547
Less accumulated depreciation	(122,450)	(439,331)	(1,363,661)	(2,146,185)	(3,184,278)	(7,255,905)
Total capital assets (net of accumulated depreciation)	40,816	276,359	5,167,907	4,594,806	3,482,608	13,562,496
TOTAL NONCURRENT ASSETS	40,816	276,359	5,685,300	4,604,615	3,964,530	14,571,620
TOTAL ASSETS	839,964	288,909	6,918,318	5,170,256	4,993,056	18,210,503
LIABILITIES						
CURRENT LIABILITIES						
Accounts payable	16,321	1,500	206,196	6,240	8,864	239,121
Salaries payable	19,223	19,475	23,277	10,631	21,899	94,505
Contracts payable	-	-	-	58,366	-	58,366
Accrued interest payable	-	-	28,664	9,178	16,470	54,312
Due to other funds	-	23,373	63,330	68,953	40,046	195,702
Deferred revenue	-	-	338,773	-	-	338,773
Customer deposits payable	-	-	13,580	-	-	13,580
Bonds, notes, and loans payable - current	-	-	180,000	81,000	7,000	268,000
TOTAL CURRENT LIABILITIES	35,544	44,348	853,820	234,368	94,279	1,262,359
NONCURRENT LIABILITIES						
Bonds, notes and loans payable	-	-	3,755,000	1,380,000	359,000	5,494,000
TOTAL LIABILITIES	35,544	44,348	4,608,820	1,614,368	453,279	6,756,359
NET ASSETS						
Invested in capital assets, net of related debt	40,816	276,359	1,232,907	3,133,806	3,116,608	7,800,496
Restricted for other purposes	-	-	390,414	-	597,286	987,700
Unrestricted	763,604	(31,798)	686,177	422,082	825,883	2,665,948
TOTAL NET ASSETS	$ 804,420	$ 244,561	$ 2,309,498	$ 3,555,888	$ 4,539,777	$ 11,454,144

The accompanying notes are an integral part of these financial statements.

CITY OF GRAND MARAIS, MINNESOTA

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUNDS
Year Ended December 31, 2008

	Business-type Activities - Enterprise Funds					
	Liquor Store Enterprise Fund	Golf Course Enterprise Fund	Electric Enterprise Fund	Water Enterprise Fund	Sewer Enterprise Fund	Totals
REVENUES						
Charges for sales and services	$ 1,535,043	$ 132,353	$ 2,445,469	$ 349,683	$ 532,902	$ 4,995,450
OPERATING EXPENSES						
Cost of sales	1,039,567	13,262	1,442,704	-	-	2,495,533
Salaries	134,840	79,656	176,029	96,973	117,791	605,289
Employee benefits and payroll taxes	44,694	21,027	65,508	38,485	37,750	207,464
Advertising	6,165	3,618	-	-	-	9,783
Bad debts	419	-	-	-	-	419
Contract services	-	-	118,970	19,307	101,741	240,018
Facility fees	-	-	61,880	-	-	61,880
Insurance	5,687	6,191	24,036	4,031	3,543	43,488
Miscellaneous	20,109	4,759	28,819	5,161	4,997	63,845
Rent	22,000	-	800	800	800	24,400
Repairs and maintenance	2,973	3,055	38,133	16,418	11,290	71,869
Supplies	3,777	18,040	69,327	19,924	15,620	126,688
Telephone	593	1,092	1,545	2,391	668	6,289
Utilities	-	3,403	6,462	21,562	54,773	86,200
Depreciation	3,557	15,109	209,545	143,724	144,866	516,801
TOTAL OPERATING EXPENSES	1,284,381	169,212	2,243,758	368,776	493,839	4,559,966
OPERATING INCOME (LOSS)	250,662	(36,859)	201,711	(19,093)	39,063	435,484
NONOPERATING REVENUES (EXPENSES)						
Interest income	11,955	-	9,058	62	15,593	36,668
Special assessments	-	-	-	11,698	-	11,698
Property taxes	-	-	-	27,787	-	27,787
Grants and contributions	-	7,303	1,227	-	-	8,530
Interest expense	-	-	(183,834)	(46,031)	(16,470)	(246,335)
TOTAL NONOPERATING REVENUES (EXPENSES)	11,955	7,303	(173,549)	(6,484)	(877)	(161,652)
INCOME (LOSS) BEFORE TRANSFERS	262,617	(29,556)	28,162	(25,577)	38,186	273,832
Transfers out	(200,000)	-	-	-	-	(200,000)
CHANGE IN NET ASSETS	62,617	(29,556)	28,162	(25,577)	38,186	73,832
TOTAL NET ASSETS - JANUARY 1	741,803	274,117	2,281,336	3,581,465	4,501,591	11,380,312
TOTAL NET ASSETS - DECEMBER 31	$ 804,420	$ 244,561	$ 2,309,498	$ 3,555,888	$ 4,539,777	$ 11,454,144

The accompanying notes are an integral part of these financial statements.

CITY OF GRAND MARAIS, MINNESOTA

STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
Year Ended December 31, 2008

	Business-type Activities - Enterprise Funds					
	Liquor Store Enterprise Fund	Golf Course Enterprise Fund	Electric Enterprise Fund	Water Enterprise Fund	Sewer Enterprise Fund	Totals
CASH FLOWS FROM OPERATING ACTIVITIES						
Cash received from customers	$ 1,535,468	$ 132,284	$ 2,423,195	$ 349,329	$ 537,284	$ 4,977,560
Cash paid to suppliers	(1,178,795)	(70,140)	(1,851,127)	(124,478)	(238,793)	(3,463,333)
Cash paid to employees	(140,713)	(78,959)	(173,411)	(99,950)	(112,870)	(605,903)
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	215,960	(16,815)	398,657	124,901	185,621	908,324
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES						
Interfund financing of cash deficit	(22,754)	22,754	-	-	-	-
Transfers out to other funds	(200,000)	-	-	-	-	(200,000)
Advances to other funds	-	-	-	(251,665)	(31,931)	(283,596)
Advances from other funds	-	-	130,590	-	-	130,590
FEMA grant	-	7,303	1,227	-	-	8,530
NET CASH PROVIDED (USED) BY NONCAPITAL FINANCING ACTIVITIES	(222,754)	30,057	131,817	(251,665)	(31,931)	(344,476)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES						
Purchase or construction of fixed assets	(8,279)	(13,242)	-	(208,647)	-	(230,168)
Special assessments collected	-	-	-	21,649	-	21,649
Property taxes collected	-	-	-	27,787	-	27,787
Principal paid on long-term debt	-	-	(175,000)	(68,576)	(6,000)	(249,576)
Interest paid on long-term debt	-	-	(177,726)	(46,060)	(16,740)	(240,526)
Proceeds from water revenue note	-	-	-	470,000	-	470,000
Bond financing costs	-	-	-	(10,327)	-	(10,327)
NET CASH PROVIDED (USED) BY CAPITAL AND RELATED FINANCING ACTIVITIES	(8,279)	(13,242)	(352,726)	185,826	(22,740)	(211,161)
CASH FLOWS FROM INVESTING ACTIVITIES						
Purchase of investments	-	-	-	-	(35,000)	(35,000)
Interest on investments	11,955	-	9,058	62	15,593	36,668
NET CASH PROVIDED (USED) BY INVESTING ACTIVITIES	11,955	-	9,058	62	(19,407)	1,668
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(3,118)	-	186,806	59,124	111,543	354,355
CASH AND CASH EQUIVALENTS, JANUARY 1	541,446	-	874,985	-	1,263,753	2,680,184
CASH AND CASH EQUIVALENTS, DECEMBER 31	$ 538,328	$ -	$ 1,061,791	$ 59,124	$ 1,375,296	$ 3,034,539

The accompanying notes are an integral part of these financial statements.

CITY OF GRAND MARAIS, MINNESOTA

STATEMENT OF CASH FLOWS (CONTINUED)
PROPRIETARY FUNDS
Year Ended December 31, 2008

	Business-type Activities - Enterprise Funds					
	Liquor Store Enterprise Fund	Golf Course Enterprise Fund	Electric Enterprise Fund	Water Enterprise Fund	Sewer Enterprise Fund	Totals
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES						
Operating income (loss)	$ 250,662	$ (36,859)	$ 201,711	$ (19,093)	$ 39,063	$ 435,484
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:						
Depreciation	3,557	15,109	209,545	143,724	144,866	516,801
Changes in assets and liabilities						
(Increase) decrease in:						
Accounts receivable	425	(69)	(23,054)	(354)	4,382	(18,670)
Inventories	(5,751)	3,254	9,279	3,589	(289)	10,082
Prepaid items	(343)	(95)	(2,287)	(1,188)	(1,099)	(5,012)
Increase (decrease) in:						
Accounts payable	(26,717)	1,148	65	1,200	(6,223)	(30,527)
Salaries payable	(5,873)	697	2,618	(2,977)	4,921	(614)
Customer deposits	-	-	780	-	-	780
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	$ 215,960	$ (16,815)	$ 398,657	$ 124,901	$ 185,621	$ 908,324
NONCASH INVESTING, CAPITAL, AND FINANCING ACTIVITIES:						
Total capital asset additions	$ -	$ -	$ -	$ 71,312	$ -	$ 71,312
Accounts payable	-	-	-	195,701	-	195,701
Contracts payable	-	-	-	(58,366)	-	(58,366)
Cash paid for capital assets	$ -	$ -	$ -	$ 208,647	$ -	$ 208,647

The accompanying notes are an integral part of these financial statements.

NOTES TO FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The City of Grand Marais, Minnesota, a political subdivision of the State of Minnesota, is a statutory city, governed by an elected city council which consists of one mayor and four council-members.

The accounting policies of the City of Grand Marais, Minnesota, comply with Generally Accepted Accounting Principles (GAAP). The City applies all relevant Governmental Accounting Standards Board (GASB) pronouncements. Proprietary funds apply Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements, in which case, GASB prevails.

The accounting and reporting framework and the more significant accounting policies and practices are discussed in subsequent sections of this Note. The remainder of the Notes are organized to provide explanations, including required disclosures, of the City's financial activities for the year ended December 31, 2008.

A. Financial Reporting Entity

Accounting principles generally accepted in the United States of America require that the reporting entity include (1) the City, (2) organizations for which the City is financially accountable and (3) other organizations for which the nature and significance of their relationship with the City are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete. Based on the application of these criteria, there are no component units that should be included within the City's reporting entity.

B. Basic Financial Statements

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

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

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fund Financial Statements
The City segregates transactions related to certain functions or activities in separate funds in order to aid financial management and to demonstrate legal compliance. Separate statements are presented for governmental and proprietary activities. These statements present each major fund as a separate column on the fund financial statements; all non-major funds are aggregated and presented in a single column.

The description of the funds included in this report are as follows:

Governmental Funds

Governmental funds are those funds through which most governmental functions typically are financed. The measurement focus of governmental funds is on the sources, uses and balance of current financial resources. The City has presented the following governmental funds:

Major Governmental Funds:

The General Fund is the primary operating fund of the City and is used to account for all financial resources relating to the general government, except those required to be accounted for in another fund.

The Debt Service Fund is used to account for the accumulation of resources for, and the payment of, long-term debt principal, interest, and related costs.

The Street/Utility Capital Projects Fund is used to account for the construction of a street and utility project financed with bond proceeds.

Nonmajor Governmental Funds:

Special Revenue Funds, including the library, cable TV, and storefront renovation special revenue funds, are used to account for specific revenues that are legally restricted to expenditure for particular purposes.

Capital Projects Funds are used to account for the acquisition and construction of major capital assets other than those financed by proprietary funds.

Proprietary Funds

Proprietary funds are accounted for using the economic resources measurement focus and the accrual basis of accounting. The accounting objectives are determinations of net income, financial position and cash flow. All assets and liabilities are included on the Statement of Net Assets. The City has presented the following proprietary funds:

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Major Proprietary Funds:

The Liquor Store Enterprise Fund is used to account for the revenues generated from liquor sales.

The Golf Course Enterprise Fund is used to account for the revenues generated from golf course fees and sales.

The Electric Enterprise Fund is used to account for the revenues generated from the charges for distribution of electric services to the residential and commercial users of the City.

The Water Enterprise Fund is used to account for the revenues generated from the charges for distribution of water to the residential and commercial users of the City.

The Sewer Enterprise Fund is used to account for revenues generated from the charges for wastewater treatment services provided to the residential and commercial users of the City.

C. Measurement Focus and Basis of Accounting

Measurement focus refers to what is being measured; basis of accounting refers to when revenues and expenditures are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurement made, regardless of the measurement focus applied.

The government-wide statements and fund financial statements for proprietary funds are reported using the economic resources measurement focus and the accrual basis of accounting. The economic resources measurement focus means all assets and liabilities (whether current or non-current) are included on the statement of net assets and the operating statements present increases (revenues) and decreases (expenses) in net total assets. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized at the time the liability is incurred. Property taxes are generally recognized as revenues in the fiscal year for which they are levied. Grants and similar items are recognized when all requirements imposed by the provider have been met.

When both restricted and unrestricted resources are available for use, it is the City's policy to use restricted resources first, then unrestricted resources as they are needed. Depreciation expense can be specifically identified by program and is included in the direct expenses of each program. Interest on long-term debt is considered an indirect expense and is reported separately on the Statement of Activities. Generally, the effect of material interfund activity has been removed from the government-wide financial statements.

Governmental fund financial statements are reported using the current financial resources measurement focus and are accounted for using the modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues are recognized when susceptible to accrual (i.e., when they become both "measurable and available"). "Measurable" means the amount of the transaction can be determined and "available" means collectible within the

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

current period or soon enough thereafter to be used to pay liabilities of the current period. The City considers property taxes as available if they are collected within 60 days after year end. Grant revenue is recorded in the year in which the related expenditure is made. Other revenue is considered available if collected within one year. Expenditures are generally recorded when a liability is incurred. However, expenditures are recorded as prepaid for approved disbursements incurred in advance of the year in which the item or service is to be used and debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes, special assessments and loan repayments are considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the government.

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

D. Cash and Cash Equivalents

For the purpose of the statement of cash flows, cash and cash equivalents are defined as cash on hand, demand deposits and short-term investments purchased with a maturity of three months or less.

E. Assets, Liabilities and Fund Balances

1) Cash balances for all funds of the City are maintained on a combined basis and invested to the extent possible, in allowable short-term investments. All investments are stated at fair value.

2) The City maintains inventories in its general fund and enterprise funds. All inventories are valued at cost, on a first-in, first-out (FIFO) basis, and the cost of these inventories are recorded as expenditures when consumed rather than when purchased.

3) Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances".

   Legally authorized transfers are treated as interfund transfers and are included in the results of operations of both Governmental and Proprietary Funds.

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

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

5) Restricted assets are cash and cash equivalents whose use is limited by legal requirements such as a bond indenture. Restricted assets are reported only in the government-wide and proprietary fund financial statements.

6) Capital assets, which include land, construction in progress, buildings, improvements, infrastructure, machinery and equipment, and licensed vehicles are reported in the applicable governmental or business-type activities columns in the government-wide financial statements and in the proprietary fund financial statements.

   Capital assets are capitalized at historical cost, or estimated historical cost for assets where actual historical cost is not available. Donated assets are recorded as capital assets at their estimated fair value at the date of donation. The City elected not to report general infrastructure assets acquired prior to January 1, 2004, therefore, general infrastructure assets include only those acquired subsequent to January 1, 2004. The City maintains a threshold level of $2,500 or more for capitalizing land, buildings, improvements, infrastructure, machinery and equipment, and licensed vehicles. The cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives is not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets of business-type activities is included as part of the capitalized value of the assets constructed.

   Capital assets are depreciated using the straight-line method over their estimated useful lives. When assets are no longer needed by the City, such assets are either disposed of if it is determined there is no value, or sold for an immaterial amount. Useful lives vary from 20 to 50 years for improvements, buildings and infrastructure, and 4 to 30 years for machinery and equipment, and licensed vehicles. Land and construction in progress are not being depreciated.

7) Delinquent property taxes receivable, less any delinquent taxes that are to be received within 60 days, are recorded as a deferred revenue in the fund financial statements because they are not available to finance the current year operations of the City. Deferred revenue reported in the debt service fund represents special assessments receivable and in the Storefront Renovation Special Revenue Fund represents loans receivable.

8) In the government-wide financial statements and proprietary fund type financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type statement of net assets. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs, if material, are reported as deferred charges and amortized over the term of the related debt. The long-term debt consists primarily of general obligation improvement and revenue bonds and revenue notes.

   Long-term debt for governmental funds is not reported as a liability in the fund financial statements. Debt proceeds are reported as other financing sources and payment of principal and interest are reported as expenditures. Severance pay expenditures are recognized at retirement date.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

9) Net assets represent the difference between assets and liabilities in the government-wide financial statements. Net assets invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any long-term debt used to build or acquire the capital assets. Net assets are reported as restricted in the government-wide financial statement when there are limitations imposed on their use through external restrictions imposed by creditors, grantors, or laws or regulations of other governments.

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

F. Revenues and Expenditures

1) The property tax calendar in Minnesota follows the calendar year. Property tax levies are certified to the County Auditor in December of each year for collection from taxpayers in May and October of the following calendar year. In Minnesota, counties act as collection agents for all property taxes. The county spreads all levies over taxable property. Property taxes become a lien on the property the following January 1. The county generally remits taxes to the City at periodic intervals as they are collected. A portion of property taxes levied is paid by the State of Minnesota through various tax credits, which are included in revenue from state sources in the financial statements.

   Federal, state, and other revenues are reported under the legal and contractual requirements of the individual programs and are classified into essentially two types of revenues. In one, monies must be expended for the specific purpose before any amounts will be paid to the City; therefore, revenues are recognized based on expenditures recorded. In the other, monies are virtually unrestricted as to purpose of expenditure, and the resources are recorded as revenue at the time of receipt or earlier if they are available.

2) City employees earn vacation and sick leave based on years of service and union and employment contracts. Vacation leave may be accrued up to 1½ times the amount of actual vacation earned in the previous year. The liability for accrued vacation leave is recorded in the appropriate funds as an accrued liability. City employees accrue sick leave at the rate of 12 hours per month, up to a maximum of 960 hours. Unpaid sick leave does not vest and, therefore, is not accrued. Sick pay is expensed in the year taken.

NOTE 2 - CASH AND CASH EQUIVALENTS AND INVESTMENTS

The City's funds are combined (pooled) and invested to the extent available in various investments authorized by Minnesota statutes. This pool functions essentially as a demand account for all participating funds. Each fund's portion of this pool is displayed on the financial statements as "cash and cash equivalents, investments, and restricted assets". Several funds hold cash and investments separate from the cash and investment pool.

NOTE 2 - CASH AND CASH EQUIVALENTS AND INVESTMENTS (CONTINUED)

"Cash and cash equivalents, investments, and restricted assets" recorded are comprised of:

Cash	$ 5,728,947
Petty Cash	3,255
Certificates of Deposit	192,000
Investments	391,983
Total	$ 6,316,185

Deposits

Custodial Credit Risk – Deposits
Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the City will not be able to recover its deposits. The City's deposit policy requires that deposits in excess of FDIC insurance of $100,000 be protected by pledged securities.

The City maintains deposits at financial institutions authorized by the City Council. Minnesota statutes require that all City deposits be protected by insurance, surety bond or collateral. The market value of collateral pledged must equal 110 percent of the deposits not covered by insurance or bonds. State statutes authorize the types of securities which may be pledged as collateral and require that those securities be held in safekeeping by the City or in a financial institution other than that furnishing the collateral. At year-end, the carrying amount of the City's deposits, which includes certificates of deposit, was $5,920,947; the bank balance was $6,020,415. Of the bank balance, $777,457 was insured; of the remaining balance, $5,242,958 was collateralized with securities held by the pledging financial institution's agent in the City's name.

Investments

Custodial Credit Risk – Investments
For an investment, custodial credit risk is the risk that in the event of the failure of the counterparty, the City will not be able to recover the value of its investments or securities that are in the possession of an outside party. The City does not have a formal investment policy for custodial credit risk for investments. All investments purchased by the City are held by a third-party safekeeping agent appointed as custodian.

Credit Risk and Concentration of Credit Risk
According to the City's investment policy, the City is authorized and allowed by state statute to invest in qualified repurchase agreements, obligations of the U.S. government, obligations of the State of Minnesota or its municipalities, shares of certain investment companies, banker's acceptance notes, commercial paper issued by United States corporations rated A-1, P-1 and F-1, and guaranteed investment contracts.

NOTE 2 - CASH AND CASH EQUIVALENTS AND INVESTMENTS (CONTINUED)

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation. The City's investments in Federal National Mortgage Association notes and money market funds are not rated as to credit risk.

The City places no limit on the amount the City may invest in any one issuer and, as of December 31, 2008, had no investments in any issuer that exceeded five percent of net assets.

Interest Rate Risk
Interest rate risk is the risk that changes in interest rates of investments will adversely affect the fair value of an investment. The City does not have a formal investment policy that addresses interest rate risk.

The City manages its exposure to fair value losses arising from changing interest rates by purchasing investments with varying maturity dates. As of December 31, 2008, the City had the following investments:

		Maturity	
Investment Type	Fair Value	Less than 2 Years	More than 5 Years
Federal National Mortgage Association Notes	$ 135,000	$ -	$ 135,000
Minnesota Municipal Money Market Fund	214,493	214,493	-
Smith Barney Money Market Funds	42,407	42,407	-
Wells Fargo Money Market Funds	83	83	-
Total Investments	$ 391,983	$ 256,983	$ 135,000

The City utilizes the Minnesota Municipal Money Market (4M) Fund which is an external investment pool not registered with the Securities Exchange Commission (SEC) that follows the same regulatory rules of the SEC under rule 2a7. The fair value of the position in the pool is the same as the value of the pool shares.

NOTE 3 - NOTES RECEIVABLE

Several businesses have received loans from the City through the City's Storefront Loan Program. The unpaid principal balance on these loans as of December 31, 2008 was $30,385.

NOTE 4 - CAPITAL ASSETS

Capital asset activity for the year ended December 31, 2008, was as follows:

	Beginning Balance	Additions	Deletions	Ending Balance
Governmental activities				
Capital assets, not being depreciated:				
Land	$ 630,922	$ -	$ -	$ 630,922
Construction in progress	2,001,370	1,986,639	-	3,988,009
Total capital assets, not being depreciated	2,632,292	1,986,639	-	4,618,931
Capital assets, being depreciated:				
Buildings	4,319,190	26,930	-	4,346,120
Improvements	524,162	-	-	524,162
Infrastructure	4,504,162	3,807	-	4,507,969
Machinery and equipment	330,667	22,835	-	353,502
Licensed vehicles	404,526	13,933	(15,000)	403,459
Total capital assets, being depreciated	10,082,707	67,505	(15,000)	10,135,212
Less accumulated depreciation for:				
Buildings	(3,132,803)	(70,579)	-	(3,203,382)
Improvements	(100,840)	(17,039)	-	(117,879)
Infrastructure	(1,858,567)	(112,365)	-	(1,970,932)
Machinery and equipment	(202,260)	(17,527)	-	(219,787)
Licensed vehicles	(135,925)	(17,650)	15,000	(138,575)
Total accumulated depreciation	(5,430,395)	(235,160)	15,000	(5,650,555)
Total capital assets, being depreciated, net	4,652,312	(167,655)	-	4,484,657
Governmental activities capital assets, net	$ 7,284,604	$ 1,818,984	$ -	$ 9,103,588
Business-type activities				
Capital assets, not being depreciated:				
Land	$ 186,100	$ -	$ -	$ 186,100
Construction in progress	236,108	-	(236,108)	-
Total capital assets, not being depreciated	422,208	-	(236,108)	186,100
Capital assets, being depreciated:				
Buildings	7,205,055	-	-	7,205,055
Improvements	304,340	5,718	-	310,058
Infrastructure	10,224,443	307,421	-	10,531,864
Machinery and equipment	2,182,975	15,802	-	2,198,777
Licensed vehicles	386,547	-	-	386,547
Total capital assets, being depreciated	20,303,360	328,941	-	20,632,301
Less accumulated depreciation for:				
Buildings	(2,333,101)	(177,901)	-	(2,511,002)
Improvements	(263,692)	(2,271)	-	(265,963)
Infrastructure	(2,061,611)	(240,341)	-	(2,301,952)
Machinery and equipment	(1,846,580)	(72,197)	-	(1,918,777)
Licensed vehicles	(234,120)	(24,091)	-	(258,211)
Total accumulated depreciation	(6,739,104)	(516,801)	-	(7,255,905)
Total capital assets, being depreciated, net	13,564,256	(187,860)	-	13,376,396
Business-type activities capital assets, net	$ 13,986,464	$ (187,860)	$ (236,108)	$ 13,562,496

NOTE 4 - CAPITAL ASSETS (CONTINUED)

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

Governmental activities	
General government	$ 2,280
Public safety	23,594
Streets	119,931
Culture and recreation	89,355
Total depreciation expense-governmental activities	$ 235,160
Business-type activities	
Liquor Store	$ 3,557
Golf Course	15,109
Electric	209,545
Water	143,724
Sewer	144,866
Total depreciation expense-business-type activities	$ 516,801

NOTE 5 - RATE STABILIZATION PROVISION

A reserve for rate stabilization was established in 1996. The concept of rate stabilization is used by utilities to defer current revenues to future periods to reduce impacts of future rate increases to customers. The reserve, which is recorded as deferred revenue, will be used to offset future rate increases and maintain income stability in future periods. At December 31, 2008, the rate stabilization reserve was $338,773.

NOTE 6 - LONG-TERM LIABILITIES

The City issues general obligation bonds, improvement notes and revenue notes and bonds to finance the purchase of major capital items and the acquisition or construction of major capital facilities or improvements. Bonded indebtedness has also been entered into to advance refund general obligation bonds. General obligation bonds and notes have been issued for both governmental and business-type activities and are being repaid from the applicable resources. The water revenue note and interest is payable solely from the net revenues of the Water Enterprise Fund. The electric revenue bonds and interest are payable solely from the net revenues of the Electric Enterprise Fund.

NOTE 6 - LONG-TERM LIABILITIES (CONTINUED)

Components of long-term liabilities are as follows:

	Issue Date	Interest Rates	Original Issue	Final Maturity	Principal Outstanding
Governmental Activities					
General Obligation Bonds					
1980 Water and Sewer Revenue	05/28/1980	5.00%	$ 867,000	01/01/2010	$ 54,000
2004 Improvement	06/01/2004	3.40-5.10%	$ 710,000	02/01/2025	635,000
2005 Improvement	11/22/2005	3.50-4.60%	$ 895,000	02/01/2027	865,000
2005 Improvement Refunding	01/06/2005	3.40-4.60%	$ 875,000	02/01/2021	875,000
2007 Temporary Improvement	01/09/2007	3.65%	$ 1,630,000	01/09/2010	1,630,000
2008 Improvement	10/07/2008	3.25-4.50%	$ 2,695,000	02/01/2029	2,695,000
Governmental Activities Long-term Liabilities					6,754,000
Business-type activities					
Revenue Bonds					
2003 Electric System	05/01/2003	3.00-4.875%	$ 2,885,000	05/01/2023	2,340,000
2004 Electric System	09/01/2004	4.00-4.80%	$ 815,000	05/01/2023	720,000
2005 Electric System	06/21/2005	2.75-4.60%	$ 940,000	05/01/2024	875,000
Total Revenue Bonds					3,935,000
General Obligation Bonds					
2006 Sewer	09/15/2004	4.50%	$ 372,000	01/01/2036	366,000
General Obligation Notes					
1999 Water Revenue	04/27/1999	2.56%	$ 484,112	08/20/2019	308,000
2004 Improvement	07/21/2004	2.53%	$ 812,229	02/20/2024	693,000
Total General Obligation Notes					1,001,000
Revenue Note					
2008 Water	01/24/2008	3.59%	$ 470,000	12/01/2027	460,000
Business-type Activities Long-term Liabilities					5,762,000
Total Long-Term Liabilities					$ 12,516,000

Long-term liability activity for the year ended December 31, 2008 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Governmental activities					
Bonds Payable					
1980 GO Water and Sewer Revenue	$ 106,000	$ -	$ 52,000	$ 54,000	$ -
2000 GO Improvements	855,000	-	855,000	-	-
2004 GO Improvements	660,000	-	25,000	635,000	25,000
2005 GO Improvements	895,000	-	30,000	865,000	30,000
2005 GO Improvement Refunding	875,000	-	-	875,000	50,000
2007 GO Temporary Improvement	1,630,000	-	-	1,630,000	-
2008 GO Improvement	-	2,695,000	-	2,695,000	-
Governmental Activities - Long-term Liabilities	$ 5,021,000	$ 2,695,000	$ 962,000	$ 6,754,000	$ 105,000

NOTE 6 - LONG-TERM LIABILITIES (CONTINUED)

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Business-type Activities					
Bonds Payable					
2003 Electric System Revenue	$ 2,455,000	$ -	$ 115,000	$ 2,340,000	$ 120,000
2004 Electric System Revenue	755,000	-	35,000	720,000	35,000
2005 Electric System Revenue	900,000	-	25,000	875,000	25,000
2006 GO Sewer Revenue	372,000	-	6,000	366,000	7,000
Total Bonds Payable	4,482,000	-	181,000	4,301,000	187,000
Notes Payable					
1999 GO Water Revenue	332,000	-	24,000	308,000	25,000
2004 GO Improvement	727,576	-	34,576	693,000	36,000
2008 Water Revenue	-	470,000	10,000	460,000	20,000
Total Notes Payable	1,059,576	470,000	68,576	1,461,000	81,000
Business-type Activities - Long-term Liabilities	$ 5,541,576	$ 470,000	$ 249,576	$ 5,762,000	$ 268,000

Minimum annual principal and interest payments required to retire long-term liabilities are as follows:

Year Ending	Governmental Activities		Business-Type Activities		Government-wide	
December 31	Principal	Interest	Principal	Interest	Principal	Interest
2009	$ 105,000	$ 248,735	$ 268,000	$ 229,181	$ 373,000	$ 477,916
2010	2,074,000	232,781	274,000	221,843	2,348,000	454,624
2011	205,000	190,173	280,000	212,080	485,000	402,253
2012	210,000	182,734	292,000	201,747	502,000	384,481
2013	215,000	174,826	299,000	190,814	514,000	365,640
2014-2018	1,235,000	735,506	1,676,000	769,508	2,911,000	1,505,014
2019-2023	1,355,000	450,295	1,942,000	386,911	3,297,000	837,206
2024-2028	1,165,000	165,731	579,000	65,320	1,744,000	231,051
2029-2033	190,000	4,275	89,000	26,550	279,000	30,825
2034-2036	-	-	63,000	5,760	63,000	5,760
Total	$ 6,754,000	$ 2,385,056	$ 5,762,000	$ 2,309,714	$12,516,000	$ 4,694,770

NOTE 7 - INTERFUND BALANCES AND ACTIVITY

The composition of interfund balances as of December 31, 2008, is as follows:

Due to/from other funds –

Receivable Fund	Payable Fund	Amount
General	Cable TV	$ 1,223
General	Electric Enterprise	63,330
General	Water Enterprise	15,829
General	Sewer Enterprise	24,040
Debt Service	Water Enterprise	53,124
Debt Service	Sewer Enterprise	16,006
Liquor Store Enterprise	Golf Enterprise	23,373
Water Enterprise	General	813
Water Enterprise	Debt Service	174,222
Water Enterprise	Street/Utility Project Capital Projects	43,180
Sewer Enterprise	General	989
Sewer Enterprise	Debt Service	1,344
Sewer Enterprise	Street/Utility Project Capital Projects	43,180
		$ 460,653

The balances resulted from the time lag between the dates that (1) interfund goods and services are provided or reimbursable expenditures occur, (2) transactions are recorded in the accounting system, (3) payments between funds are made, and (4) the elimination of deficit cash balances.

Interfund transfers for the year ended December 31, 2008 consisted of the following:

	Transfers Out		
	General Fund	Liquor Store Enterprise Fund	Total
Transfers In			
General Fund	$ -	$ 200,000	$ 200,000
Nonmajor Funds			
Library Special Revenue Fund	119,434	-	119,434
Cable TV Special Revenue Fund	3,250	-	3,250
	$ 122,684	$ 200,000	$ 322,684

Transfers are used to: 1) move profits or excess cash from the Liquor Store Enterprise Fund to the General Fund, and 2) move the City's contribution to the City library and cable TV operations.

NOTE 8 - FUND EQUITY

The amounts reported as fund balances unreserved, designated on the Balance Sheet are comprised of the following:

General Fund	
Designated for:	
Street seal coat project	$ 70,965
Buildings	51,713
Insurance reserve	10,804
Street equipment	18,282
Street improvements	254,916
Total General Fund - Designated	$ 406,680
Library Special Revenue Fund	
Designated for library improvements	$ 60,076

The amounts reported as net assets restricted for other purposes on the statement of net assets is comprised of the following:

Electric Enterprise Fund	
Restricted for debt service	$ 390,414
Sewer Enterprise Fund	
Restricted for MPCA contract	$ 597,286

NOTE 9 - RISK MANAGEMENT

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets, errors and omissions; injuries to employees; and natural disasters. To cover these risks of loss, except for boiler and machinery risks, the City, as allowed under state statutes, joined the League of Minnesota Cities Insurance Trust, a public entity risk pool currently operating as a common risk management and insurance program for its member cities. The City pays annual premiums to the Trust for its insurance coverage and retains the risk for the deductible portions of the insurance. The League of Minnesota Cities Insurance Trust is self-sustaining through member premiums and reinsures through commercial companies for claims in excess of the limits set by the Trustees. The City carries commercial insurance for boiler and machinery risks. There were no significant increases or reductions in insurance from the previous year. Settled claims resulting from these risks have not exceeded insurance coverage in any of the past three fiscal years.

NOTE 10 - JOINTLY GOVERNED ORGANIZATION

Cook County/Grand Marais Joint Economic Development Authority
The City of Grand Marais and Cook County established, through special legislation, the Cook County/Grant Marais Joint Economic Development Authority to jointly increase the tax base and employment opportunities of the City and County through public support of private development efforts.

The Authority is governed by seven commissioners composed of three members appointed by the City and four members appointed by the County.

The Authority is currently developing lots to be sold in Cedar Grove Business Park. The City, in consideration for construction of street improvements, water and sewer extensions and curb and gutter on the platted roads in the Business Park, has entered into an agreement with the Authority whereby owners will be assessed $60,000 per platted lot, payable from the closing proceeds at the time of sale. The City expended $78,082 in 2008 and $1,775,573 in 2007 on infrastructure for this project.

On January 9, 2007, the City of Grand Marais issued $1,630,000 General Obligation Temporary Improvement Bonds to temporally finance the improvements. Interest is payable semi-annually and final payment of principal is due January 9, 2010.

NOTE 11 - JOINT VENTURE

Joint Recreation Board
The City entered into a joint powers agreement with Independent School District No. 166-Cook County and Cook County to build, manage, and maintain recreational facilities for the benefit of both residents and visitors to Cook County.

The Joint Recreation Board is governed by a nine-member board composed of three members from the City, three from the County, and three from the School District.

If the agreement is terminated, all real and personal property will be sold and any surplus money and property remaining after payment of all liabilities shall be returned to the parties in proportion to each party's total contribution over the three years prior to termination.

In 2008, the City did not contribute to the Joint Recreation Board. Complete financial information can be obtained from the Joint Recreation Board, Cook County Courthouse, 411 West Second Street, Grand Marais, MN 55604.

NOTE 12 - OTHER COMMITMENTS AND CONTINGENCIES

Grants

The City participates in grant programs, which are governed by various rules and regulations of the grantor agencies. Costs charged to the respective grant programs are subject to audit and adjustment by the grantor agencies; therefore, to the extent that the City has not complied with the rules and regulations governing the grants, refunds of any money received may be required and the collectibility of any related receivable at December 31, 2008, may be impaired. In the opinion of the City, there are no significant contingent liabilities relating to compliance with the rules and regulations governing the respective grants; therefore, no provision has been recorded in the accompanying financial statements for such contingencies.

Electric Utility Commitment

The Grand Marais Public Utilities Commission purchases power from Southern Minnesota Municipal Power Agency (SMMPA) under a power sales contract which extends to April 1, 2030. Under the terms of the contract, the Commission is obligated to buy all the electrical power and energy needed to operate the electric utilities through the term of the contract. The City of Grand Marais and SMMPA have entered into a quick-start capacity and energy purchase agreement in which SMMPA has agreed to purchase all of the energy and capacity of the Grand Marais generating plant. SMMPA will pay the Grand Marais Public Utilities $216,000 annually for the capacity of the plant. The term of this contract is the period commencing on the commercial operating date of the plant (February 18, 2004) and ending on the day of the contract year that includes the twentieth anniversary of the commercial operating date, unless earlier terminated or extended as provided in the agreement.

Construction Commitment

The City had outstanding construction projects as of December 31, 2008. The projects were evidenced by contractual commitments with contractors.

Project	Spent-to-Date	Commitment Remaining
Business Park	$ 1,677,269	$ 150,940
Utility and street reconstruction	$ 1,661,665	$ 382,521

NOTE 13 - FUNDS HELD BY OTHERS

The City of Grand Marais' Public Library is a beneficiary of a designated fund at Minnesota Community Foundation. Pursuant to the terms of the agreement establishing this fund, property contributed to Minnesota Community Foundation is held as a separate fund designated for the benefit of the City of Grand Marais' Public Library. The agreement provides that payments from the fund to the City of Grand Marais' Public Library can be made at the discretion of the Minnesota Community Foundation at such times and in such amounts and for such charitable purposes as the Minnesota Community Foundation deems appropriate. The fund is not included in the City of Grand Marais, Minnesota's financial statements, since all property in the fund was contributed to Minnesota Community Foundation to be held and administered for the benefit of the City of Grand Marais' Public Library. The market value of the fund assets was approximately $15,780 on December 31, 2008.

NOTE 14 - DEFINED BENEFIT PENSION PLANS - STATEWIDE

A. Plan Description

All full-time and certain part-time employees of the City of Grand Marais, Minnesota, are covered by defined benefit plans administered by the Public Employees Retirement Association of Minnesota (PERA). PERA administers the Public Employees Retirement Fund (PERF) which is a cost-sharing, multiple-employer retirement plan. This plan is established and administered in accordance with *Minnesota Statutes*, Chapter 353 and 356.

PERF members belong to either the Coordinated Plan or the Basic Plan. Coordinated Plan members are covered by Social Security and Basic Plan members are not. All new members must participate in the Coordinated Plan.

PERA provides retirement benefits as well as disability benefits to members, and benefits to survivors upon death of eligible members. Benefits are established by State Statute, and vest after three years of credited service. The defined retirement benefits are based on a member's highest average salary for any five successive years of allowable service, age, and years of credit at termination of service.

Two methods are used to compute benefits for PERF's Coordinated and Basic Plan members. The retiring member receives the higher of a step-rate benefit accrual formula (Method 1) or a level accrual formula (Method 2). Under Method 1, the annuity accrual rate for a Basic Plan member is 2.2 percent of average salary for each of the first 10 years of service and 2.7 percent for each remaining year. The annuity accrual rate for a Coordinated Plan member is 1.2 percent of average salary for each of the first 10 years and 1.7 percent for each remaining year. Under Method 2, the annuity accrual rate is 2.7 percent of average salary for Basic Plan members and 1.7 percent for Coordinated Plan members for each year of service. For PERF members hired prior to July 1, 1989 whose annuity is calculated using Method 1, a full annuity is available when age plus years of service equal 90. Normal retirement age is 65 for Basic and Coordinated members hired prior to July 1, 1989. Normal retirement age is the age for unreduced social security benefits capped at 66 for Coordinated members hired on or after July 1, 1989. A reduced retirement annuity is also available to eligible members seeking early retirement.

There are different types of annuities available to members upon retirement. A single-life annuity is a lifetime annuity that ceases upon the death of the retiree--no survivor annuity is payable. There are also various types of joint and survivor annuity options available which will be payable over joint lives. Members may also leave their contributions in the fund upon termination of public service in order to qualify for a deferred annuity at retirement age. Refunds of contributions are available at any time to members who leave public service, but before retirement benefits begin.

The benefit provisions stated in the previous paragraphs of this section are current provisions and apply to active plan participants. Vested, terminated employees who are entitled to benefits but are not receiving them yet are bound by the provisions in effect at the time they last terminated their public service.

NOTE 14 - DEFINED BENEFIT PENSION PLANS - STATEWIDE (CONTINUED)

PERA issues a publicly available financial report that includes financial statements and required supplementary information for PERF. That report may be obtained on the internet at www.mnpera.org, by writing to PERA at 60 Empire Drive #200, St. Paul, Minnesota, 55103-2088 or by calling 1-651-296-7460 or 1-800-652-9026.

B. Funding Policy

Minnesota Statutes Chapter 353 sets the rates for employer and employee contributions. These statutes are established and amended by the state legislature. The City makes annual contributions to the pension plans equal to the amount required by state statutes. PERF Basic Plan members and Coordinated Plan members were required to contribute 9.10% and 6.00%, respectively, of their annual covered salary in 2008. The City of Grand Marais is required to contribute the following percentages of annual covered payroll: 11.78% for Basic Plan PERF members and 6.50% for Coordinated Plan PERF members. Employer contribution rates for the Coordinated Plan will increase to 6.75%, effective January 1, 2009. The City's contributions to the Public Employees Retirement Fund for the years ending December 31, 2008, 2007, and 2006 were $73,401, $70,576, and $64,410, respectively. The City's contributions were equal to the contractually required contributions for each year as set by state statute.

NOTE 15 - DEFINED CONTRIBUTION PLAN

One council member of the City of Grand Marais, Minnesota is covered by the Public Employees Defined Contribution Plan (PEDCP), a multiple-employer deferred compensation plan administered by the Public Employees Retirement Association of Minnesota (PERA). The PEDCP is a tax qualified plan under Section 401(a) of the Internal Revenue Code and all contributions by or on behalf of employees are tax deferred until time of withdrawal.

Plan benefits depend solely on amounts contributed to the plan plus investment earnings, less administrative expenses. Minnesota Statutes, Chapter 353D.03, specifies plan provisions, including the employee and employer contribution rates for those qualified personnel who elect to participate. An eligible elected official who decides to participate contributes 5 percent of salary which is matched by the elected official's employer.

Employees who are paid for their services may elect to make member contributions in an amount not to exceed the employer share. Employer and employee contributions are combined and used to purchase shares in one or more of the seven accounts of the Minnesota Supplemental Investment Fund. For administering the plan, PERA receives 2 percent of employer contributions and twenty-five hundredths of one percent of the assets in each member's account annually.

NOTE 15 - DEFINED CONTRIBUTION PLAN (CONTINUED)

Total contributions made by the City of Grand Marais, Minnesota during fiscal year 2008 were:

Contribution Amount		Percentage of Covered Payroll		Required
Employee	Employer	Employee	Employer	Rates
$ 240	$ 240	5.0%	5.0%	5.0%

NOTE 16 - ENVIRONMENTAL SITE CLEAN UP OF FORMER ELECTRIC POWER PLANT

The City has identified the site of its former electric power plant as requiring remediation and clean up. Cleanup expenses of $176,793 were incurred during 2007. The estimated remaining costs of $200,000 are not recorded since the City is anticipating reimbursement from the Minnesota Petro Fund for a significant portion of the cost.

REQUIRED SUPPLEMENTARY INFORMATION

CITY OF GRAND MARAIS, MINNESOTA

GENERAL FUND
SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE - BUDGET AND ACTUAL
Year Ended December 31, 2008

	Budgeted Amounts		Actual Amounts, Budgetary Basis	Variance with Final Budget - Positive (Negative)
	Original	Final		
REVENUES				
Taxes				
Property	$ 586,958	$ 586,958	$ 544,671	$ (42,287)
Special assessments	2,066	2,066	13,232	11,166
Licenses and permits	76,750	76,750	80,515	3,765
Intergovernmental	189,524	189,524	268,012	78,488
Charges for services	806,014	806,014	818,404	12,390
Fines	3,500	3,500	1,552	(1,948)
Gifts and contributions	500	500	18,613	18,113
Interest	18,000	18,000	10,386	(7,614)
Miscellaneous	-	-	3,960	3,960
TOTAL REVENUES	1,683,312	1,683,312	1,759,345	76,033
EXPENDITURES				
Current				
General government	338,899	338,899	349,817	(10,918)
Public safety	215,959	215,959	241,610	(25,651)
Streets	353,014	353,014	261,989	91,025
Culture and recreation	836,006	836,006	752,351	83,655
TOTAL EXPENDITURES	1,743,878	1,743,878	1,605,767	138,111
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	(60,566)	(60,566)	153,578	214,144
OTHER FINANCING SOURCES (USES)				
Transfers in	200,000	200,000	200,000	-
Transfers out	(122,684)	(122,684)	(122,684)	-
Sale of capital assets	-	-	11,175	11,175
TOTAL OTHER FINANCING SOURCES (USES)	77,316	77,316	88,491	11,175
NET CHANGE IN FUND BALANCE	16,750	16,750	242,069	225,319
FUND BALANCE - JANUARY 1	602,064	602,064	602,064	-
FUND BALANCE - DECEMBER 31	$ 618,814	$ 618,814	$ 844,133	$ 225,319

NOTE TO REQUIRED SUPPLEMENTARY INFORMATION
December 31, 2008

NOTE 1 - BUDGETING

The City Clerk/Treasurer prepares a proposed budget for the City's funds on the same basis as the fund financial statements. The City Council adopts an annual budget for the fiscal year for the City's General Fund, Special Revenue Funds, and Debt Service Fund.

Legal budgetary control is at the fund account level; management control is exercised at line-item levels. Budget appropriations lapse at year end, if unexpended.

Budgeted amounts are as originally adopted or as amended by the City Council. The Schedule of Revenues, Expenditures and Changes in Fund Balance – Budget and Actual – General Fund presents a comparison of budgetary data to actual results.

OTHER SUPPLEMENTARY INFORMATION

NONMAJOR GOVERNMENTAL FUNDS

Special Revenue Funds

Special revenue funds are used to account for specific revenues that are legally restricted to expenditure for particular purposes.

The Library Special Revenue Fund is used to account for county grants, charges for services, and private donations that are restricted to the library operations.

The Cable TV Special Revenue Fund is used to account for revenues collected to fund the operation of a local channel to televise local events.

The Storefront Renovation Special Revenue Fund is used to account for collection and disbursement of revolving loan funds to area businesses for storefront renovation.

Capital Projects Funds

Capital projects funds are used to account for the acquisition and construction of major capital facilities other than those financed by proprietary funds.

The EDA Cedar Grove Business Park Capital Projects Fund is used to account for the construction of infrastructure and streets in the Cedar Grove Business Park.

CITY OF GRAND MARAIS, MINNESOTA

COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS
December 31, 2008

	Library Special Revenue Fund	Cable TV Special Revenue Fund	Storefront Renovation Special Revenue Fund	EDA Cedar Grove Business Park Capital Projects Fund	Total Nonmajor Governmental Funds
ASSETS					
Cash and cash equivalents	$ 405,832	$ -	$ 83,481	$ 382,197	$ 871,510
Accounts receivable	-	1,482	-	-	1,482
Loans receivables	-	-	30,385	-	30,385
Prepaid items	3,262	1,300	-	-	4,562
TOTAL ASSETS	$ 409,094	$ 2,782	$ 113,866	$ 382,197	$ 907,939
LIABILITIES AND FUND BALANCES					
LIABILITIES					
Accounts payable	$ 3,824	$ -	$ -	$ 76,180	$ 80,004
Salaries payable	19,692	-	-	-	19,692
Due to other funds	-	1,223	-	-	1,223
Deferred revenue	-	-	30,385	-	30,385
TOTAL LIABILITIES	23,516	1,223	30,385	76,180	131,304
FUND BALANCES					
Unreserved, designated	60,076	-	-	-	60,076
Unreserved, undesignated	325,502	1,559	83,481	306,017	716,559
TOTAL FUND BALANCES	385,578	1,559	83,481	306,017	776,635
TOTAL LIABILITIES AND FUND BALANCES	$ 409,094	$ 2,782	$ 113,866	$ 382,197	$ 907,939

CITY OF GRAND MARAIS, MINNESOTA

COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
NONMAJOR GOVERNMENTAL FUNDS
Year Ended December 31, 2008

	Library Special Revenue Fund	Cable TV Special Revenue Fund	Storefront Renovation Special Revenue Fund	EDA Cedar Grove Business Park Capital Projects Fund	Total Nonmajor Governmental Funds
REVENUES					
Taxes - franchise fee	$ -	$ 6,335	$ -	$ -	$ 6,335
Special assessments	-	-	-	120,000	120,000
Intergovernmental	101,319	-	-	-	101,319
Charges for services	18,078	-	-	2,473	20,551
Gifts and contributions	11,712	-	-	-	11,712
Interest	8,151	-	683	3,224	12,058
Miscellaneous	-	-	5,769	-	5,769
TOTAL REVENUES	139,260	6,335	6,452	125,697	277,744
EXPENDITURES					
Current					
Culture and recreation	256,877	12,450	-	-	269,327
Economic development	-	-	25,000	-	25,000
Debt Service					
Interest and other charges	-	-	-	59,945	59,945
Capital outlay					
Economic development	-	-	-	78,082	78,082
TOTAL EXPENDITURES	256,877	12,450	25,000	138,027	432,354
DEFICIENCY OF REVENUES OVER EXPENDITURES	(117,617)	(6,115)	(18,548)	(12,330)	(154,610)
OTHER FINANCING SOURCES					
Transfers in	119,434	3,250	-	-	122,684
NET CHANGE IN FUND BALANCES	1,817	(2,865)	(18,548)	(12,330)	(31,926)
FUND BALANCES - JANUARY 1	383,761	4,424	102,029	318,347	808,561
FUND BALANCES - DECEMBER 31	$ 385,578	$ 1,559	$ 83,481	$ 306,017	$ 776,635

CITY OF GRAND MARAIS, MINNESOTA

GENERAL FUND
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
Year Ended December 31, 2008

REVENUES	
Taxes	
General property	$ 544,671
Special Assessments	13,232
Licenses and permits	80,515
Intergovernmental	
Federal grants	
FEMA	43,595
State	
Local government aid	146,260
Market value credit	53,496
PERA aid	5,315
Fire aid	13,346
Other state aids	6,000
Total Intergovernmental	268,012
Charges for Services	
General government	
Rent	33,954
Miscellaneous	3,950
Public safety	
Fire protection contacts	31,093
Culture and recreation	
Park	612,233
Swimming pool	68,475
Boat harbors	68,699
Total Charges for Services	818,404
Fines	
Court fines	1,552
Gifts and Contributions	18,613
Interest	10,386
Miscellaneous	
Insurance recoveries	895
Other	3,065
Total Miscellaneous	3,960
TOTAL REVENUES	1,759,345

CITY OF GRAND MARAIS, MINNESOTA

GENERAL FUND
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
(CONTINUED)
Year Ended December 31, 2008

EXPENDITURES	
Current	
General Government	
Mayor and council	$ 27,908
City clerk	162,890
Elections	11,539
Independent audit	11,100
Legal	20,604
Planning and zoning	26,701
Buildings	61,408
Other	27,667
Total General Government	349,817
Public Safety	
Police	140,000
Fire	80,134
Fire capital outlay	13,927
Medical services	5,777
Animal control	1,772
Total Public Safety	241,610
Streets	
Maintenance	236,208
Street lighting	16,805
Capital outlay	8,976
Total Streets	261,989
Culture and Recreation	
Recreation	350,846
Recreation capital outlay	18,970
Swimming pool	279,488
Swimming pool capital outlay	7,895
Boat harbors	62,021
Boat harbors capital outlay	3,740
City parks	29,391
Total Culture and Recreation	752,351
TOTAL EXPENDITURES	1,605,767
EXCESS OF REVENUES OVER EXPENDITURES	153,578
OTHER FINANCING SOURCES (USES)	
Transfers in	200,000
Transfers out	(122,684)
Sale of capital assets	11,175
TOTAL OTHER FINANCING SOURCES (USES)	88,491
NET CHANGE IN FUND BALANCE	242,069
FUND BALANCE - JANUARY 1	602,064
FUND BALANCE - DECEMBER 31	$ 844,133

Walker, Giroux, Hahne LTD

CERTIFIED PUBLIC ACCOUNTANTS & CONSULTANTS

P.O. Box 960 • 225 1st Street North, Suite 2400 • Virginia, Minnesota 55792
218-749-4880 • FAX 218-749-8528

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

To the City Council
City of Grand Marais, Minnesota

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of City of Grand Marais, Minnesota, as of and for the year ended December 31, 2008, which collectively comprise the City of Grand Marais, Minnesota's basic financial statements and have issued our report thereon dated June 2, 2009. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered City of Grand Marais, Minnesota's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the City of Grand Marais, Minnesota's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the City's financial statements that is more than inconsequential will not be prevented or detected by the City's internal control. We consider the deficiencies described in the accompanying schedule of findings and responses as items 2008-1 and 2008-2 to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the City of Grand Marais, Minnesota's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider item 2008-2 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether City of Grand Marais, Minnesota's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We also conducted our audit in accordance with the provisions of the *Minnesota Legal Compliance Audit Guide for Local Government*, promulgated by the State Auditor pursuant to Minn. Stat. §6.65. Accordingly, the audit included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

The *Minnesota Legal Compliance Audit Guide for Local Government* covers six categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements and miscellaneous provisions. Our study included all of the listed categories. The results of our tests indicate that for the items tested, the City of Grand Marais, Minnesota, complied with the material terms and conditions of applicable legal provisions.

We noted certain matters that we reported to management of City of Grand Marais, Minnesota in a separate letter dated June 2, 2009, included under this cover.

City of Grand Marais, Minnesota's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. We did not audit City of Grand Marais, Minnesota's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the City Council, management, and the State of Minnesota, and is not intended to be and should not be used by anyone other than these specified parties.

Walker, Hirsch & Nelson, Ltd

June 2, 2009

SCHEDULE OF FINDINGS AND RESPONSES
Year Ended December 31, 2008

SIGNIFICANT DEFICIENCIES

2008-1. SEGREGATION OF DUTIES

Condition
Due to the limited number of personnel within the City's financial and utility offices, the segregation of accounting functions necessary to ensure adequate internal accounting control is not possible.

Criteria
The concentration of duties and responsibilities in a limited number of individuals is not desirable from an internal accounting control point of view.

Effect
Because of the weakness in segregation of duties, the City has not provided adequate internal control over its transactions.

Cause
This occurred because of staffing limitation caused by fiscal constraints.

Recommendations
Officials and management of the City should constantly be aware of this condition, attempt to segregate duties as much as possible and provide oversight to partially compensate for this deficiency.

Corrective Action Plan (CAP)

1. Explanation of Disagreement with Audit Finding
   There is no disagreement with the audit finding.

2. Actions Planned in Response to Finding
   The City Administrator will attempt to monitor transactions and structure the duties of office personnel to help ensure as much segregation of duties as possible within the City's staffing limitations and funding constraints.

3. Official Responsible for Ensuring CAP
   Michael J. Roth, City Administrator, is the official responsible for ensuring this plan.

4. Planned Completion Date for CAP
   The City's Administrator has been monitoring transactions and reviewing the duties of office personnel on an ongoing basis.

5. Plan to Monitor Completion of CAP
   The City Council recognizes the weakness in segregation of duties and has continually provided oversight to partially compensate for this deficiency.

2008-2. LACK OF CONTROL OVER FINANCIAL REPORTING PROCESS

Condition and Criteria
As part of the audit, management requested that the auditor prepare a draft of the City's financial statements, including the related notes to financial statements. Management reviewed, approved, and accepted responsibility for those financial statements prior to their issuance; however, management did not perform a detailed review of the financial statements.

Effect
The potential exists that a material misstatement of the financial statements could occur and not be prevented or detected by the City's internal control.

Cause
This occurred because of staffing limitations caused by fiscal constraints.

Recommendations
In order to provide controls over the financial statement preparation services at an appropriate level, we suggest management establish effective review policies and procedures.

Corrective Action Plan (CAP)

1. Explanation of Disagreement with Audit Finding
   There is no disagreement with the audit finding.

2. Actions Planned in Response to Finding
   Management has determined that the cost and training involved to review or prepare the City's financial statements exceeds the benefit that would result.

3. Official Responsible for Ensuring CAP
   None – see number 2 above.

4. Planned Completion Date for CAP
   None – see number 2 above.

5. Plan to Monitor Completion of CAP
   None – see number 2 above.

Walker, Giroux, Hahne LLP

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P.O. Box 960 • 225 1st Street North, Suite 2400 • Virginia, Minnesota 55792
218-749-4880 • FAX 218-749-8528

MANAGEMENT LETTER

To the City Council
City of Grand Marais, Minnesota

In planning and performing our audit of the financial statements of the City of Grand Marais, Minnesota, as of and for the year ended December 31, 2008, in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

However, during our audit we became aware of several matters that are opportunities for strengthening internal controls and operating efficiency. A separate report dated June 2, 2009, contains our report on significant deficiencies in the City's internal control. This letter does not affect our report dated June 2, 2009, on the financial statements of the City of Grand Marais, Minnesota.

We will review the status of these comments during our next audit engagement. We have already discussed these comments and suggestions with management, and we will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations. Our comments and suggestions are summarized as follows:

Internal Control and Operating Efficiency

Public Utilities merchandise and other miscellaneous sales must be recorded in the general ledger when billed. Currently, the sales are recorded when payment is received resulting in poor internal controls over receivables and revenue transactions. Also, an outstanding accounts receivable balance by customer report should be generated monthly and reconciled to the general ledger. Uncollectible accounts should be presented to the commission for approval prior to write-off.

This report is intended solely for the information and use of the City Council, management, and the State of Minnesota, and is not intended to be and should not be used by anyone other than these specified parties.

Walker, Giroux + Hahne, LLP

June 2, 2009