

CITY OF GRAND MARAIS, MINNESOTA

**FINANCIAL STATEMENTS AND
SUPPLEMENTARY INFORMATION
Year Ended December 31, 2012**

CITY OF GRAND MARAIS, MINNESOTA

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CITY OF GRAND MARAIS, MINNESOTA

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CITY OF GRAND MARAIS, MINNESOTA

**ORGANIZATION
December 31, 2012**

CITY COUNCIL

Mayor	Laurence Carlson
Councilmember	Tim Kennedy
Councilmember	William Lenz
Councilmember	Jan Sivertson
Councilmember	Robert Spry

ADMINISTRATION

City Administrator	Michael J. Roth
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FINANCIAL SECTION



CERTIFIED PUBLIC ACCOUNTANTS & CONSULTANTS

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INDEPENDENT AUDITOR'S REPORT

To the City Council
City of Grand Marais, Minnesota

Report on the Financial Statements

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 the City of Grand Marais, Minnesota, as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

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, 2012, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

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 listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The combining nonmajor and individual fund financial statements are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the combining nonmajor and individual fund financial statements are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated June 18, 2013, on our consideration of 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering City of Grand Marais, Minnesota's internal control over financial reporting and compliance.

Walker, Hironaka & Nelson, Ltd

Virginia, Minnesota
June 18, 2013

MANAGEMENT'S DISCUSSION AND ANALYSIS

CITY OF GRAND MARAIS, MINNESOTA

MANAGEMENT'S DISCUSSION AND ANALYSIS

December 31, 2012

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, 2012. 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 position is \$8,520,754, of which net investment in capital assets is \$4,073,281.
- Business-type activities total net position is \$13,818,386. Net investment in capital assets represents \$9,223,866 of the total.
- The City of Grand Marais's net position increased by \$783,368 for the year ended December 31, 2012. Of the increase, an increase of \$874,963 was reported in the governmental activities' net position and \$(91,595) represented the decrease in business-type activities' net position. The changes are primarily due to transfers.
- The net expense of governmental activities was \$767,071 for the current year. General revenues totaled \$978,036.
- Governmental funds' fund balances increased by \$163,220.

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. This report also contains required and other supplementary information in addition to the basic financial statements.

There are two government-wide financial statements. The statement of net position 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 position 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.

CITY OF GRAND MARAIS, MINNESOTA

MANAGEMENT'S DISCUSSION AND ANALYSIS

December 31, 2012

These government-wide statements report the City's net position and how they have changed. You can think of the City's net position — 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 position is 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 aids and the condition of City buildings also need to be considered in assessing the overall health of the City.

In the statement of net position 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 Position 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 Position 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.

CITY OF GRAND MARAIS, MINNESOTA

**MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2012**

Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

Other Information

In addition to the basic financial statements and accompanying notes, this report also presents the required supplementary information for budgetary comparison schedules. Combining and individual financial statements are presented immediately following the required supplementary information.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

As noted earlier, net position may serve over time as a useful indicator of a City's financial position. The following tables show that in the case of the City of Grand Marais, assets exceeded liabilities by \$22,339,140, an increase of \$783,368 from the prior year.

**Table 1
Net Assets**

	Governmental Activities		Business-Type Activities		Total Primary Government	
	2012	2011	2012	2011	2012	2011
Current and other assets	\$ 4,724,797	\$ 4,538,635	\$ 5,311,035	\$ 5,349,654	\$ 10,035,832	\$ 9,888,289
Capital assets	9,198,281	9,352,792	13,872,952	14,219,288	23,071,233	23,572,080
Total assets	<u>13,923,078</u>	<u>13,891,427</u>	<u>19,183,987</u>	<u>19,568,942</u>	<u>33,107,065</u>	<u>33,460,369</u>
Long-term debt outstanding	5,125,000	6,045,000	4,728,000	4,940,000	9,853,000	10,985,000
Other liabilities	277,324	200,636	637,601	718,961	914,925	919,597
Total liabilities	<u>5,402,324</u>	<u>6,245,636</u>	<u>5,365,601</u>	<u>5,658,961</u>	<u>10,767,925</u>	<u>11,904,597</u>
Net position						
Net investment in capital assets	4,073,281	3,307,792	9,223,866	9,279,288	13,297,147	12,587,080
Restricted	2,046,616	2,284,926	1,152,656	1,189,220	3,199,272	3,474,146
Unrestricted	2,400,857	2,053,073	3,441,864	3,441,473	5,842,721	5,494,546
Total net position	<u>\$ 8,520,754</u>	<u>\$ 7,645,791</u>	<u>\$ 13,818,386</u>	<u>\$ 13,909,981</u>	<u>\$ 22,339,140</u>	<u>\$ 21,555,772</u>

Net position of the City's governmental activities increased by 11.4 percent (\$8,520,754 compared to \$7,645,791) in 2012. Unrestricted net position—the part of net position that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation, or other legal requirements - increased from a \$2,053,073 surplus at December 31, 2011 to a \$2,400,857 surplus at the end of this year.

Net position of the City's business-type activities decreased by .7 percent (\$13,818,386 compared to \$13,909,981) in 2012.

CITY OF GRAND MARAIS, MINNESOTA

**MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2012**

**Table 2
Changes in Net Position**

	Governmental Activities		Business-Type Activities		Total Primary Government	
	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>
Revenues						
Program revenues:						
Fees, fines, charges, and other	\$ 1,222,294	\$ 1,175,197	\$ 5,418,001	\$ 5,374,263	\$ 6,640,295	\$ 6,549,460
Operating grants and contributions	197,443	122,573	5,000	-	202,443	122,573
Capital grants and contributions	194,496	1,760,423	30,883	-	225,379	1,760,423
General revenues:						
Property taxes	787,330	752,429	31,040	27,876	818,370	780,305
Grants and contributions not restricted to specific programs	104,575	119,432	-	-	104,575	119,432
Other general revenues (losses)	86,131	(21,502)	23,565	28,047	109,696	6,545
Total revenues	<u>2,592,269</u>	<u>3,908,552</u>	<u>5,508,489</u>	<u>5,430,186</u>	<u>8,100,758</u>	<u>9,338,738</u>
Program expenses:						
General government	408,482	344,623	-	-	408,482	344,623
Public safety	214,861	224,078	-	-	214,861	224,078
Streets	371,148	341,175	-	-	371,148	341,175
Culture and recreation	1,161,220	1,124,121	-	-	1,161,220	1,124,121
Interest	225,593	257,579	-	-	225,593	257,579
Liquor store	-	-	1,476,400	1,392,605	1,476,400	1,392,605
Golf course	-	-	164,416	156,318	164,416	156,318
Electric	-	-	2,410,099	2,462,576	2,410,099	2,462,576
Water	-	-	364,551	392,725	364,551	392,725
Sewer	-	-	520,620	545,707	520,620	545,707
Total program expenses	<u>2,381,304</u>	<u>2,291,576</u>	<u>4,936,086</u>	<u>4,949,931</u>	<u>7,317,390</u>	<u>7,241,507</u>
Excess before extraordinary item and transfers	210,965	1,616,976	572,403	480,255	783,368	2,097,231
Extraordinary item	-	7,417	-	-	-	7,417
Transfers	<u>663,998</u>	<u>(309,948)</u>	<u>(663,998)</u>	<u>309,948</u>	<u>-</u>	<u>-</u>
Change in net position	874,963	1,314,445	(91,595)	790,203	783,368	2,104,648
Net position, January 1	<u>7,645,791</u>	<u>6,331,346</u>	<u>13,909,981</u>	<u>13,119,778</u>	<u>21,555,772</u>	<u>19,451,124</u>
Net position, December 31	<u>\$ 8,520,754</u>	<u>\$ 7,645,791</u>	<u>\$ 13,818,386</u>	<u>\$ 13,909,981</u>	<u>\$ 22,339,140</u>	<u>\$ 21,555,772</u>

Governmental Activities

The most significant revenues of the governmental activities are fees, fines, charges, and other, comprised mostly of culture and recreation fees, totaling 47% of revenues. Capital grants and contributions, 8% of revenues, include the grants for major projects or equipment. Operating grants and contributions, 8% of revenues, are used for operating expenses. Unrestricted grants and contributions, 4% of revenues, are used to finance the general activities. Property taxes levied for general purposes amount to \$641,720 or 25% of revenues, an increase of \$26,195 over the prior year.

Culture and recreation expenses are the most significant (49%), followed by general government (17%), streets (16%), interest on long-term debt (9%), and public safety (9%).

CITY OF GRAND MARAIS, MINNESOTA

MANAGEMENT'S DISCUSSION AND ANALYSIS

December 31, 2012

Business-Type Activities

Revenues of the City's business-type activities were \$5,508,489; expenses were \$4,936,086 (see Table 2). Net assets decreased by \$91,595 during the year ended December 31, 2012. Factors driving these results include:

- Operations produced income of \$687,563 during the year ended December 31, 2012.
- All segments recorded operating income except for the golf course.
- Transfers out to other funds totaled \$714,755.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

Governmental Funds

The focus of the City's governmental funds is to provide information on near term inflows, outflows and balances of spendable resources. In particular, the unassigned fund balance may serve as a useful measure of the City's net resources available for spending at the end of the year.

At December 31, 2012, the City's governmental funds reported total ending fund balances of \$3,263,359, an increase of \$163,220 in comparison with the prior year. Restricted funds, which are considered unavailable for appropriation for general operations, made up nearly 28%, or \$900,104, of the total ending fund balance. The nonspendable fund balance of \$61,355 is also not available for general operations. The committed fund balance of \$20,078 represents revenues collected to fund the operation of a local TV channel. The City assigned \$620,748 to specific purposes.

At the end of the year, the general fund reported a fund balance of \$2,112,823, increasing \$318,594 from the prior year. General fund revenues were \$221,941 more than the prior years and expenditures increased by \$59,379. During the current year, the general fund transfers to other funds were \$375,772, which exceeded the prior year's transfers of \$151,706.

The debt service fund recorded a decrease in fund balance of \$157,819 primarily due to early extinguishment of the 2005 GO Improvement Refunding Bonds.

In other governmental funds, changes in fund balances were insignificant.

Proprietary Funds

The proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail.

The liquor store enterprise fund accounts for the operations of the City owned liquor store. In 2012, operating revenues increased by \$116,018, while the operating expenses increased by \$83,795 from the prior year. The liquor store operations produced an operating income of \$270,967 for this current year, which is an increase of \$32,223 from the prior year's operating income. A transfer out of \$200,000 was made during 2012 to the general fund, as in prior years.

CITY OF GRAND MARAIS, MINNESOTA

MANAGEMENT'S DISCUSSION AND ANALYSIS

December 31, 2012

The golf course enterprise fund accounts for the operations of the municipal golf course. In 2012, operating revenues increased by \$12,371 compared to the prior year. The golf course operations produced an operating loss of \$10,713. The City transferred in \$50,757 from the general fund and the County contributed \$5,000 to partially fund this loss. In addition, a grant of \$30,883 was received to fund the cost of solar panels. Net position increased by \$75,937 for the year.

The electric enterprise fund accounts for the electric operations of the City. In 2012, operating revenues decreased by \$50,721 compared to the prior year. Operating expenses also decreased from the prior year by \$41,168. The electric operations produced operating income of \$335,123 in 2012. Interest expense charged to the electric distribution was \$152,730. Net position increased by \$184,277.

The water enterprise fund accounts for the water operations of the City. In 2012, operating revenues decreased by \$2,634 compared to the prior year. Operating expenses decreased by \$25,609. In 2012, operating income of \$48,295 was recorded compared to an operating income of \$25,320 in the prior year. Interest expense charged to the water operations was \$37,753. A transfer to the debt service fund was made in the amount of \$45,315 during 2012. Net position increased by \$5,924.

The sewer enterprise fund accounts for the sewer operations of the City. In 2012, operating revenues decreased by \$31,296 compared to the prior year. Operating expenses decreased from the prior year by \$24,727. The sewer operations produced operating income of \$43,891 in 2012. Interest expense charged to the sewer operations was \$15,165. A transfer of \$465,210 was made to the debt service fund. These transactions resulted in a decrease of \$432,368 in net position in the current year.

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 \$118,837 below the final budget amounts. Negative variances occurred in economic development (\$90,000) and general government (\$47,893) expenditures. Resources available for appropriation were \$287,329 above the final budgeted amounts. Although the City received less in property taxes than expected, more intergovernmental aids and charges for services were received. Transfers out to other funds exceeded the amount budgeted by \$235,953.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

At the end of 2012, the City had \$23,071,233 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 3 below.) This amount represents a net decrease (including additions and deductions) of \$500,847 over last year.

CITY OF GRAND MARAIS, MINNESOTA

**MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2012**

**Table 3
Capital Assets at Year-end
(Net of Depreciation)**

	Governmental Activities		Business-type Activities		Totals	
	2012	2011	2012	2011	2012	2011
Land	\$ 630,922	\$ 630,922	\$ 186,100	\$ 186,100	\$ 817,022	\$ 817,022
Construction in progress	-	-	40,000	-	40,000	-
Buildings	2,344,133	2,447,135	4,343,576	4,539,881	6,687,709	6,987,016
Improvements	501,550	436,307	35,624	37,489	537,174	473,796
Infrastructure	5,194,240	5,342,810	9,045,443	9,208,099	14,239,683	14,550,909
Machinery and equipment	263,904	212,062	172,864	176,470	436,768	388,532
Licensed vehicles	263,532	283,556	49,345	71,249	312,877	354,805
Totals	\$ 9,198,281	\$ 9,352,792	\$ 13,872,952	\$ 14,219,288	\$ 23,071,233	\$ 23,572,080

This year's major additions were:

- 2001 reconditioned Pelican sweeper
- paving of 11th Avenue W.
- solar panels and a new mower at the golf course
- electric system upgrades
- water system upgrades

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 \$9,853,000 in long-term debt outstanding versus \$10,985,000 last year—as shown in Table 4.

**Table 4
Outstanding Debt, at Year-end**

	Governmental Activities		Business-type Activities		Totals	
	2012	2011	2012	2011	2012	2011
General obligation bonds (backed by the City)	\$ 5,125,000	\$ 6,045,000	\$ -	\$ -	\$ 5,125,000	\$ 6,045,000
Electric system revenue bonds	-	-	3,260,000	3,380,000	3,260,000	3,380,000
General obligation sewer revenue bonds	-	-	337,000	345,000	337,000	345,000
General obligation notes	-	-	751,000	815,000	751,000	815,000
Water revenue note	-	-	380,000	400,000	380,000	400,000
Total	\$ 5,125,000	\$ 6,045,000	\$ 4,728,000	\$ 4,940,000	\$ 9,853,000	\$ 10,985,000

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. As of December 31, 2012, the City had no outstanding qualifying net debt that applied to this \$4,438,026 state-imposed limit.

CITY OF GRAND MARAIS, MINNESOTA
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2012

Additional information on the City's long-term debt can be found in Note 6 to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The City's elected and appointed officials considered many factors when setting the 2013 budget, adopting the tax levy, and setting fees that will be charged for the business-type activities.

- The property tax levy increase will be held to 1.1%.
- Utility rates were held to a 0% increase.
- The City's capital plan for 2013 includes planning for a maintenance facility, electric power plant compliance with NESHAP and completion of the Community Connection Project in the recreation park.
- Employees were given a 1.5% cost of living adjustment raise.

REQUEST FOR INFORMATION

This financial report is designed to provide a general overview of the City's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to 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 POSITION
December 31, 2012**

	Primary Government		
	Governmental Activities	Business-type Activities	Total
ASSETS			
Cash and cash equivalents	\$ 3,237,641	\$ 3,329,959	\$ 6,567,600
Taxes receivable	122,226	-	122,226
Special assessments receivable	1,079,594	191,879	1,271,473
Accounts receivable	7,159	328,144	335,303
Internal balances	64,899	(64,899)	-
Loans receivable	71,959	-	71,959
Inventories	18,757	412,554	431,311
Prepaid items	42,598	38,152	80,750
Deferred debt issue costs	79,964	76,494	156,458
Temporarily restricted assets			
Cash and cash equivalents	-	998,752	998,752
Capital assets not being depreciated:			
Land	630,922	186,100	817,022
Construction in progress	-	40,000	40,000
Capital assets, net of accumulated depreciation:			
Buildings	2,344,133	4,343,576	6,687,709
Improvements	501,550	35,624	537,174
Infrastructure	5,194,240	9,045,443	14,239,683
Machinery and equipment	263,904	172,864	436,768
Licensed vehicles	263,532	49,345	312,877
TOTAL ASSETS	13,923,078	19,183,987	33,107,065
LIABILITIES			
Accounts payable	26,806	228,053	254,859
Salaries payable	66,862	82,628	149,490
Customer deposits	-	16,800	16,800
Unearned revenues	94,889	338,773	433,662
Accrued interest payable	88,767	50,261	139,028
Noncurrent liabilities			
Due within one year	210,000	334,000	544,000
Due in more than one year	4,915,000	4,394,000	9,309,000
Deferred amount on refunding	-	(78,914)	(78,914)
TOTAL LIABILITIES	5,402,324	5,365,601	10,767,925
NET POSITION			
Net investment in capital assets	4,073,281	9,223,866	13,297,147
Restricted for:			
Capital projects	13,059	-	13,059
Debt service	1,636,110	555,370	2,191,480
Library	252,263	-	252,263
Sewer equipment replacement	-	597,286	597,286
Storefront renovation	145,184	-	145,184
Unrestricted	2,400,857	3,441,864	5,842,721
TOTAL NET POSITION	\$ 8,520,754	\$ 13,818,386	\$ 22,339,140

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

CITY OF GRAND MARAIS, MINNESOTA

**STATEMENT OF ACTIVITIES
Year Ended December 31, 2012**

<u>Functions/Programs</u>	<u>Expenses</u>	<u>Charges for Services</u>	<u>Program Revenues Operating Grants and Contributions</u>
PRIMARY GOVERNMENT			
Governmental Activities			
General government	\$ 408,482	\$ 158,381	\$ 6,128
Public safety	214,861	49,457	1,270
Streets	371,148	-	-
Culture and recreation	1,161,220	1,014,456	190,045
Economic development	-	-	-
Interest on long-term debt	225,593	-	-
Total Governmental Activities	<u>2,381,304</u>	<u>1,222,294</u>	<u>197,443</u>
Business-type Activities			
Liquor Store	\$ 1,476,400	\$ 1,747,367	\$ -
Golf Course	164,416	153,703	5,000
Electric	2,410,099	2,592,492	-
Water	364,551	375,093	-
Sewer	520,620	549,346	-
Total Business-type Activities	<u>4,936,086</u>	<u>5,418,001</u>	<u>5,000</u>
TOTAL PRIMARY GOVERNMENT	<u>\$ 7,317,390</u>	<u>\$ 6,640,295</u>	<u>\$ 202,443</u>

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 POSITION

NET POSITION - JANUARY 1

NET POSITION - DECEMBER 31

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

Net (Expense) Revenue and Changes in Net Position
Primary Government

Capital Grants and Contributions	Governmental Activities	Business-type Activities	Total
\$ 7,561	\$ (236,412)	\$ -	\$ (236,412)
-	(164,134)	-	(164,134)
96,935	(274,213)	-	(274,213)
-	43,281	-	43,281
90,000	90,000	-	90,000
-	(225,593)	-	(225,593)
<u>194,496</u>	<u>(767,071)</u>	<u>-</u>	<u>(767,071)</u>
\$ -	-	270,967	270,967
30,883	-	25,170	25,170
-	-	182,393	182,393
-	-	10,542	10,542
-	-	28,726	28,726
<u>30,883</u>	<u>-</u>	<u>517,798</u>	<u>517,798</u>
<u>\$ 225,379</u>	<u>(767,071)</u>	<u>517,798</u>	<u>(249,273)</u>
	641,720	-	641,720
	141,181	31,040	172,221
	4,429	-	4,429
	104,575	-	104,575
	11,452	23,565	35,017
	74,679	-	74,679
	<u>663,998</u>	<u>(663,998)</u>	<u>-</u>
	<u>1,642,034</u>	<u>(609,393)</u>	<u>1,032,641</u>
	874,963	(91,595)	783,368
	<u>7,645,791</u>	<u>13,909,981</u>	<u>21,555,772</u>
	<u>\$ 8,520,754</u>	<u>\$ 13,818,386</u>	<u>\$ 22,339,140</u>

CITY OF GRAND MARAIS, MINNESOTA

**BALANCE SHEET
GOVERNMENTAL FUNDS
December 31, 2012**

	<u>General Fund</u>	<u>Debt Service Fund</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
ASSETS				
Cash and cash equivalents	\$ 2,087,790	\$ 536,765	\$ 613,086	\$ 3,237,641
Taxes receivable	102,475	19,751	-	122,226
Special assessments receivable	-	1,079,594	-	1,079,594
Accounts receivable	6,075	-	1,084	7,159
Due from other funds	64,899	-	-	64,899
Loans receivables	5,040	-	66,919	71,959
Inventories	18,757	-	-	18,757
Prepaid items	38,858	-	3,740	42,598
	<u>2,323,894</u>	<u>1,636,110</u>	<u>684,829</u>	<u>4,644,833</u>
TOTAL ASSETS	\$ 2,323,894	\$ 1,636,110	\$ 684,829	\$ 4,644,833
 LIABILITIES AND FUND BALANCES				
LIABILITIES				
Accounts payable	\$ 22,323	\$ -	\$ 4,483	\$ 26,806
Salaries payable	47,454	-	19,408	66,862
Deferred revenue	141,294	1,079,593	66,919	1,287,806
	<u>211,071</u>	<u>1,079,593</u>	<u>90,810</u>	<u>1,381,474</u>
TOTAL LIABILITIES	211,071	1,079,593	90,810	1,381,474
 FUND BALANCES				
Nonspendable	57,615	-	3,740	61,355
Restricted	-	556,517	343,587	900,104
Committed	-	-	20,078	20,078
Assigned	394,134	-	226,614	620,748
Unassigned	1,661,074	-	-	1,661,074
	<u>2,112,823</u>	<u>556,517</u>	<u>594,019</u>	<u>3,263,359</u>
TOTAL FUND BALANCES	2,112,823	556,517	594,019	3,263,359
 TOTAL LIABILITIES AND FUND BALANCES	 \$ 2,323,894	 \$ 1,636,110	 \$ 684,829	 \$ 4,644,833

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 POSITION**

December 31, 2012

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

TOTAL FUND BALANCES, GOVERNMENTAL FUNDS	\$ 3,263,359
Unamortized bond issuance costs are susceptible to full accrual on the government-wide statements.	79,964
Capital assets used in governmental activities are not current financial resources and therefore are not reported in the funds.	9,198,281
Deferred revenue in governmental funds is susceptible to full accrual on the government-wide statements.	1,192,917
Interest payable on long-term debt is susceptible to full accrual on the government-wide statements.	(88,767)
Long-term liabilities, including bonds payable are not due and payable in the current period and therefore not reported in the governmental funds.	<u>(5,125,000)</u>
NET POSITION OF GOVERNMENTAL ACTIVITIES	<u>\$ 8,520,754</u>

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, 2012

	<u>General Fund</u>	<u>Debt Service Fund</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
REVENUES				
Taxes				
Property	\$ 625,429	\$ 141,181	\$ -	\$ 766,610
Franchise	-	-	4,429	4,429
Special assessments	8,226	144,484	-	152,710
Licenses and permits	82,990	-	-	82,990
Intergovernmental	266,607	-	102,329	368,936
Charges for services	1,117,686	-	14,675	1,132,361
Fines	4,734	-	-	4,734
Gifts and contributions	9,120	-	20,894	30,014
Interest	7,257	1,106	3,089	11,452
Miscellaneous	29,696	-	18,778	48,474
	<u>2,151,745</u>	<u>286,771</u>	<u>164,194</u>	<u>2,602,710</u>
TOTAL REVENUES				
EXPENDITURES				
Current				
General government	415,082	-	-	415,082
Public safety	197,222	-	-	197,222
Streets	259,217	-	-	259,217
Culture and recreation	776,110	-	264,911	1,041,021
Economic development	90,000	-	21,853	111,853
Debt service				
Principal	-	920,000	-	920,000
Interest and other charges	-	235,115	-	235,115
	<u>1,737,631</u>	<u>1,155,115</u>	<u>286,764</u>	<u>3,179,510</u>
TOTAL EXPENDITURES				
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES				
	<u>414,114</u>	<u>(868,344)</u>	<u>(122,570)</u>	<u>(576,800)</u>
OTHER FINANCING SOURCES (USES)				
Transfers in	204,230	710,525	125,015	1,039,770
Transfers out	(375,772)	-	-	(375,772)
Sale of capital assets	76,022	-	-	76,022
	<u>(95,520)</u>	<u>710,525</u>	<u>125,015</u>	<u>740,020</u>
TOTAL OTHER FINANCING SOURCES (USES)				
NET CHANGE IN FUND BALANCES	318,594	(157,819)	2,445	163,220
FUND BALANCES - JANUARY 1	<u>1,794,229</u>	<u>714,336</u>	<u>591,574</u>	<u>3,100,139</u>
FUND BALANCES - DECEMBER 31	<u>\$ 2,112,823</u>	<u>\$ 556,517</u>	<u>\$ 594,019</u>	<u>\$ 3,263,359</u>

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, 2012**

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

NET CHANGE IN FUND BALANCES - TOTAL GOVERNMENTAL FUNDS		\$ 163,220
<p>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.</p>		
Expenditures for capital assets	203,184	
Less current year depreciation	<u>(356,352)</u>	
Net capital assets		(153,168)
<p>Governmental funds report the entire net sales price (proceeds) from sale of an asset as revenue because it provides current financial resources. In contrast, the statement of activities reports only the gain on the sale of the assets. Thus, the change in net assets differs from the change in fund balance by the cost of the asset sold.</p>		
		(1,343)
<p>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.</p>		
Change in deferred revenue - delinquent property taxes	16,516	
Change in deferred revenue - special assessments receivable	(82,858)	
Change in deferred revenue - loans receivable	<u>3,074</u>	
		(63,268)
<p>Repayment of debt principal is an expenditure in the governmental funds, but the repayment reduced long-term liabilities in the statement of net assets.</p>		
Principal repaid		920,000
<p>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.</p>		
		(4,708)
<p>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.</p>		
Change in accrued interest payable on long-term debt		<u>14,230</u>
CHANGE IN NET POSITION OF GOVERNMENTAL ACTIVITIES		<u><u>\$ 874,963</u></u>

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

CITY OF GRAND MARAIS, MINNESOTA

STATEMENT OF NET POSITION
 PROPRIETARY FUNDS
 December 31, 2012

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	\$ 882,702	\$ 19,712	\$ 1,377,375	\$ 272,031	\$ 778,139	\$ 3,329,959
Accounts receivable	-	-	251,208	33,988	42,948	328,144
Special assessments receivable	-	-	-	191,879	-	191,879
Inventories	130,489	5,731	257,319	18,739	276	412,554
Prepaid items	6,295	4,856	18,779	3,686	4,536	38,152
TOTAL CURRENT ASSETS	<u>1,019,486</u>	<u>30,299</u>	<u>1,904,681</u>	<u>520,323</u>	<u>825,899</u>	<u>4,300,688</u>
NONCURRENT ASSETS						
Restricted cash and cash equivalents						
Revenue bond covenant accounts	-	-	507,327	-	-	507,327
MPCA contract accounts	-	-	-	-	491,425	491,425
Total restricted cash and cash equivalents	-	-	507,327	-	491,425	998,752
Deferred debt issue costs	-	-	68,759	7,735	-	76,494
Capital assets						
Land	-	154,100	25,000	5,000	2,000	186,100
Construction in progress	-	-	40,000	-	-	40,000
Buildings	20,529	89,466	2,759,697	2,287,824	2,462,238	7,619,754
Improvements	-	310,058	-	-	-	310,058
Infrastructure	-	65,516	3,337,573	5,291,670	3,525,050	12,219,809
Machinery and equipment	144,722	167,226	148,376	400,193	1,106,663	1,967,180
Licensed vehicles	-	500	240,918	28,150	52,885	322,453
Less accumulated depreciation	(132,863)	(468,973)	(2,124,106)	(2,659,769)	(3,406,691)	(8,792,402)
Total capital assets (net of accumulated depreciation)	32,388	317,893	4,427,458	5,353,068	3,742,145	13,872,952
TOTAL NONCURRENT ASSETS	<u>32,388</u>	<u>317,893</u>	<u>5,003,544</u>	<u>5,360,803</u>	<u>4,233,570</u>	<u>14,948,198</u>
TOTAL ASSETS	<u>1,051,874</u>	<u>348,192</u>	<u>6,908,225</u>	<u>5,881,126</u>	<u>5,059,469</u>	<u>19,248,886</u>
LIABILITIES						
CURRENT LIABILITIES						
Accounts payable	38,843	1,283	174,233	3,552	10,142	228,053
Salaries payable	17,727	18,286	24,864	6,460	15,291	82,628
Accrued interest payable	-	-	28,184	6,912	15,165	50,261
Due to other funds	-	-	64,899	-	-	64,899
Deferred revenue	-	-	338,773	-	-	338,773
Customer deposits payable	-	-	16,800	-	-	16,800
Bonds, notes, and loans payable - current	-	-	240,000	86,000	8,000	334,000
TOTAL CURRENT LIABILITIES	<u>56,570</u>	<u>19,569</u>	<u>887,753</u>	<u>102,924</u>	<u>48,598</u>	<u>1,115,414</u>
NONCURRENT LIABILITIES						
Bonds, notes and loans payable, less current	-	-	3,020,000	1,045,000	329,000	4,394,000
Deferred amount on refunding	-	-	(78,914)	-	-	(78,914)
TOTAL NON CURRENT LIABILITIES	<u>-</u>	<u>-</u>	<u>2,941,086</u>	<u>1,045,000</u>	<u>329,000</u>	<u>4,315,086</u>
TOTAL LIABILITIES	<u>56,570</u>	<u>19,569</u>	<u>3,828,839</u>	<u>1,147,924</u>	<u>377,598</u>	<u>5,430,500</u>
NET POSITION						
Net investment in capital assets	32,388	317,893	1,246,372	4,222,068	3,405,145	9,223,866
Restricted for debt service	-	-	363,491	191,879	-	555,370
Restricted for sewer equipment replacement	-	-	-	-	597,286	597,286
Unrestricted	962,916	10,730	1,469,523	319,255	679,440	3,441,864
TOTAL NET POSITION	<u>\$ 995,304</u>	<u>\$ 328,623</u>	<u>\$ 3,079,386</u>	<u>\$ 4,733,202</u>	<u>\$ 4,681,871</u>	<u>\$ 13,818,386</u>

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 POSITION
 PROPRIETARY FUNDS
 Year Ended December 31, 2012

	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	\$ 1,747,367	\$ 153,703	\$ 2,592,492	\$ 375,093	\$ 549,346	\$ 5,418,001
OPERATING EXPENSES						
Cost of sales	1,167,764	19,304	1,541,592	-	-	2,728,660
Salaries	169,475	77,722	204,196	65,657	119,240	636,290
Employee benefits and payroll taxes	53,266	20,338	66,977	21,775	43,962	206,318
Advertising	6,112	2,042	-	-	-	8,154
Bad debts	-	-	1,934	218	299	2,451
Contract services	-	-	40,071	8,876	109,986	158,933
Facility fees	-	-	63,460	-	-	63,460
Insurance	3,524	4,366	30,239	2,782	2,954	43,865
Miscellaneous	25,405	3,245	14,540	4,090	4,346	51,626
Rent	38,400	-	9,000	4,500	4,500	56,400
Repairs and maintenance	4,434	6,652	40,346	3,061	15,974	70,467
Supplies	3,391	14,027	32,168	17,542	15,443	82,571
Telephone	729	770	986	2,075	577	5,137
Utilities	-	3,372	2,728	22,320	56,576	84,996
Depreciation	3,900	12,578	209,132	173,902	131,598	531,110
TOTAL OPERATING EXPENSES	<u>1,476,400</u>	<u>164,416</u>	<u>2,257,369</u>	<u>326,798</u>	<u>505,455</u>	<u>4,730,438</u>
OPERATING INCOME (LOSS)	<u>270,967</u>	<u>(10,713)</u>	<u>335,123</u>	<u>48,295</u>	<u>43,891</u>	<u>687,563</u>
NONOPERATING REVENUES (EXPENSES)						
Interest income	3,668	10	3,998	10,715	5,174	23,565
Property taxes	-	-	-	31,040	-	31,040
Grants and contributions	-	5,000	-	-	-	5,000
Interest expense	-	-	(152,730)	(37,753)	(15,165)	(205,648)
TOTAL NONOPERATING REVENUES (EXPENSES)	<u>3,668</u>	<u>5,010</u>	<u>(148,732)</u>	<u>4,002</u>	<u>(9,991)</u>	<u>(146,043)</u>
INCOME (LOSS) BEFORE CAPITAL GRANTS AND TRANSFERS	274,635	(5,703)	186,391	52,297	33,900	541,520
Capital grants	-	30,883	-	-	-	30,883
Transfers in	-	50,757	-	-	-	50,757
Transfers out	(200,000)	-	(2,114)	(46,373)	(466,268)	(714,755)
CHANGE IN NET POSITION	74,635	75,937	184,277	5,924	(432,368)	(91,595)
TOTAL NET POSITION - JANUARY 1	<u>920,669</u>	<u>252,686</u>	<u>2,895,109</u>	<u>4,727,278</u>	<u>5,114,239</u>	<u>13,909,981</u>
TOTAL NET POSITION - DECEMBER 31	<u>\$ 995,304</u>	<u>\$ 328,623</u>	<u>\$ 3,079,386</u>	<u>\$ 4,733,202</u>	<u>\$ 4,681,871</u>	<u>\$ 13,818,386</u>

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, 2012

	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	\$ 1,747,367	\$ 153,703	\$ 2,590,620	\$ 373,285	\$ 553,934	\$ 5,418,909
Cash paid to suppliers	(1,316,721)	(82,412)	(1,856,416)	(94,113)	(254,388)	(3,604,050)
Cash paid to employees	(172,353)	(78,408)	(200,513)	(62,157)	(119,835)	(633,266)
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	<u>258,293</u>	<u>(7,117)</u>	<u>533,691</u>	<u>217,015</u>	<u>179,711</u>	<u>1,181,593</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES						
Transfers in from other funds	-	50,757	-	-	-	50,757
Transfers out to other funds	(200,000)	-	(2,114)	(46,373)	(466,268)	(714,755)
Advances to other funds	-	-	(1,947)	(48,318)	(65,535)	(115,800)
Advances from other funds	-	-	23	235	-	258
County grants and contributions	-	5,000	-	-	-	5,000
NET CASH PROVIDED (USED) BY NONCAPITAL FINANCING ACTIVITIES	<u>(200,000)</u>	<u>55,757</u>	<u>(4,038)</u>	<u>(94,456)</u>	<u>(531,803)</u>	<u>(774,540)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES						
Purchase or construction of fixed assets	-	(83,436)	(60,181)	(34,087)	(7,070)	(184,774)
Special assessments collected	-	-	-	9,711	-	9,711
Property taxes collected	-	-	-	31,040	-	31,040
Principal paid on long-term debt	-	-	(200,000)	(84,000)	(8,000)	(292,000)
Irrevocable escrow deposit to defease refunded bonds	-	-	(1,927,096)	-	-	(1,927,096)
Interest paid on long-term debt	-	-	(108,428)	(37,882)	(15,525)	(161,835)
Capital grants	-	30,883	-	-	-	30,883
Proceeds from electric revenue refunding bonds	-	-	1,925,000	-	-	1,925,000
Bond financing costs	-	-	(23,980)	-	-	(23,980)
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	<u>-</u>	<u>(52,553)</u>	<u>(394,685)</u>	<u>(115,218)</u>	<u>(30,595)</u>	<u>(593,051)</u>
CASH FLOWS FROM INVESTING ACTIVITIES						
Sale of investments	-	-	-	-	100,000	100,000
Interest on investments	3,668	10	3,998	10,715	5,174	23,565
NET CASH PROVIDED BY INVESTING ACTIVITIES	<u>3,668</u>	<u>10</u>	<u>3,998</u>	<u>10,715</u>	<u>105,174</u>	<u>123,565</u>
NET INCREASE (DECREASE) IN CASH AND AND CASH EQUIVALENTS	61,961	(3,903)	138,966	18,056	(277,513)	(62,433)
CASH AND CASH EQUIVALENTS, JANUARY 1	<u>820,741</u>	<u>23,615</u>	<u>1,745,736</u>	<u>253,975</u>	<u>1,547,077</u>	<u>4,391,144</u>
CASH AND CASH EQUIVALENTS, DECEMBER 31	<u>\$ 882,702</u>	<u>\$ 19,712</u>	<u>\$ 1,884,702</u>	<u>\$ 272,031</u>	<u>\$ 1,269,564</u>	<u>\$ 4,328,711</u>

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, 2012

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)	\$ 270,967	\$ (10,713)	\$ 335,123	\$ 48,295	\$ 43,891	\$ 687,563
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities:						
Depreciation	3,900	12,578	209,132	173,902	131,598	531,110
Changes in assets and liabilities (Increase) decrease in:						
Accounts receivable	-	-	(972)	(1,808)	4,588	1,808
Inventories	(11,573)	(1,331)	5,436	(1,885)	58	(9,295)
Prepaid items	(4,909)	(4,175)	(10,723)	(2,479)	(2,984)	(25,270)
Increase (decrease) in:						
Accounts payable	2,786	(2,790)	(7,088)	(2,510)	3,155	(6,447)
Salaries payable	(2,878)	(686)	3,683	3,500	(595)	3,024
Customer deposits	-	-	(900)	-	-	(900)
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	<u>\$ 258,293</u>	<u>\$ (7,117)</u>	<u>\$ 533,691</u>	<u>\$ 217,015</u>	<u>\$ 179,711</u>	<u>\$ 1,181,593</u>
RECONCILIATION OF CASH AND CASH EQUIVALENTS TO THE STATEMENT OF NET POSITION - PROPRIETARY FUNDS						
Cash and cash equivalents	\$ 882,702	\$ 19,712	\$ 1,377,375	\$ 272,031	\$ 778,139	\$ 3,329,959
Restricted cash and cash equivalents:						
Revenue bond covenant accounts	-	-	507,327	-	-	507,327
MPCA contract accounts	-	-	-	-	491,425	491,425
CASH AND CASH EQUIVALENTS, DECEMBER 31	<u>\$ 882,702</u>	<u>\$ 19,712</u>	<u>\$ 1,884,702</u>	<u>\$ 272,031</u>	<u>\$ 1,269,564</u>	<u>\$ 4,328,711</u>

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

NOTES TO FINANCIAL STATEMENTS

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

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 councilmembers.

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, 2012.

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 position and the statement of activities) report information on all of the activities of the primary government. 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.

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 fund 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:

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 used to account for and report all financial resources not accounted for in another fund.

The Debt Service Fund is used to account for and report financial resources that are restricted, committed, or assigned to expenditure for principal and interest.

Nonmajor Governmental Funds:

Special Revenue Funds are used to account for and report the proceeds of specific revenue sources that are restricted or committed to expenditure for specified purposes other than debt service or capital projects.

Capital Projects Funds are used to account for and report financial resources that are restricted, committed, or assigned to expenditure for capital outlays, including the acquisition or construction of capital facilities and other capital assets. Capital projects funds exclude those types of capital-related outflows 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 Position. The City has presented the following proprietary funds:

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.

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 position and the operating statements present increases (revenues) and decreases (expenses) in net position. 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 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.

CITY OF GRAND MARAIS, MINNESOTA

**NOTES TO FINANCIAL STATEMENTS
December 31, 2012**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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) Receivables from and payables to external parties are reported separately and are not offset in the proprietary fund financial statements and business-type activities of the government-wide financial statements, unless a right of offset exists.
- 3) 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.
- 4) Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances". Outstanding balances between funds are reported as "due to/from other funds".

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

- 5) 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.
- 6) Restricted assets are cash and cash equivalents and investments 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.
- 7) 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.

CITY OF GRAND MARAIS, MINNESOTA

**NOTES TO FINANCIAL STATEMENTS
December 31, 2012**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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.

- 8) Government-wide financial statements report unearned revenue in connection with resources that have been received, but not yet earned. Governmental funds defer revenue in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period and resources that have been received, but not yet earned.

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.

- 9) 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 position. 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.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures. Severance pay expenditures are recognized at retirement date.

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

10) Net position represents the difference between assets and liabilities in the government-wide financial statements. Net investment in capital assets 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 position is 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, proprietary fund equity is classified the same as in the government-wide statements. Fund balances of the governmental funds are classified as follows:

Nonspendable—amounts that cannot be spent either because they are in nonspendable form, such as inventory and prepaid items, or because they are legally or contractually required to be maintained intact.

Restricted—amounts that can be spent only for specific purposes because of enabling legislation or because of constraints that are externally imposed by creditors, grantors, contributors, or the laws or regulations of other governments.

Committed—amounts that can be used only for specific purposes determined by a formal action of the City Council. The City Council is the highest level of decision making authority for the City. Commitments may be established, modified, or rescinded only through ordinances or resolutions approved by the City Council.

Assigned—amounts that do not meet the criteria to be classified as restricted or committed but that are intended to be used for specific purposes. The City Council or, City Administrator or Finance Director authorized by the City Council may assign amounts for specific purposes.

Unassigned—all other spendable amounts.

When an expenditure is incurred for purposes for which both restricted and unrestricted fund balance is available, the City considers restricted funds to have been spent first. When an expenditure is incurred for which committed, assigned, or unassigned fund balances are available, the City considers amounts to have been spent first out of committed funds, then assigned funds, and finally unassigned funds, as needed, unless the City Council has provided otherwise in its commitment or assignment actions.

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

CITY OF GRAND MARAIS, MINNESOTA

**NOTES TO FINANCIAL STATEMENTS
December 31, 2012**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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. The liability for accrued vacation leave is recorded in the appropriate funds as an accrued liability. 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

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", and "restricted cash and cash equivalents". Several funds hold cash separate from the cash and investment pool.

"Cash and cash equivalents" and "restricted cash and cash equivalents" recorded are comprised of:

Cash	\$ 6,875,379
Petty Cash	3,300
Certificates of Deposit	312,000
Investments	<u>375,673</u>
Total	<u>\$ 7,566,352</u>

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 be protected by pledged securities.

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

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

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 \$7,187,379; the bank balance was \$7,201,144. Of the bank balance, \$1,151,336 was insured; of the remaining balance, \$1,049,808 was collateralized with securities held by the pledging financial institution's agent in the City's name and \$5,000,000 was collateralized with an irrevocable standby letter of credit.

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.

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation. The City's investments in 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, 2012, had no investments in any issuer that exceeded five percent of total investments.

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, 2012, the City had the following investments which are not rated:

CITY OF GRAND MARAIS, MINNESOTA

**NOTES TO FINANCIAL STATEMENTS
December 31, 2012**

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

<u>Investment Type</u>	<u>Fair Value</u>
Minnesota Municipal Money Market Fund	\$ 215,253
Morgan Stanley Smith Barney Money Market Funds	160,337
Wells Fargo Money Market Funds	<u>83</u>
Total Investments	<u>\$ 375,673</u>

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, 2012 was \$66,919.

On February 18, 2009, the City loaned \$100,000 to the Cook County/Grand Marais Joint Economic Development Authority. The note bears interest at 6% and was due on October 15, 2010. A payment of \$100,000 was made in 2010 for principal and interest. The balance as of December 31, 2012 was \$5,040.

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

NOTE 4 - CAPITAL ASSETS

Capital asset activity for the year ended December 31, 2012, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Deletions</u>	<u>Ending Balance</u>
Governmental activities				
Capital assets, not being depreciated:				
Land	\$ 630,922	\$ -	\$ -	\$ 630,922
Capital assets, being depreciated:				
Buildings	5,865,079	5,855	-	5,870,934
Improvements	616,919	90,000	-	706,919
Infrastructure	7,713,541	26,858	-	7,740,399
Machinery and equipment	457,836	80,471	(81,368)	456,939
Licensed vehicles	442,098	-	-	442,098
Total capital assets, being depreciated	<u>15,095,473</u>	<u>203,184</u>	<u>(81,368)</u>	<u>15,217,289</u>
Less accumulated depreciation for:				
Buildings	(3,417,944)	(108,857)	-	(3,526,801)
Improvements	(180,612)	(24,757)	-	(205,369)
Infrastructure	(2,370,731)	(175,428)	-	(2,546,159)
Machinery and equipment	(245,774)	(27,286)	80,025	(193,035)
Licensed vehicles	(158,542)	(20,024)	-	(178,566)
Total accumulated depreciation	<u>(6,373,603)</u>	<u>(356,352)</u>	<u>80,025</u>	<u>(6,649,930)</u>
Total capital assets, being depreciated, net	<u>8,721,870</u>	<u>(153,168)</u>	<u>(1,343)</u>	<u>8,567,359</u>
Governmental activities capital assets, net	<u>\$ 9,352,792</u>	<u>\$ (153,168)</u>	<u>\$ (1,343)</u>	<u>\$ 9,198,281</u>
Business-type activities				
Capital assets, not being depreciated:				
Land	\$ 186,100	\$ -	\$ -	\$ 186,100
Construction in progress	-	40,000	-	40,000
Total capital assets, not being depreciated	<u>186,100</u>	<u>40,000</u>	<u>-</u>	<u>226,100</u>
Capital assets, being depreciated:				
Buildings	7,619,754	-	-	7,619,754
Improvements	310,058	-	-	310,058
Infrastructure	12,111,356	108,453	-	12,219,809
Machinery and equipment	1,930,859	36,321	-	1,967,180
Licensed vehicles	322,453	-	-	322,453
Total capital assets, being depreciated	<u>22,294,480</u>	<u>144,774</u>	<u>-</u>	<u>22,439,254</u>
Less accumulated depreciation for:				
Buildings	(3,079,873)	(196,305)	-	(3,276,178)
Improvements	(272,569)	(1,865)	-	(274,434)
Infrastructure	(2,903,257)	(271,109)	-	(3,174,366)
Machinery and equipment	(1,754,389)	(39,927)	-	(1,794,316)
Licensed vehicles	(251,204)	(21,904)	-	(273,108)
Total accumulated depreciation	<u>(8,261,292)</u>	<u>(531,110)</u>	<u>-</u>	<u>(8,792,402)</u>
Total capital assets, being depreciated, net	<u>14,033,188</u>	<u>(386,336)</u>	<u>-</u>	<u>13,646,852</u>
Business-type activities capital assets, net	<u>\$14,219,288</u>	<u>\$ (346,336)</u>	<u>\$ -</u>	<u>\$13,872,952</u>

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

NOTE 4 - CAPITAL ASSETS (CONTINUED)

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

Governmental activities

General government	\$ 1,859
Public safety	25,589
Streets	184,746
Culture and recreation	<u>144,158</u>
Total depreciation expense- governmental activities	<u>\$ 356,352</u>

Business-type activities

Liquor Store	\$ 3,900
Golf Course	12,578
Electric	209,132
Water	173,902
Sewer	<u>131,598</u>
Total depreciation expense- business-type activities	<u>\$ 531,110</u>

NOTE 5 - RATE STABILIZATION PROVISION

A reserve for rate stabilization in the electric enterprise fund 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, 2012, 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 electric revenue bonds are payable solely from the net revenues of the Electric Enterprise Fund, the water revenue notes are payable solely from the net revenues of the Water Enterprise Fund, and the sewer revenue bond is payable solely from the net revenues of the Sewer Enterprise Fund.

CITY OF GRAND MARAIS, MINNESOTA

**NOTES TO FINANCIAL STATEMENTS
December 31, 2012**

NOTE 6 - LONG-TERM LIABILITIES (CONTINUED)

Components of long-term liabilities are as follows:

	<u>Issue Date</u>	<u>Interest Rates</u>	<u>Original Issue</u>	<u>Final Maturity</u>	<u>Principal Outstanding</u>
Governmental Activities					
General Obligation Bonds					
2004 Improvement	06/01/2004	3.40-5.10%	\$ 710,000	02/01/2025	\$ 525,000
2005 Improvement	11/22/2005	3.50-4.60%	\$ 895,000	02/01/2027	735,000
2008 Improvement	10/07/2008	3.25-4.50%	\$ 2,695,000	02/01/2029	2,245,000
2009 Improvement Refunding	12/10/2009	2.10-4.70%	\$ 1,675,000	02/01/2031	<u>1,620,000</u>
					<u>5,125,000</u>
Governmental Activities Long-term Liabilities					
Business-type activities					
Revenue Bonds					
2004 Electric System	09/01/2004	4.00-4.80%	\$ 815,000	05/01/2023	575,000
2005 Electric System	06/21/2005	2.75-4.60%	\$ 940,000	05/01/2024	760,000
2012 Electric System Refunding	07/25/2012	2.00-2.50%	\$ 1,925,000	05/01/2023	<u>1,925,000</u>
Total Revenue Bonds					<u>3,260,000</u>
General Obligation Revenue Bonds					
2006 Sewer	01/17/2006	4.50%	\$ 372,000	01/01/2036	<u>337,000</u>
General Obligation Notes					
1999 Water Revenue	04/27/1999	2.56%	\$ 484,112	08/20/2019	206,000
2004 Improvement	08/11/2004	2.53%	\$ 812,229	02/20/2024	<u>545,000</u>
Total General Obligation Notes					<u>751,000</u>
Revenue Note					
2008 Water	01/24/2008	3.59%	\$ 470,000	12/01/2027	<u>380,000</u>
					<u>4,728,000</u>
Business-type Activities Long-term Liabilities					
Total Long-Term Liabilities					\$ <u>9,853,000</u>

Governmental Funds

Pledged Revenues

The City issued GO improvement bonds to finance various improvement projects within the City in 2004 of \$710,000, in 2005 of \$895,000, and in 2008 of \$2,695,000. Principal and interest paid for the current year on these issues was \$303,371. At December 31, 2012 principal and interest on the bonds to be paid from special assessments levied upon the benefitted property and ad valorem taxes to maturity is:

	<u>Issue</u>	<u>Maturity</u>	<u>Principal and Interest</u>
	2004	2025	\$ 714,853
	2005	2027	1,011,457
	2008	2029	<u>3,169,145</u>
			<u>\$ 4,895,455</u>

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

NOTE 6 - LONG-TERM LIABILITIES (CONTINUED)

In 2005, the City issued \$875,000 GO improvement refunding bonds of which the proceeds were used to effect a crossover refunding of \$815,000 of the outstanding GO Improvement Bonds of 2000 issued to finance the costs of various municipal improvements within the City. Principal and interest paid for the current year was \$730,251 resulting in an early extinguishment of the outstanding bonds.

In 2009, the City issued \$1,675,000 improvement refunding bonds of which the proceeds were used to effect a refunding of \$1,630,000 of the outstanding GO Temporary Improvement Bonds of 2007 issued to finance various municipal improvement projects within the City. Principal and interest paid for the current year was \$118,893. At December 31, 2012, principal and interest to maturity in 2031 to be paid primarily from special assessments levied upon the benefitted property and ad valorem taxes totaled \$2,363,750.

Enterprise Funds

Pledged Revenues

The City has pledged Electric Enterprise Fund revenues, net of any normal and reasonable expenses of operations, to repay electric system revenue bonds issued in 2003 of \$2,885,000, in 2004 of \$815,000, and in 2005 of \$940,000. Proceeds from the bonds were used to finance electric system improvements. In 2012, the City issued \$1,925,000 revenue refunding bonds of which the proceeds were used to effect an advance refunding of the outstanding 2003 electric system revenue bonds. Principal and interest paid for the current year on these issues was \$2,150,912. At December 31, 2012 principal and interest on the bonds to be paid from pledged future revenues to maturity is:

<u>Issue</u>	<u>Maturity</u>	<u>Principal and Interest</u>
2004	2023	\$ 733,610
2005	2024	1,048,583
2012	2023	<u>2,184,403</u>
		<u>\$ 3,966,596</u>

The City has pledged future Sewer Enterprise Fund revenues, net of any normal and reasonable expenses of operations, to repay \$372,000 in GO sewer revenue bonds issued in 2006. Proceeds from the bonds were used to finance improvements to the sewer system. Principal and interest paid for the current year was \$23,525. At December 31, 2012, principal and interest on the bonds to maturity in 2036 to be paid from pledged future revenues totaled \$557,410.

The City has pledged future Water Enterprise Fund revenues, net of any normal and reasonable expenses for operations, to repay a \$484,112 GO revenue note issued in 1999, an \$812,229 GO improvement note issued in 2004, and a \$470,000 revenue note issued in 2008. Proceeds from all three issues were used to finance water system renovations and improvements. Principal and interest paid for the current year on these issues was \$118,329. At December 31, 2012, principal and interest on the notes to be paid from pledged future revenues, and special assessments and ad valorem taxes for the 2004 issue, to maturity is:

<u>Issue</u>	<u>Maturity</u>	<u>Principal and Interest</u>
1999	2019	\$ 227,658
2004	2024	631,943
2008	2027	<u>526,111</u>
		<u>\$ 1,385,712</u>

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

NOTE 6 - LONG-TERM LIABILITIES (CONTINUED)

Long-term liability activity for the year ended December 31, 2012 was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Amounts Due Within One Year</u>
Governmental activities					
Bonds Payable					
2004 GO Improvements	\$ 555,000	\$ -	\$ 30,000	\$ 525,000	\$ 30,000
2005 GO Improvements	770,000	-	35,000	735,000	35,000
2005 GO Improvement Refunding	715,000	-	715,000	-	-
2008 GO Improvement	2,330,000	-	85,000	2,245,000	90,000
2009 GO Improvement Refunding	<u>1,675,000</u>	-	<u>55,000</u>	<u>1,620,000</u>	<u>55,000</u>
Governmental Activities - Long-term Liabilities	<u>\$ 6,045,000</u>	<u>\$ -</u>	<u>\$ 920,000</u>	<u>\$ 5,125,000</u>	<u>\$ 210,000</u>
Business-type Activities					
Bonds Payable					
2003 Electric System Revenue	\$ 1,975,000	\$ -	\$ 1,975,000	\$ -	\$ -
2004 Electric System Revenue	615,000	-	40,000	575,000	40,000
2005 Electric System Revenue	790,000	-	30,000	760,000	30,000
2006 GO Sewer Revenue	345,000	-	8,000	337,000	8,000
2012 Electric System Revenue Refunding	-	<u>1,925,000</u>	-	<u>1,925,000</u>	<u>170,000</u>
Total Bonds Payable	<u>3,725,000</u>	<u>1,925,000</u>	<u>2,053,000</u>	<u>3,597,000</u>	<u>248,000</u>
Notes Payable					
1999 GO Water Revenue	232,000	-	26,000	206,000	27,000
2004 GO Improvement	583,000	-	38,000	545,000	39,000
2008 Water Revenue	<u>400,000</u>	-	<u>20,000</u>	<u>380,000</u>	<u>20,000</u>
Total Notes Payable	<u>1,215,000</u>	<u>-</u>	<u>84,000</u>	<u>1,131,000</u>	<u>86,000</u>
Business-type Activities - Long-term Liabilities	<u>\$ 4,940,000</u>	<u>\$ 1,925,000</u>	<u>\$ 2,137,000</u>	<u>\$ 4,728,000</u>	<u>\$ 334,000</u>

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

<u>Year Ending December 31</u>	<u>Governmental Activities</u>		<u>Business-Type Activities</u>		<u>Government-wide</u>	
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2013	\$ 210,000	\$ 210,481	\$ 334,000	\$ 160,020	\$ 544,000	\$ 370,501
2014	220,000	203,163	331,000	139,640	551,000	342,803
2015	240,000	195,120	339,000	130,227	579,000	325,347
2016	245,000	186,335	346,000	120,509	591,000	306,844
2017	250,000	177,072	359,000	110,459	609,000	287,531
2018-2022	1,425,000	721,934	1,889,000	383,670	3,314,000	1,105,604
2023-2027	1,700,000	378,438	962,000	97,322	2,662,000	475,760
2028-2032	835,000	61,662	86,000	30,420	921,000	92,082
2033-2037	-	-	82,000	9,450	82,000	9,450
Total	<u>\$ 5,125,000</u>	<u>\$ 2,134,205</u>	<u>\$ 4,728,000</u>	<u>\$ 1,181,717</u>	<u>\$ 9,853,000</u>	<u>\$ 3,315,922</u>

No interest was capitalized during 2012; interest incurred and charged to expense totaled \$375,928.

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

NOTE 6 - LONG-TERM LIABILITIES (CONTINUED)

Deferred Amount on Refunding

On July 25, 2012, the City issued \$1,925,000 Electric System Revenue Refunding Bonds, Series 2012A with interest rates ranging between 2.000% and 2.500% to advance refund \$1,845,000 of the outstanding 2003 Electric System Revenue Bonds with interest rates ranging between 4.000% and 4.875%. The proceeds of the new bonds were placed in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the refunded bonds are not included in the City's financial statements. As of December 31, 2012, \$1,845,000 of the bonds outstanding are considered defeased. The advance refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of \$82,096 which was deferred and is being amortized over the life of the new debt.

NOTE 7 - INTERFUND BALANCES AND ACTIVITY

The composition of interfund balances as of December 31, 2012, is as follows:

Due to/from other funds –

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General	Electric Enterprise	\$ <u>64,899</u>

The balance 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, and (3) payments between funds are made.

Interfund transfers for the year ended December 31, 2012 consisted of the following:

	<u>Transfers Out</u>					<u>Total</u>
	<u>General Fund</u>	<u>Liquor Store Enterprise Fund</u>	<u>Electric Enterprise Fund</u>	<u>Water Enterprise Fund</u>	<u>Sewer Enterprise Fund</u>	
<u>Transfers In</u>						
General Fund	\$ -	\$ 200,000	\$ 2,114	\$ 1,058	\$ 1,058	\$ 204,230
Debt Service Fund	200,000	-	-	45,315	465,210	710,525
Golf Course Enterprise Fund	50,757	-	-	-	-	50,757
Nonmajor fund - Library Special Revenue Fund	<u>125,015</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>125,015</u>
	<u>\$ 375,772</u>	<u>\$ 200,000</u>	<u>\$ 2,114</u>	<u>\$ 46,373</u>	<u>\$ 466,268</u>	<u>\$1,090,527</u>

Transfers are used to: 1) move profits or excess cash from the Liquor Store Enterprise Fund to the General Fund; 2) move the City's contribution to the City library; 3) move funds from the Water and Sewer Enterprise funds to the Debt Service Fund for debt service expenditures; and 4) fund the operations of the Golf Course.

CITY OF GRAND MARAIS, MINNESOTA

**NOTES TO FINANCIAL STATEMENTS
December 31, 2012**

NOTE 8 - FUND EQUITY

As of December 31, 2012, fund balances are comprised of the following:

	<u>General Fund</u>	<u>Debt Service Fund</u>	<u>Nonmajor Governmental Funds</u>	<u>Total</u>
Nonspendable:				
Inventories	\$ 18,757	\$ -	\$ -	\$ 18,757
Prepaid items	<u>38,858</u>	<u>-</u>	<u>3,740</u>	<u>42,598</u>
Total Nonspendable	<u>57,615</u>	<u>-</u>	<u>3,740</u>	<u>61,355</u>
Restricted:				
Library	-	-	252,263	252,263
Storefront renovation	-	-	78,265	78,265
Debt service	-	556,517	-	556,517
Capital projects	<u>-</u>	<u>-</u>	<u>13,059</u>	<u>13,059</u>
Total Restricted	<u>-</u>	<u>556,517</u>	<u>343,587</u>	<u>900,104</u>
Committed:				
Cable TV	<u>-</u>	<u>-</u>	<u>20,078</u>	<u>20,078</u>
Assigned:				
Buildings	51,713	-	-	51,713
Insurance reserve	10,804	-	-	10,804
Street equipment	18,282	-	-	18,282
Street improvements	242,370	-	-	242,370
Street sealcoat project	70,965	-	-	70,965
Library	<u>-</u>	<u>-</u>	<u>226,614</u>	<u>226,614</u>
Total Assigned	<u>394,134</u>	<u>-</u>	<u>226,614</u>	<u>620,748</u>
Unassigned	<u>1,661,074</u>	<u>-</u>	<u>-</u>	<u>1,661,074</u>
Total fund balances	<u>\$ 2,112,823</u>	<u>\$ 556,517</u>	<u>\$ 594,019</u>	<u>\$ 3,263,359</u>

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.

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

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.

NOTE 11 - JOINT VENTURE

Joint Powers Agreement for Library Services

The City of Grand Marais entered into a joint powers agreement with Cook County on December 15, 1992. The purpose of the agreement is to provide library services to the residents of the City and County through the City's Grand Marais Public Library. The County, in consideration of the services provided to its residents, agrees to continue its membership in the multi-county Arrowhead Library System and contribute 50% of the budgeted annual operating costs of the library board to the City, which totaled \$102,329 in 2012.

The library is governed by a board of seven members serving staggered three-year terms and appointed by the Mayor of the City with the consent of the City Council. Four members shall be residents of the City and three members shall be county residents from outside the City limits.

If the agreement is terminated, any capital assets (other than the original library building) purchased during the term of the agreement having a purchase price in excess of \$1,000, shall be reimbursed fifty percent of the then market value to the County. This reimbursement only applies to the purchase price paid from the normal operating budget shared by the City and County and shall not apply to the purchase price paid by gift, grant, or other outside funding.

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.

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

NOTE 11 - JOINT VENTURE (CONTINUED)

In 2012, 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.

Joint Powers Agreement for Shared Costs of Cook County Community Center

The City entered into a joint powers agreement with Cook County to implement procedures for the sharing of costs by the County and City for the new Cook County Community Center benefitting constituents of the City and County.

The use of the Community Center will be under the control of the County who has contracted with the Duluth Area Family YMCA (the "YMCA") pursuant to a management agreement.

The County, through the YMCA, shall establish the schedule of operating hours, events, services and programs for the use of the Community Center consistent with the Management Agreement and this Agreement.

In consideration of the services provided to its residents, the City shall:

- (i) Annually contribute to the County fifty percent (50%) of the prior year's annual operating losses based on costs of maintenance of the Community Center building (not including any outdoor recreation areas or amenities) and programming up to \$100,000. If the annual operating losses exceed \$200,000 the City contribution shall increase annually by the lesser of five percent (5%) or a percentage equal to the annual Consumer Price Index (CPI – Midwest Urban Nonmetropolitan (less than 50,000) for the preceding calendar year; *provided, however,* that if such increase is greater than the lesser of five percent (5%) or a percentage equal to the annual CPI for the preceding calendar year, such greater amount must be approved by the City. The County shall annually invoice the City for the City's portion of the operating loss up to the maximum allowed percent increase as applicable at least 60 days prior to the payment date and shall include a separate itemized accounting of the operating loss with the County's invoice. Any request for additional payments for operating losses above the allowed percent maximum increase in any given year shall be by separate written request from the County.
- (ii) Pay fifty percent (50%) of the YMCA personnel costs for the 6-month period prior to the official opening of the YMCA in the year that the Community Center building commences operation, up to a maximum of \$35,000.
- (iii) Annually contribute \$10,000 to the Community Center Capital Improvement Fund. The County shall manage the Capital Improvement Fund, which shall be used for the repair, replacement, and maintenance of the structural components of the Community Center building.
- (iv) The City shall not be responsible for payment of any costs or expenses for or related to the Community Center except as otherwise provided in this Agreement.

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

NOTE 11 - JOINT VENTURE (CONTINUED)

In consideration of the City's commitment to share the ongoing costs of maintenance and of the Community Center as provided above, the County shall:

- (i) Pay fifty percent (50%) of the costs to demolish and remove the existing City-owned swimming pool, which amount shall not exceed \$25,000 without the prior written consent of the County; and
- (ii) Pay fifty percent (50%) of the costs to settle the case with Burbach Aquatics, Inc. (including exclusively the settlement amount as contained in that certain 2012 settlement and release agreement between Burbach Aquatics, Inc. and the City, along with the City's attorney fees incurred in settling such matter) which amount shall not exceed \$39,628; and
- (iii) Pay or arrange for payment of all other costs and expenses related to the Community Center.

Management of the Cook County Family YMCA shall be pursuant to the Management Agreement between the County and Duluth YMCA. A representative appointed by the City Council shall serve as a voting member on the Branch Board of Directors for the Community Center; such representation is not intended to create a joint venture or joint enterprise between the City and the County.

The County will own the Community Center, and this Agreement provides the City no ownership interest in the Community Center as the intent of this Agreement is to allow the City to contribute financially to assist the County with the future operating losses of the Community Center. The County will be responsible for operation, maintenance, construction, repair and reconstruction of the Community Center and all improvements thereto; provided that the County may assign operation and management obligations to the YMCA.

This Agreement shall remain in full force and effect for a period of twenty-five (25) years from its effective date and shall automatically renew in five (5) year increments thereafter, unless the City or County within 180 days of the expiration of a respective period provides written notice of termination to the other party. Notwithstanding the foregoing, this Agreement may be terminated by mutual written agreement of the City and County.

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, 2012, 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.

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

NOTE 12 - OTHER COMMITMENTS AND CONTINGENCIES (CONTINUED)

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, 2050. 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.

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 \$20,655 on December 31, 2012.

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 General Employees Retirement Fund (GERF) which is a cost-sharing, multiple-employer retirement plan. This plan is established and administered in accordance with *Minnesota Statutes*, Chapter 353 and 356.

GERF 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.

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

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

Two methods are used to compute benefits for PERA'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 GERP 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.

PERA issues a publicly available financial report that includes financial statements and required supplementary information for GERP. 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. GERP Basic Plan members and Coordinated Plan members were required to contribute 9.10% and 6.25%, respectively, of their annual covered salary in 2012. In 2012, the City of Grand Marais was required to contribute the following percentages of annual covered payroll: 11.78% for Basic Plan members and 7.25% for Coordinated Plan members. The City's contributions to the Public Employees Retirement Fund for the years ending December 31, 2012, 2011, and 2010 were \$87,713, \$87,853, and \$83,267, respectively. The City's contributions were equal to the contractually required contributions for each year as set by state statute.

CITY OF GRAND MARAIS, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

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.

Total contributions made by the City of Grand Marais, Minnesota during fiscal year 2012 were:

<u>Contribution Amount</u>		<u>Percentage of Covered Payroll</u>		<u>Required</u>
<u>Employee</u>	<u>Employer</u>	<u>Employee</u>	<u>Employer</u>	<u>Rates</u>
\$ 240	\$ 240	5.0%	5.0%	5.0%

NOTE 16 - SUBSEQUENT EVENT

On May 29, 2013, the City authorized the sale of \$3,635,000 General Obligation Refunding Bonds, Series 2013A of which the proceeds were used to effect a partial net cash refunding of:

- 1) \$710,000 GO Improvement Bonds, Series 2004A that were issued to finance the construction of the City's Downtown Streetscape Improvement Project;
- 2) \$895,000 GO Improvement Bonds, Series 2005C that were issued to finance various improvements within the City;
- 3) \$2,695,000 GO Improvement Bonds, Series 2008A that were issued to finance the cost of various improvement projects within the City;
- 4) \$372,000 USDA Rural Development GO Sewer Revenue Bonds, Series 2006 that were issued to finance sewer improvements within the City.

The closing date will be June 20, 2013. The City received a Standard & Poor's A+ rating. Three bids were received from 2.5553% to 3.0721%. The refunding creates present value savings of \$342,257.

CITY OF GRAND MARAIS, MINNESOTA

**NOTES TO FINANCIAL STATEMENTS
December 31, 2012**

NOTE 16 - SUBSEQUENT EVENT (CONTINUED)

On May 29, 2013, the Public Utilities Commission authorized the sale of \$1,300,000 Electric System Revenue Refunding Bonds, Series 2013B with the City concurring of which the proceeds were used to effect full net cash refunding of:

- 1) \$815,000 Electric System Revenue Bonds, Series 2004 that were issued to undertake capital improvements to the municipal electric light and power plant and distribution system of the City consisting of capital improvements to the Electric System, specifically, distribution upgrades, including replacement of existing lines to handle higher voltage;
- 2) \$940,000 Electric System Revenue Bonds, Series 2005B that were issued to undertake capital improvements to the municipal electric light and power plant and distribution system of the City consisting of improvements and extensions.

The closing date will be June 20, 2013. The Electric Fund received a Standard and Poor's A rating. Three bids were received from 2.3369% to 2.4989%. The refunding creates present value savings of \$94,761.

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, 2012**

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget - Positive (Negative)
REVENUES				
Taxes				
Property	\$ 638,574	\$ 638,574	\$ 625,429	\$ (13,145)
Special assessments	5,085	5,085	8,226	3,141
Licenses and permits	79,500	79,500	82,990	3,490
Intergovernmental	171,737	171,737	266,607	94,870
Charges for services	956,020	956,020	1,117,686	161,666
Fines	1,500	1,500	4,734	3,234
Gifts and contributions	-	-	9,120	9,120
Interest	12,000	12,000	7,257	(4,743)
Miscellaneous	-	-	29,696	29,696
TOTAL REVENUES	1,864,416	1,864,416	2,151,745	287,329
EXPENDITURES				
Current				
General government	367,189	367,189	415,082	(47,893)
Public safety	224,481	224,481	197,222	27,259
Streets	339,509	339,509	259,217	80,292
Culture and recreation	925,289	925,289	776,110	149,179
Economic development	-	-	90,000	(90,000)
TOTAL EXPENDITURES	1,856,468	1,856,468	1,737,631	118,837
EXCESS OF REVENUES OVER EXPENDITURES	7,948	7,948	414,114	406,166
OTHER FINANCING SOURCES (USES)				
Transfers in	200,000	200,000	204,230	4,230
Transfers out	(139,819)	(139,819)	(375,772)	(235,953)
Sale of capital assets	-	-	76,022	76,022
TOTAL OTHER FINANCING SOURCES (USES)	60,181	60,181	(95,520)	(155,701)
NET CHANGE IN FUND BALANCE	68,129	68,129	318,594	250,465
FUND BALANCE - JANUARY 1	1,794,229	1,794,229	1,794,229	-
FUND BALANCE - DECEMBER 31	\$ 1,862,358	\$ 1,862,358	\$ 2,112,823	\$ 250,465

See notes to required supplementary information.

CITY OF GRAND MARAIS, MINNESOTA

**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
December 31, 2012**

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 and report the proceeds of specific revenue sources that are legally restricted or committed to expenditure for specified purposes other than debt service or capital projects.

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

The Cable TV Special Revenue Fund is used to account for revenues collected to fund the operation of a TV 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 and report financial resources that are restricted, committed or assigned to expenditure for capital outlays, including the acquisition and construction of capital facilities and other capital assets. Capital projects funds exclude those types of capital-related outflows 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, 2012

	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	\$ 502,768	\$ 18,994	\$ 78,265	\$ 13,059	\$ 613,086
Accounts receivable	-	1,084	-	-	1,084
Loans receivables	-	-	66,919	-	66,919
Prepaid items	3,740	-	-	-	3,740
TOTAL ASSETS	\$ 506,508	\$ 20,078	\$ 145,184	\$ 13,059	\$ 684,829
LIABILITIES AND FUND BALANCES					
LIABILITIES					
Accounts payable	\$ 4,483	\$ -	\$ -	\$ -	\$ 4,483
Salaries payable	19,408	-	-	-	19,408
Deferred revenue	-	-	66,919	-	66,919
TOTAL LIABILITIES	23,891	-	66,919	-	90,810
FUND BALANCES					
Nonspendable	3,740	-	-	-	3,740
Restricted	252,263	-	78,265	13,059	343,587
Committed	-	20,078	-	-	20,078
Assigned	226,614	-	-	-	226,614
TOTAL FUND BALANCES	482,617	20,078	78,265	13,059	594,019
TOTAL LIABILITIES AND FUND BALANCES	\$ 506,508	\$ 20,078	\$ 145,184	\$ 13,059	\$ 684,829

CITY OF GRAND MARAIS, MINNESOTA

COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
NONMAJOR GOVERNMENTAL FUNDS
Year Ended December 31, 2012

	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	\$ -	\$ 4,429	\$ -	\$ -	\$ 4,429
Intergovernmental	102,329	-	-	-	102,329
Charges for services	14,675	-	-	-	14,675
Gifts and contributions	20,894	-	-	-	20,894
Interest	1,170	-	1,886	33	3,089
Miscellaneous	-	-	18,778	-	18,778
TOTAL REVENUES	<u>139,068</u>	<u>4,429</u>	<u>20,664</u>	<u>33</u>	<u>164,194</u>
EXPENDITURES					
Current					
Culture and recreation	264,911	-	-	-	264,911
Economic development	-	-	21,853	-	21,853
TOTAL EXPENDITURES	<u>264,911</u>	<u>-</u>	<u>21,853</u>	<u>-</u>	<u>286,764</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	<u>(125,843)</u>	<u>4,429</u>	<u>(1,189)</u>	<u>33</u>	<u>(122,570)</u>
OTHER FINANCING USES					
Transfers in	<u>125,015</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>125,015</u>
NET CHANGE IN FUND BALANCES	(828)	4,429	(1,189)	33	2,445
FUND BALANCES - JANUARY 1	<u>483,445</u>	<u>15,649</u>	<u>79,454</u>	<u>13,026</u>	<u>591,574</u>
FUND BALANCES - DECEMBER 31	<u>\$ 482,617</u>	<u>\$ 20,078</u>	<u>\$ 78,265</u>	<u>\$ 13,059</u>	<u>\$ 594,019</u>

CITY OF GRAND MARAIS, MINNESOTA

GENERAL FUND
 STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
 Year Ended December 31, 2012

REVENUES

Taxes	
General property	<u>\$ 625,429</u>
Special Assessments	<u>8,226</u>
Licenses and permits	<u>82,990</u>
Intergovernmental	
Federal grants	
Coastal	90,000
State	
Local government aid	96,422
Market value credit	9
Taconite production	2,829
PERA aid	5,315
County	
Swimming pool	64,472
Soil and water conservation	7,560
Total Intergovernmental	<u>266,607</u>
Charges for Services	
General government	
Rent	62,942
Miscellaneous	10,366
Public safety	
Fire protection contacts	44,597
Culture and recreation	
Park	821,694
Swimming pool	68,586
Boat harbors	109,501
Total Charges for Services	<u>1,117,686</u>
Fines	
Court fines	<u>4,734</u>
Gifts and Contributions	<u>9,120</u>
Interest	<u>7,257</u>
Miscellaneous	
Other	<u>29,696</u>
TOTAL REVENUES	<u>2,151,745</u>

CITY OF GRAND MARAIS, MINNESOTA

GENERAL FUND
 STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
 (CONTINUED)
 Year Ended December 31, 2012

EXPENDITURES

Current

General Government

Mayor and council	\$ 27,201
City clerk	156,455
City clerk capital outlay	8,459
Independent audit	13,300
Legal	40,098
Planning and zoning	26,380
Buildings	52,293
Other	<u>90,896</u>
Total General Government	<u>415,082</u>

Public Safety

Police	140,000
Fire	47,558
Fire capital outlay	7,951
Medical services	253
Animal control	<u>1,460</u>
Total Public Safety	<u>197,222</u>

Streets

Maintenance	159,669
Street lighting	26,734
Capital outlay	<u>72,814</u>
Total Streets	<u>259,217</u>

Culture and Recreation

Recreation	417,881
Recreation capital outlay	7,484
Swimming pool	239,338
Swimming pool capital outlay	5,435
Boat harbors	77,851
City parks	<u>28,121</u>
Total Culture and Recreation	<u>776,110</u>

Economic Development

Community development capital outlay	<u>90,000</u>
--------------------------------------	---------------

TOTAL EXPENDITURES

1,737,631

CITY OF GRAND MARAIS, MINNESOTA

GENERAL FUND
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
(CONTINUED)
Year Ended December 31, 2012

EXCESS OF REVENUES OVER EXPENDITURES	<u>414,114</u>
OTHER FINANCING SOURCES (USES)	
Transfers in	204,230
Transfers out	(375,772)
Sale of capital assets	<u>76,022</u>
TOTAL OTHER FINANCING SOURCES (USES)	<u>(95,520)</u>
NET CHANGE IN FUND BALANCE	318,594
FUND BALANCE - JANUARY 1	<u>1,794,229</u>
FUND BALANCE - DECEMBER 31	<u>\$ 2,112,823</u>



CERTIFIED PUBLIC ACCOUNTANTS & CONSULTANTS

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**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**

Independent Auditor's Report

To the City Council
City of Grand Marais, Minnesota

We have audited 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, 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, 2012, and the related notes to the financial statements, which collectively comprise the City of Grand Marais, Minnesota's basic financial statements and have issued our report thereon dated June 18, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered City of Grand Marais, Minnesota's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances 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 of Grand Marais, Minnesota's internal control. Accordingly, we do not express an opinion on the effectiveness of the City of Grand Marais, Minnesota's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and responses, we identified a certain deficiency in internal control that we consider to be a material weakness and another deficiency that we consider to be a significant deficiency.

A *deficiency in internal control* 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 and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency described in the accompanying schedule of findings and responses as item 2012-2 to be a material weakness.

A *significant deficiency* is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency described in the accompanying schedule of findings and responses as item 2012-1 to be a significant deficiency.

Compliance

As part of obtaining reasonable assurance about whether City of Grand Marais, Minnesota's financial statements are free from 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*.

Minnesota Legal Compliance

The *Minnesota Legal Compliance Audit Guide for Political Subdivisions*, promulgated by the State Auditor pursuant to Minn. Stat. § 6.65, contains 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 audit considered all of the listed categories.

In connection with our audit, nothing came to our attention that caused us to believe that City of Grand Marais, Minnesota failed to comply with the provisions of the *Minnesota Legal Compliance Audit Guide for Political Subdivisions*. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the City of Grand Marais, Minnesota's noncompliance with the above referenced provisions.

Other Matters

We noted certain matters that we reported to management of City of Grand Marais, Minnesota in a separate letter dated June 18, 2013, included under this cover.

City of Grand Marais, Minnesota's Response to Findings

City of Grand Marais, Minnesota's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. City of Grand Marais, Minnesota's response was not subjected to the auditing procedures applied in the audit of the financial statements, and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Walker, Hiron & Nelson, Ltd

June 18, 2013

CITY OF GRAND MARAIS, MINNESOTA
SCHEDULE OF FINDINGS AND RESPONSES
Year Ended December 31, 2012

SIGNIFICANT DEFICIENCIES

2012-1. 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.

Cause

This occurred because of staffing limitations 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.

CITY OF GRAND MARAIS, MINNESOTA

**SCHEDULE OF FINDINGS AND RESPONSES (CONTINUED)
Year Ended December 31, 2012**

2012-2. 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 does not possess the technical expertise to comply with governmental accounting standards.

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.



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, 2012, 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 auditing procedures that are appropriate in the circumstances 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 deficiencies in internal control other than significant deficiencies and material weaknesses and matters that are opportunities for strengthening internal controls and operating efficiency. A separate report dated June 18, 2013, included under this cover, contains our report on significant deficiencies or material weaknesses in the City's internal control. This letter does not affect our report dated June 18, 2013, 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:

Receipts

We noted monthly receipts from other locations, such as the pool, were dated and deposited into the bank account subsequent to month end. To aid in reconciling the bank statement at month end, we suggest that the month end date be reflected on these deposit slips.

Contracting and Bidding

During our review of bid/quote files we noted that an ad calling for bids for the sale of the sweeper was placed on the local website, but a hard copy of the ad was not on file. We recommend that a copy of all bid ads be maintained on file.

Utility Billing Adjustments

With regard to utility billing adjustments, we noted that a list of customer accounts written off during the year was not presented to the Commission for approval. As an internal control measure, we recommend that the customer names, account numbers, and amounts be presented to the Commission for approval to write-off.

Disbursements

- 1) Minnesota Statute §471.425, subd. 4 requires municipalities to pay all bills within the time period set by the terms of the contract or within the standard payment period (35 days). In particular, we noted two library bills that were not paid within this timeframe. The City should inform all departments of this state statute and require that all vendor invoices be promptly turned over to the City for proper and timely payment to the vendor. We recommend stamping the date received on the vendor invoice so employees are aware of this timeline.
- 2) We noted a petty cash disbursement without documentation for reimbursement. We recommend the use of formal petty cash vouchers for all fund disbursements. Such vouchers should be properly approved and should be signed and dated by the payee with supporting documentation attached. We also recommend that a maximum amount be established for individual fund disbursements.

Inventory

The physical inventory count for electric line inventory was missing individual item cost amounts and was therefore not properly totaled. Periodic physical inventories provide a basis for updating inventory balances and aid in detecting significant inventory shortages.

We recommend that the City prepare detailed written inventory instructions. These instructions, if followed, ensure that all pricing items are counted, each item is included only once, and proper summarization of counts is prepared. Pricing of the physical quantities counted should be consistent and well documented to be reliable. Persons responsible for pricing should indicate whether prices are from sources other than the most recent invoice. The computer can assist in keeping price records and computing extensions and footings.

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, Hiron & Hahn, Ltd

June 18, 2013