

**CITY OF SILVER BAY
Lake County, Minnesota**

AUDITED FINANCIAL STATEMENTS

For the Year Ended December 31, 2012

CITY OF SILVER BAY

TABLE OF CONTENTS

ELECTED OFFICIALS AND ADMINISTRATION	1	
INDEPENDENT AUDITOR’S REPORT	2	
MANAGEMENT’S DISCUSSION AND ANALYSIS	5	
BASIC FINANCIAL STATEMENTS		
Government-Wide Financial Statements:		
Statement of Net Position	14	
Statement of Activities.....	15	
Fund Financial Statements:		
Balance Sheet – Governmental Funds	16	
Reconciliation of the Balance Sheet to the Statement of Net Position Governmental Funds	19	
Statement of Revenues, Expenditures and Changes in Fund Balances Governmental Funds	20	
Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balances to the Statement of Activities – Governmental Funds.....	22	
Statement of Revenues, Expenditures and Changes in Fund Balances – Budget and Actual – General Fund	23	
Statement of Revenues, Expenditures and Changes in Fund Balances – Budget and Actual – Mary MacDonald Business Center.....	24	
Statement of Net Position – Proprietary Funds.....	25	
Statement of Revenues, Expenses and Changes in Net Position – Proprietary Funds	26	
Statement of Cash Flows – Proprietary Funds.....	27	
Notes to the Financial Statements.....	29	
SUPPLEMENTARY INFORMATION		
Combining Balance Sheet – Nonmajor Governmental Funds	54	
Combining Statement of Revenues, Expenditures and Changes in Fund Balances Nonmajor Governmental Funds.....	56	
Schedule of Revenues, Expenditures and Changes in Fund Balances – Budget and Actual – General Fund	58	
Analysis of Changes in Fund Balance – Public Works Reserve Fund.....	60	
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		63
REPORT ON LEGAL COMPLIANCE	65	
SCHEDULE OF FINDINGS AND RESPONSES ON INTERNAL CONTROL	66	

CITY OF SILVER BAY

**ELECTED OFFICIALS AND ADMINISTRATION
December 31, 2012**

<u>Elected Officials</u>	<u>Position</u>	<u>Term Expires</u>
Scott Johnson	Mayor	December 31, 2012
David Gustafson	Council Member	December 31, 2014
Steven Marolt	Council Member	December 31, 2014
Joanne Johnson	Council Member	December 31, 2012
Carlene Perfetto	Council Member	December 31, 2012
<u>Administration</u>		
Lana Fralich	City Administrator	
Cheryl Marolt	Deputy Clerk	



Expert advice. When you need it.SM

INDEPENDENT AUDITOR'S REPORT

Honorable Mayor and Members
of the City Council
City of Silver Bay
Silver Bay, 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 Silver Bay, 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 Silver Bay, 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.

Implementation of GASB 63

As discussed in Note 15 to the financial statements, the City has adopted the provisions of the Governmental Accounting Standards Board (GASB) Statement No. 63, Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis, which follows this report letter, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by GASB 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's basic financial statements. The supplementary information identified in the Table of Contents is presented for purposes of additional analysis and is not a required part of the basic financial statements.



The supplementary information is the responsibility of management and was derived from and relates 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 supplementary information is 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 February 28, 2013 on our consideration of the City'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 the City's internal control over financial reporting and compliance.

A handwritten signature in cursive script that reads "Kern, DeWenter, Viere, Ltd.".

KERN, DEWENTER, VIERE, LTD.
St. Cloud, Minnesota
February 28, 2013

(THIS PAGE LEFT BLANK INTENTIONALLY)

CITY OF SILVER BAY

MANAGEMENT'S DISCUSSION AND ANALYSIS December 31, 2012

MANAGEMENT'S DISCUSSION AND ANALYSIS (Pages 5 to 11 Unaudited)

This section of the City of Silver Bay's (the "City") annual financial report presents a discussion and analysis of the City's financial performance during the fiscal year ended December 31, 2012. Please read it in conjunction with the City's basic financial statements following this section. Comparative information from 2011 has been included as required.

FINANCIAL HIGHLIGHTS

- The net position of the City was \$ 12,476,771 in 2011 and \$ 13,528,118 in 2012. Of these amounts, \$ 3,885,879 in 2011 and \$ 4,305,828 in 2012 may be used to meet the City's ongoing obligations to citizens and creditors in accordance with the City's fund designations and fiscal policies.
- In 2011, the total net position increased by \$ 719,864. The majority of this increase was due to the development and construction of the Eco-Industrial Business Park and the Biofuel/Food Greenhouse Project. Other capital increases include the purchases of the following: 2012 Mack Snowplow and 2012 Ford F250 truck in the Street Department, 2011 Ford F150 truck, digital community event sign, digital scoreboard in the Park and Recreation Department, 2011 Ford Taurus in General Government, 2011 Ford Crown Victoria police car and solar radar sign within the Police Department and a hot water heater at the Mary MacDonald Business Center. In addition, boilers were replaced at the City Hall, Mary MacDonald Business Center and the Wastewater Treatment Facility. Capital decreases happened with the removal of the underground fuel tanks at the airport and the sale of assets in the Street Department, Water Department, General Government and Police Department. In 2012, the total net position increased by \$ 1,051,347. The majority of this increase was due to the development and construction of the Eco-Industrial Business Park and the Biofuel/Food Greenhouse Project. Other capital increases include the purchases of the following: 2012 Kubota Tractor in Parks and Recreation, a 2012 Kubota Lawn Tractor in Street Department, Police Department. Radar, and Liquor Store's ATM machine. In addition, a boiler was replaced at the Recreation Hall, zone valves were upgraded at the water plant, water repairs were made at the Library, an improvement was made to the City Wastewater Treatment Facility's primary clarifier and trickling filter and for a water pressure stabilization project for the City's Water System. Capital decreases happened with the sale of assets in the Park and Recreation Department, Mary MacDonald Business Center and Liquor Department.
- The City's governmental funds reported a combined ending fund balance in the amount of \$ 2,600,529 for 2011 and \$ 2,817,306 for 2012.
- At the end of the previous fiscal year, unreserved fund balance for the General Fund was \$ 1,351,684 (\$ 112,000 assigned and \$ 1,239,684 unassigned), or 78.4%, of total General Fund expenditures of \$ 1,724,365. At the end of the current fiscal year, the total fund balance for the General Fund was \$ 1,472,468 (\$ 112,000 assigned and \$ 1,360,468 unassigned), or 97.4%, of total General Fund expenditures of \$ 1,511,920.

CITY OF SILVER BAY
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2012

USING THE FINANCIAL SECTION OF THIS STATEMENT

This annual report consists of a series of 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. Fund financial statements are presented after the Statement of Activities. Fund financial statements report the City's operations in more detail than the government-wide statements by providing information about the City's funds.

STATEMENT OF NET POSITION AND STATEMENT OF ACTIVITIES

Our analysis of the City begins with the Statement of Net Position and the Statement of Activities. One of the most important questions asked about the City's finances is, "is the City as a whole better off or worse off as a result of the year's activities?" The Statement of Net Position and Statement of Activities report information about the City as a whole and about its activities in a way that helps answer this question. 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 revenues and expenses are taken into account regardless of when cash is received or paid.

These two Statements report the City's net position and changes in them. The City's net position, which is the difference between assets and liabilities, is one way to measure the City's financial health or financial position. Over time, increases or decreases in the City's net position are one indicator of whether its financial health is improving or deteriorating. You will need to consider other nonfinancial factors, however, to assess the overall health of the City.

FUND FINANCIAL STATEMENTS

Our analysis of the City's major funds begins with the fund financial statements and provides detailed information about the most 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 Council establishes other funds to help it control and manage money for particular purposes or to show it is meeting legal responsibilities for using certain taxes, grants and other money (like grants received). The City's two kinds of funds, governmental and proprietary, use different accounting approaches.

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 an accounting method called modified accrual accounting, which measures cash and all other financial assets that can readily be 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 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 reconciliations after the fund financial statements.

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 all activities are reported in the Statement of Net Position and Statement of Activities. In fact, the City's Enterprise Funds are the same as the business-type activities reported in the government-wide statements but provide more detail and additional information, such as cash flows, for proprietary funds.

CITY OF SILVER BAY

MANAGEMENT'S DISCUSSION AND ANALYSIS December 31, 2012

STATEMENT OF NET POSITION

The City's combined net position increased from a year ago. Our analysis below and on the next page focuses on the net position (Table 1) and changes in net position (Table 2) of the City's governmental and business-type activities.

	Governmental			Business-Type		
	Activities	Activities	Total	Activities	Activities	Total
	2011	2011	2011	2012	2012	2012
Current and Other Assets	\$ 3,089,803	\$ 1,622,995	\$ 4,712,798	\$ 3,228,978	\$ 1,825,891	\$ 5,054,869
Capital Assets	5,856,866	4,751,478	10,608,344	6,226,673	4,727,147	10,953,820
Total Assets	\$ 8,946,669	\$ 6,374,473	\$ 15,321,142	\$ 9,455,651	\$ 6,553,038	\$ 16,008,689
Current and Other Liabilities	\$ 434,379	\$ 312,580	\$ 746,959	\$ 372,657	\$ 326,931	\$ 699,588
Long-Term Liabilities	495,729	1,601,683	2,097,412	416,835	1,364,148	1,780,983
Total Liabilities	930,108	1,914,263	2,844,371	789,492	1,691,079	2,480,571
Net Position:						
Invested in Capital Assets, Net of						
Related Debt	5,364,109	2,942,874	8,306,983	5,817,931	3,151,213	8,969,144
Restricted	283,909	-	283,909	253,146	-	253,146
Unrestricted	2,368,543	1,517,336	3,885,879	2,595,082	1,710,746	4,305,828
Total Net Position	8,016,561	4,460,210	12,476,771	8,666,159	4,861,959	13,528,118
Total Liabilities and Net Position	\$ 8,946,669	\$ 6,374,473	\$ 15,321,142	\$ 9,455,651	\$ 6,553,038	\$ 16,008,689

GOVERNMENTAL ACTIVITIES

Total net position of the City's governmental activities increased in 2011 by \$ 524,389 or 7.0%, and increased in 2012 by \$ 649,598 or 8.1%. This change was primarily due to the construction for the new Biofuel/Food Greenhouse Project and the purchase and removal of various capital assets.

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, totaled \$ 2,368,543 in 2011 and \$ 2,595,082 in 2012. This is an increase of \$ 226,539 or 9.5%. This is mainly due to lower expenditures than anticipated, deferred revenues from FEMA for the 2012 Flood, and a large property insurance dividend.

Current and other assets totaled \$ 3,089,803 in 2011 and \$ 3,228,978 in 2012. Cash in the General Fund increased by \$ 45,469 in 2011 and increased by \$ 120,431 in 2012. The City experienced an increase in total revenues and a decrease in expenditures in the General Fund in 2012. The total increase in revenues was \$ 151,773 from the previous year and expenditures decreased \$ 212,445 from the previous year. The decrease in expenditures was due to a one-time adjustment for the changes in post retirement benefits and capital outlay for the purchase of the Mack snowplow truck and other capital assets in 2011.

Cash in the Public Works Reserve Fund decreased by \$ 547,395 in 2011 and increased by \$ 349,382 in 2012. In 2010, grant money was received for the Business Park and expended in 2011 and 2012. At fiscal year-end, \$ 47,526 was due from reimbursable grants for the construction of the Biofuel/Food Greenhouse Project. Additional funds were added from levy dollars for vehicle replacement plan and sidewalks; however, a majority of those funds were not expended.

CITY OF SILVER BAY

MANAGEMENT'S DISCUSSION AND ANALYSIS December 31, 2012

BUSINESS-TYPE ACTIVITIES

The net position of the City's business-type activities increased by \$ 195,475 in 2011 and increased by \$ 401,749 in 2012. The increase in 2011 and 2012 were due to the increase in charges for services and capital improvements for the year. The following table indicates the changes in net position for the City's governmental and business-type activities.

	Governmental Activities	Business-Type Activities	Total	Governmental Activities	Business-Type Activities	Total
	2011	2011	2011	2012	2012	2012
REVENUES:						
Program Revenues:						
Charges for Services	\$ 425,835	\$ 2,256,750	\$ 2,682,585	\$ 452,983	\$ 2,418,220	\$ 2,871,203
Operating Grants and Contributions	321,111	-	321,111	371,690	-	371,690
Capital Grants and Contributions	560,563	-	560,563	618,534	-	618,534
General Revenues:						
Property Taxes	744,649	-	744,649	928,690	-	928,690
Property Sales	19,928	-	19,928	3,292	-	3,292
State Aids	1,080,561	-	1,080,561	1,025,135	-	1,025,135
Other	46,372	1,223	47,595	51,460	3,172	54,632
Interest	16,834	8,359	25,193	12,016	8,718	20,734
Total Revenues	\$ 3,215,853	\$ 2,266,332	\$ 5,482,185	\$ 3,463,800	\$ 2,430,110	\$ 5,893,910
EXPENSES:						
General Services	\$ 494,810	\$ -	\$ 494,810	\$ 488,276	\$ -	\$ 488,276
Public Safety	637,741	-	637,741	570,068	-	570,068
Public Works	194,950	-	194,950	539,718	-	539,718
Culture and Recreation	1,033,233	-	1,033,233	1,007,102	-	1,007,102
Economic Development	157,567	-	157,567	39,660	-	39,660
Airport	155,595	-	155,595	149,035	-	149,035
Interest on Long-Term Debt	17,568	-	17,568	20,343	-	20,343
Water Utility	-	649,194	649,194	-	622,110	622,110
Sewer Utility	-	496,567	496,567	-	489,539	489,539
Municipal Liquor	-	925,096	925,096	-	916,712	916,712
Total Expenses	2,691,464	2,070,857	4,762,321	2,814,202	2,028,361	4,842,563
Change in Net Position before Transfers	524,389	195,475	719,864	649,598	401,749	1,051,347
Transfers	-	-	-	-	-	-
Change in Net Position	524,389	195,475	719,864	649,598	401,749	1,051,347
NET POSITION:						
Beginning of Year	7,492,172	4,264,735	11,756,907	8,016,561	4,460,210	12,476,771
End of Year	\$ 8,016,561	\$ 4,460,210	\$ 12,476,771	\$ 8,666,159	\$ 4,861,959	\$ 13,528,118

CITY OF SILVER BAY

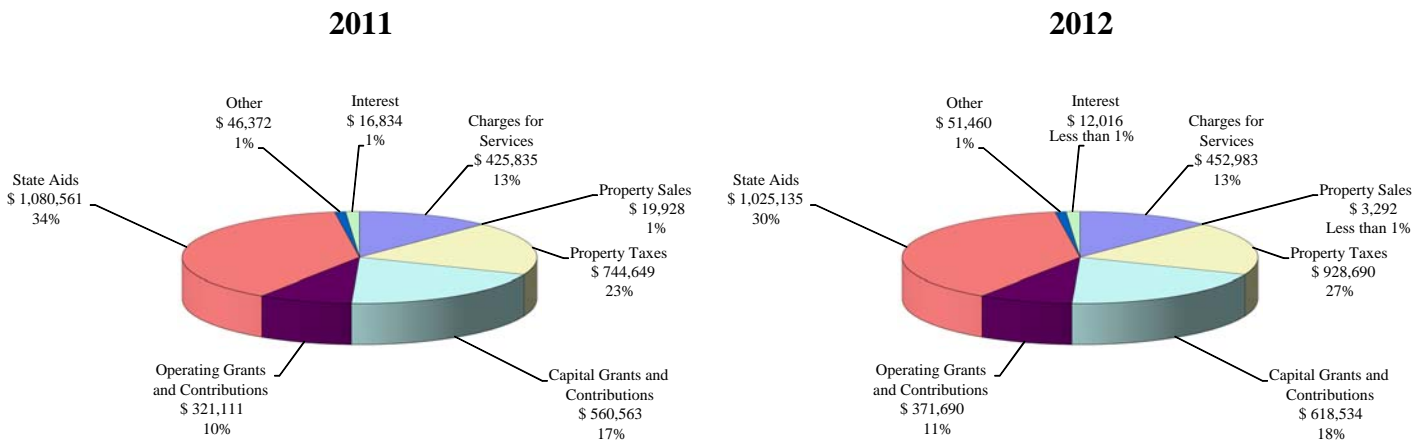
**MANAGEMENT’S DISCUSSION AND ANALYSIS
December 31, 2012**

GOVERNMENTAL ACTIVITIES

Revenues

The following chart visually illustrates the City’s revenue by source for its governmental activities:

REVENUE BY SOURCE – GOVERNMENTAL ACTIVITIES



Revenues for the City’s governmental activities totaled \$ 3,215,853 for 2011 and \$ 3,463,800 for 2012. The major components of these revenues are explained as follows:

Charges for services revenue totaled \$ 425,835 in 2011 and \$ 452,983 in 2012 and were collected through the Marina Fund and various recreation programs. Some fees come from public safety.

Capital grants and contributions totaled \$ 560,563 in 2011 and \$ 618,534 in 2012 and were used to fund the Eco-Industrial Park ongoing project and the construction of the Biofuel/Food Greenhouse Project. Minor grants were received for police equipment, the Mary MacDonald Playground project, Prairie Fire Theatre and for Eco-Park Development.

The City’s property tax and state aid revenues totaled \$ 1,825,210 and were 57% of the City’s total revenue in 2011. In 2012 they totaled \$ 1,953,825 and were 56% of the City’s total revenue. Included in these revenues are taconite state aids, Local Government Aid (LGA) and general property taxes. Taconite aids are generated by mining activities and allocated by the State of Minnesota based on various formulas.

Overall, interest revenue decreased significantly in 2011 due to interest rates falling throughout the year for City’s investments. In 2012, interest decreased again due to interest rates falling in the previous year and the interest rates remained at the all time low throughout the 2012 year.

CITY OF SILVER BAY
MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2012

GOVERNMENTAL ACTIVITIES

Expenses

The City's expenses for governmental activities totaled \$ 2,691,464 for 2011 and \$ 2,814,202 for 2012 and were consistent with budgeted expectations.

BUSINESS-TYPE ACTIVITIES

Revenues

The City's business-type revenues totaled \$ 2,266,332 for 2011 and \$ 2,430,110 for 2012. The Municipal Liquor Fund generated operating revenues of \$ 902,688 in 2011 and \$ 944,914 in 2012. Both water and sewer revenues significantly increased due to the changes in the rates that primarily affected metered accounts, which were in addition to the regularly scheduled rate increases. All business-types were affected from the loss in interest income.

Expenses

Business-type expenses totaled \$ 2,070,857 for 2011 and \$ 2,028,361 for 2012. The municipal liquor operating expenses increased at a rate of 4.8% for 2011 while the operating revenues decreased by less than 1%. In 2012, the operating expenses decreased at a rate of 0.9% while the operating revenues increased by a rate of 4.6%. As a result, an operating loss of \$ 7,309 happened in 2011 but an operating profit gain of \$ 41,349 happened in 2012. Expenses in the Water Utility Fund increased in 2011 to \$ 649,194 and in 2012, they decreased to \$ 622,110. Sewer expenses for 2011 were \$ 496,567, while 2012 expenses decreased to \$ 489,539.

FINANCIAL ANALYSIS OF THE CITY'S MAJOR FUNDS

General Fund

The City's 2011 General Fund balance was \$ 1,351,684. The City's General Fund balance increased by \$ 120,784 in 2012 to \$ 1,472,468.

Mary MacDonald Fund

The Mary MacDonald Fund balance for 2011 was \$ 129,288. The Mary MacDonald Fund balance increased by \$ 29,101, for an ending fund balance of \$ 158,389.

Debt Service Fund

The \$ 3,072 increase in this Fund's balance to \$ 41,952 was due to special assessment income.

Public Works Reserve

The Public Works Reserve Fund balance for 2011 was \$ 352,832. In 2012, the fund balance increased to \$ 400,185. The increase was a result of funding for the Business Park, vehicle replacement planning, sidewalks and from General Fund transfer of property tax to reimburse Bell Apartment Condemnation.

CITY OF SILVER BAY

MANAGEMENT'S DISCUSSION AND ANALYSIS December 31, 2012

GENERAL FUND BUDGETARY HIGHLIGHTS

Over the course of the year, the City Council reviewed and revised the City's General Fund budget to reflect current trends in operations.

CAPITAL ASSETS

At the end of 2011, the City had \$ 10,608,344 invested in a broad range of capital assets (refer to Note 4 for a schedule showing the City's capital asset activity). At the end of 2012, the City had \$ 10,953,820 invested in a broad range of capital assets. The City's fiscal year 2013 capital budget calls for continued spending for capital projects, including infrastructure, building renovations and future investments in technology and equipment.

LONG-TERM DEBT

At 2011 year-end, the City had \$ 2,526,720 in notes, leases and compensated absences outstanding. The majority, \$ 1,287,603, is related to utility loans from the State of Minnesota PFA Fund for capital improvements in the Water and Sewer Funds (refer to Note 6 for further information).

At 2012 year-end, the City had \$ 2,223,270 in notes, leases and compensated absences outstanding. The majority, \$ 1,128,565, is related to utility loans from the State of Minnesota PFA Fund for capital improvements in the Water and Sewer Funds (refer to Note 6 for further information).

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The City's appointed officials considered many factors when setting the fiscal year 2013 budget, rates and fees that will be charged for the general and business-type activities for the City. The major factor in the development of the 2013 budget was to prepare a balanced budget based upon historical trends, known future expectations, and estimated increases/decreases due to trends in the economy. The budget was prepared and analyzed by individual object codes.

The City's Public Utilities Commission adopted resolution P.U.C. 2007-#1 on May 21, 2007. The resolution allows the water and sewer rates charged by the City to have set increases with the first rate increase effective January 1, 2008 and respective rate and fee changes to be made effective each January 1 through and including January 1, 2016, for both residential and metered accounts. These rate increases were necessary to finance debt service for the debt issued in prior years by the Water and Sewer Funds. Effective June 1, 2011, water and sewer rates were adjusted (Resolution 2011-#13) and significantly affected metered accounts.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, customers, and creditors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the City of Silver Bay at 7 Davis Drive, Silver Bay, Minnesota 55614, (218) 226-4408.

(THIS PAGE LEFT BLANK INTENTIONALLY)

BASIC FINANCIAL STATEMENTS

CITY OF SILVER BAY

**STATEMENT OF NET POSITION
December 31, 2012**

	Governmental Activities	Business-Type Activities	Total
ASSETS			
Cash and Investments (Including Cash Equivalents)	\$ 2,769,968	\$ 1,563,222	\$ 4,333,190
Cash with Fiscal Agent	25,000	-	25,000
Property Tax Receivable	75,384	-	75,384
Accounts Receivable	4,418	107,548	111,966
Interest Receivable	1,701	1,119	2,820
Due from Other Governments	133,798	3,957	137,755
Loan Receivable	79,647	-	79,647
Special Assessments Receivable	139,062	-	139,062
Inventory	-	144,415	144,415
Prepaid Items	-	5,630	5,630
Capital Assets not being Depreciated:			
Land	905,793	37,463	943,256
Construction in Progress	19,006	133,418	152,424
Capital Assets being Depreciated:			
Buildings and Building Improvements	4,952,576	7,653,939	12,606,515
Improvements Other than Buildings	3,014,923	400,325	3,415,248
Vehicles, Machinery and Equipment	2,100,466	658,609	2,759,075
Less Accumulated Depreciation	<u>(4,766,091)</u>	<u>(4,156,607)</u>	<u>(8,922,698)</u>
 Total Assets	 <u>\$ 9,455,651</u>	 <u>\$ 6,553,038</u>	 <u>\$ 16,008,689</u>
LIABILITIES AND NET POSITION			
Liabilities			
Accounts Payable	\$ 17,710	\$ 5,326	\$ 23,036
Contracts Payable	-	5,967	5,967
Due to Other Governments	50	11,575	11,625
Salaries and Benefits Payable	50,068	18,989	69,057
Interest Payable	6,470	11,748	18,218
Unearned Revenue	129,398	-	129,398
Bond Principal Payable:			
Payable Within One Year	68,873	49,865	118,738
Payable After One Year	296,777	219,504	516,281
Notes Payable:			
Payable Within One Year	-	190,510	190,510
Payable After One Year	-	1,116,055	1,116,055
Capital Lease Payable:			
Payable Within One Year	19,566	-	19,566
Payable After One Year	23,526	-	23,526
Compensated Absences Payable:			
Payable Within One Year	80,522	32,951	113,473
Payable After One Year	96,532	28,589	125,121
Total Liabilities	<u>789,492</u>	<u>1,691,079</u>	<u>2,480,571</u>
 Net Position			
Net Investment in Capital Assets	5,817,931	3,151,213	8,969,144
Restricted	253,146	-	253,146
Unrestricted	2,595,082	1,710,746	4,305,828
Total Net Position	<u>8,666,159</u>	<u>4,861,959</u>	<u>13,528,118</u>
 Total Liabilities and Net Position	 <u>\$ 9,455,651</u>	 <u>\$ 6,553,038</u>	 <u>\$ 16,008,689</u>

The Notes to the Financial Statements are an integral part of this statement.

CITY OF SILVER BAY

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

Functions/Programs	Program Revenue			Net (Expense) Revenue and Changes in Net Assets			
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-Type Activities	Total
Governmental Activities							
General Government	\$ 488,276	\$ -	\$ 1,380	\$ -	\$ (486,896)	\$ -	\$ (486,896)
Public Safety	570,068	83,825	55,327	-	(430,916)	-	(430,916)
Public Works	539,718	3,719	29,605	8,070	(498,324)	-	(498,324)
Culture and Recreation	1,007,102	347,420	233,621	27,021	(399,040)	-	(399,040)
Economic Development	39,660	5,174	30,000	583,443	578,957	-	578,957
Airport	149,035	12,845	21,757	-	(114,433)	-	(114,433)
Interest on Long-Term Debt	20,343	-	-	-	(20,343)	-	(20,343)
Total Governmental Activities	<u>2,814,202</u>	<u>452,983</u>	<u>371,690</u>	<u>618,534</u>	<u>(1,370,995)</u>	<u>-</u>	<u>(1,370,995)</u>
Business-Type Activities							
Water	622,110	836,845	-	-	-	214,735	214,735
Sewer	489,539	636,461	-	-	-	146,922	146,922
Municipal Liquor	916,712	944,914	-	-	-	28,202	28,202
Total Business-Type Activities	<u>2,028,361</u>	<u>2,418,220</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>389,859</u>	<u>389,859</u>
Total Governmental and Business-Type Activities	<u>\$ 4,842,563</u>	<u>\$ 2,871,203</u>	<u>\$ 371,690</u>	<u>\$ 618,534</u>	<u>(1,370,995)</u>	<u>389,859</u>	<u>(981,136)</u>
General Revenues							
Property and Taconite Taxes					928,690	-	928,690
State Aids					1,025,135	-	1,025,135
Unrestricted Investment Earnings					12,016	8,718	20,734
Other General Revenue					51,460	3,172	54,632
Gain on Sale of Asset					3,292	-	3,292
Total General Revenues					<u>2,020,593</u>	<u>11,890</u>	<u>2,032,483</u>
Change in Net Position					<u>649,598</u>	<u>401,749</u>	<u>1,051,347</u>
Net Position - Beginning					<u>8,016,561</u>	<u>4,460,210</u>	<u>12,476,771</u>
Net Position - Ending					<u>\$ 8,666,159</u>	<u>\$ 4,861,959</u>	<u>\$ 13,528,118</u>

CITY OF SILVER BAY

BALANCE SHEET - GOVERNMENTAL FUNDS

December 31, 2012

		<u>Special Revenue</u>	<u>Debt Service</u>
		Mary MacDonald Business Center	Debt Service
	<u>General (101)</u>	<u>(265)</u>	<u>(352)</u>
ASSETS			
Cash and Investments	\$ 1,400,506	\$ 177,772	\$ 41,933
Cash with Fiscal Agent	-	-	-
Taxes Receivable - Delinquent	63,310	-	70
Special Assessment Receivable - Deferred	-	-	139,062
Accounts Receivable	659	2,830	-
Interest Receivable	888	127	20
Due from Other Funds	39,588	-	-
Due from Other Governments	86,257	15	-
Loan Receivable	41,002	-	-
	<u> </u>	<u> </u>	<u> </u>
Total Assets	<u>\$ 1,632,210</u>	<u>\$ 180,744</u>	<u>\$ 181,085</u>
LIABILITIES AND FUND BALANCES			
Liabilities			
Accounts Payable	\$ 1,238	\$ 13,450	\$ -
Due to Other Funds	-	-	-
Due to Other Governments	-	-	-
Salaries and Benefits Payable	36,946	-	-
Deferred Revenue	121,558	8,905	139,133
Total Liabilities	<u>159,742</u>	<u>22,355</u>	<u>139,133</u>
Fund Balances			
Nonspendable	-	-	-
Restricted	-	-	41,952
Committed	112,000	-	-
Assigned	-	158,389	-
Unassigned	1,360,468	-	-
Total Fund Balances	<u>1,472,468</u>	<u>158,389</u>	<u>41,952</u>
	<u> </u>	<u> </u>	<u> </u>
Total Liabilities and Fund Balances	<u>\$ 1,632,210</u>	<u>\$ 180,744</u>	<u>\$ 181,085</u>

Capital Projects

<u>Public Works Reserve (401)</u>	<u>Nonmajor Governmental Funds</u>	<u>Total Governmental Funds</u>
\$ 354,607	\$ 795,150	\$ 2,769,968
-	25,000	25,000
12,004	-	75,384
-	-	139,062
-	929	4,418
218	448	1,701
-	-	39,588
47,526	-	133,798
-	38,645	79,647
<u>\$ 414,355</u>	<u>\$ 860,172</u>	<u>\$ 3,268,566</u>
\$ 2,166	\$ 856	\$ 17,710
-	39,588	39,588
-	50	50
-	13,122	50,068
12,004	62,244	343,844
<u>14,170</u>	<u>115,860</u>	<u>451,260</u>
-	25,000	25,000
52,531	26,001	120,484
-	-	112,000
347,654	737,029	1,243,072
-	(43,718)	1,316,750
<u>400,185</u>	<u>744,312</u>	<u>2,817,306</u>
<u>\$ 414,355</u>	<u>\$ 860,172</u>	<u>\$ 3,268,566</u>

The Notes to the Financial Statements are an integral part of this statement.

(THIS PAGE LEFT BLANK INTENTIONALLY)

CITY OF SILVER BAY

**RECONCILIATION OF THE BALANCE SHEET TO
THE STATEMENT OF NET POSITION - GOVERNMENTAL FUNDS
December 31, 2012**

Total Fund Balances - Governmental Funds \$ 2,817,306

Amounts reported for governmental activities in the Statement of Net Position
are different because:

Capital assets used in governmental activities are not current financial resources
and, therefore, are not reported as assets in governmental funds.

Cost of Capital Assets	10,992,764
Less Accumulated Depreciation	(4,766,091)

Long-term liabilities, including bonds payable, are not due and payable in
the current period and, therefore, are not reported as liabilities in the funds.

Long-term liabilities at year-end consist of:

Bond Principal Payable	(365,650)
Capital Lease Payable	(43,092)
Compensated Absences Payable	(177,054)

Delinquent receivables will be collected in subsequent years, but are not
available soon enough to pay for the current period's expenditures and,
therefore, are deferred in the funds.

Property Taxes	75,384
----------------	--------

Revenues in the Statement of Activities that do not provide current
financial resources are not reported as revenues in the funds.

Deferred Special Assessments	139,062
------------------------------	---------

Governmental funds do not report a liability for accrued interest on long-term
debt until due and payable.

(6,470)

Total Net Position - Governmental Activities

\$ 8,666,159

CITY OF SILVER BAY

**STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS
For the Year Ended December 31, 2012**

		<u>Special Revenue</u>	<u>Debt Service</u>
		Mary MacDonald Business Center	Debt Service
	<u>General (101)</u>	<u>(265)</u>	<u>(352)</u>
REVENUES			
General Property Taxes	\$ 663,145	\$ -	\$ 18
Special Assessments	-	-	31,246
Licenses and Permits	15,411	-	-
Intergovernmental	1,083,161	599	-
Charges for Services	66,173	161,460	-
Fines and Forfeitures	6,060	-	-
Miscellaneous:			
Investment Income	6,424	1,003	147
Contributions and Donations	1,680	-	-
Loan Repayments	17,021	-	-
Other	28,593	5,207	-
Total Revenues	<u>1,887,668</u>	<u>168,269</u>	<u>31,411</u>
EXPENDITURES			
Current			
General Government	434,300	-	-
Public Safety	529,727	-	-
Public Works	470,546	-	-
Culture and Recreation	27,086	116,500	-
Economic Development	-	-	-
Airport	-	-	-
Debt Service			
Principal	18,398	-	65,617
Interest and Other Charges	3,024	-	18,643
Capital Outlay			
General Government	1,600	-	-
Public Safety	14,127	-	-
Public Works	13,112	-	-
Culture and Recreation	-	23,494	-
Economic Development	-	-	-
Total Expenditures	<u>1,511,920</u>	<u>139,994</u>	<u>84,260</u>
Excess of Revenues Over (Under) Expenditures	375,748	28,275	(52,849)
OTHER FINANCING SOURCES (USES)			
Proceeds from Sale of Capital Asset	-	826	-
Transfers In	13,112	-	55,921
Transfers Out	(268,076)	-	-
Total Other Financing Sources (Uses)	<u>(254,964)</u>	<u>826</u>	<u>55,921</u>
Net Change in Fund Balances	120,784	29,101	3,072
FUND BALANCES			
Beginning of Year	<u>1,351,684</u>	<u>129,288</u>	<u>38,880</u>
End of Year	<u>\$ 1,472,468</u>	<u>\$ 158,389</u>	<u>\$ 41,952</u>

Capital Projects

Public Works Reserve (401)	Nonmajor Governmental Funds	Total Governmental Funds
\$ 160,035	\$ 97,000	\$ 920,198
-	-	31,246
-	-	15,411
570,049	241,388	1,895,197
-	180,272	407,905
-	-	6,060
1,184	3,258	12,016
70,000	28,810	100,490
-	5,174	22,195
3,285	27,389	64,474
<u>804,553</u>	<u>583,291</u>	<u>3,475,192</u>
-	-	434,300
-	-	529,727
7,494	-	478,040
-	723,608	867,194
47,698	-	47,698
-	42,919	42,919
-	-	84,015
-	-	21,667
-	-	1,600
-	-	14,127
-	-	13,112
-	56,411	79,905
647,403	-	647,403
<u>702,595</u>	<u>822,938</u>	<u>3,261,707</u>
101,958	(239,647)	213,485
-	2,466	3,292
34,837	260,458	364,328
(89,442)	(6,810)	(364,328)
<u>(54,605)</u>	<u>256,114</u>	<u>3,292</u>
47,353	16,467	216,777
<u>352,832</u>	<u>727,845</u>	<u>2,600,529</u>
<u>\$ 400,185</u>	<u>\$ 744,312</u>	<u>\$ 2,817,306</u>

The Notes to the Financial Statements are an integral part of this statement.

CITY OF SILVER BAY

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES TO THE STATEMENT OF ACTIVITIES - GOVERNMENTAL FUNDS For the Year Ended December 31, 2012

Net Change in Fund Balances - Governmental Funds \$ 216,777

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

Capital outlays are reported in governmental funds as expenditures. However, in the Statement of Activities, the cost of those assets is allocated over the estimated useful lives and reported as depreciation expense.

Capital Outlays	740,512
Depreciation Expense	(369,701)
Loss on Disposal	(1,004)

Compensated absences are recognized as paid in the governmental funds but recognized as the expense is incurred in the Statement of Activities. (7,641)

Principal payments on long-term debt are recognized as expenditures in the governmental funds but as an increase in net position in the Statement of Activities. 84,015

Interest on long-term debt in the Statement of Activities differs from the amount reported in the governmental funds because interest is recognized as an expenditure in the funds when it is due and thus requires use of current financial resources. In the Statement of Activities, however, interest expense is recognized as the interest accrues, regardless of when it is due. 1,324

Revenues in the Statement of Activities that do not provide current financial resources are not reported as revenues in the funds.

Special Assessments Deferred	(23,176)
------------------------------	----------

Delinquent property taxes receivable will be collected in subsequent years, but are not available soon enough to pay for the current period's expenditures and, therefore, are deferred in the funds. 8,492

Change in Net Position - Governmental Activities \$ 649,598

CITY OF SILVER BAY
Lake County, Minnesota

**STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES -
BUDGET AND ACTUAL - GENERAL FUND
For the Year Ended December 31, 2012**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget - Over (Under)
	Original	Final		
REVENUES				
General Property Taxes	\$ 686,750	\$ 687,405	\$ 663,145	\$ (24,260)
Licenses and Permits	13,240	15,270	15,411	141
Intergovernmental	1,084,600	1,098,495	1,083,161	(15,334)
Charges for Services	36,825	42,000	66,173	24,173
Fines and Forfeitures	6,800	5,125	6,060	935
Miscellaneous:				
Investment Income	6,000	6,000	6,424	424
Contributions and Donations	1,000	1,600	1,680	80
Loan Repayments	17,020	17,020	17,021	1
Other	14,800	28,350	28,593	243
Total Revenues	1,867,035	1,901,265	1,887,668	(13,597)
EXPENDITURES				
Current				
General Government	468,500	435,500	434,300	(1,200)
Public Safety	529,975	531,340	529,727	(1,613)
Public Works	524,000	473,150	470,546	(2,604)
Culture and Recreation	18,900	27,200	27,086	(114)
Debt Service				
Principal	18,400	18,400	18,398	(2)
Interest and Other Charges	3,030	3,030	3,024	(6)
Capital Outlay				
General Government	2,500	1,650	1,600	(50)
Public Safety	8,100	14,200	14,127	(73)
Public Works	-	13,200	13,112	(88)
Total Expenditures	1,573,405	1,517,670	1,511,920	(5,750)
Excess of Revenues Over (Under) Expenditures	293,630	383,595	375,748	(7,847)
OTHER FINANCING SOURCES (USES)				
Transfers In	-	13,100	13,112	12
Transfers Out	(293,630)	(268,076)	(268,076)	-
Total Other Financing Sources (Uses)	(293,630)	(254,976)	(254,964)	12
Net Change in Fund Balances	\$ -	\$ 128,619	120,784	\$ (7,835)
FUND BALANCES				
Beginning of Year			1,351,684	
End of Year			\$ 1,472,468	

The Notes to the Financial Statements are an integral part of this statement.

CITY OF SILVER BAY
Lake County, Minnesota

**STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES -
BUDGET AND ACTUAL - MARY MACDONALD BUSINESS CENTER
For the Year Ended December 31, 2012**

	<u>Budgeted Amounts</u>		Actual Amounts	Variance with Final Budget - Over (Under)
	<u>Original</u>	<u>Final</u>		
REVENUES				
Intergovernmental	\$ -	\$ 570	\$ 599	\$ 29
Charges for Services	145,000	161,400	161,460	60
Miscellaneous:				
Investment Income	500	750	1,003	253
Other	-	5,190	5,207	17
Total Revenues	<u>145,500</u>	<u>167,910</u>	<u>168,269</u>	<u>359</u>
EXPENDITURES				
Current				
Park and Recreation	132,220	109,170	116,500	7,330
Capital Outlay				
Park and Recreation	<u>28,000</u>	<u>23,500</u>	<u>23,494</u>	<u>(6)</u>
Total Expenditures	<u>160,220</u>	<u>132,670</u>	<u>139,994</u>	<u>7,324</u>
Excess of Revenues Over (Under) Expenditures	(14,720)	35,240	28,275	(6,965)
OTHER FINANCING SOURCES				
Proceeds from Sale of Capital Asset	<u>-</u>	<u>825</u>	<u>826</u>	<u>1</u>
Net Change in Fund Balances	<u>\$ (14,720)</u>	<u>\$ 36,065</u>	29,101	<u>\$ (6,964)</u>
FUND BALANCES				
Beginning of Year			<u>129,288</u>	
End of Year			<u>\$ 158,389</u>	

CITY OF SILVER BAY

STATEMENT OF NET POSITION - PROPRIETARY FUNDS
December 31, 2012

	<u>Water (602)</u>	<u>Sewer (604)</u>	<u>Municipal Liquor Dispensary (609)</u>	<u>Total</u>
ASSETS				
Current Assets				
Cash and Investments (Including Cash Equivalents)	\$ 444,913	\$ 735,356	\$ 382,953	\$ 1,563,222
Accounts Receivable	53,481	52,283	1,784	107,548
Interest Receivable	293	550	276	1,119
Due from Other Governments	1,996	1,961	-	3,957
Inventory	66,881	9,873	67,661	144,415
Prepaid Items	-	-	5,630	5,630
Total Current Assets	<u>567,564</u>	<u>800,023</u>	<u>458,304</u>	<u>1,825,891</u>
Noncurrent Assets				
Capital Assets:				
Land	18,568	5,000	13,895	37,463
Buildings and Building Improvements	2,703,549	3,670,062	1,280,328	7,653,939
Improvements Other than Buildings	122,702	246,326	31,297	400,325
Vehicles, Machinery and Equipment	281,581	341,192	35,836	658,609
Construction in Progress	-	133,418	-	133,418
Total Capital Assets	<u>3,126,400</u>	<u>4,395,998</u>	<u>1,361,356</u>	<u>8,883,754</u>
Less Accumulated Depreciation	<u>(1,498,434)</u>	<u>(2,192,401)</u>	<u>(465,772)</u>	<u>(4,156,607)</u>
Net Capital Assets	<u>1,627,966</u>	<u>2,203,597</u>	<u>895,584</u>	<u>4,727,147</u>
Total Assets	<u>\$ 2,195,530</u>	<u>\$ 3,003,620</u>	<u>\$ 1,353,888</u>	<u>\$ 6,553,038</u>
LIABILITIES AND NET POSITION				
Current Liabilities				
Accounts Payable	\$ -	\$ 2,303	\$ 3,023	\$ 5,326
Contracts Payable	-	5,967	-	5,967
Due to Other Governments	5,422	-	6,153	11,575
Salaries and Benefits Payable	5,590	5,590	7,809	18,989
Interest Payable	5,574	4,261	1,913	11,748
Long-Term Liabilities Due Within One Year	78,927	123,437	70,962	273,326
Total Current Liabilities	<u>95,513</u>	<u>141,558</u>	<u>89,860</u>	<u>326,931</u>
Noncurrent Liabilities				
Compensated Absences	11,069	11,069	39,402	61,540
Notes Payable	804,000	502,565	-	1,306,565
Bonds Payable	-	-	269,369	269,369
Less Amount Due Within One Year	<u>(78,927)</u>	<u>(123,437)</u>	<u>(70,962)</u>	<u>(273,326)</u>
Total Noncurrent Liabilities	<u>736,142</u>	<u>390,197</u>	<u>237,809</u>	<u>1,364,148</u>
Total Liabilities	<u>831,655</u>	<u>531,755</u>	<u>327,669</u>	<u>1,691,079</u>
Net Position				
Net Investment in Capital Assets	823,966	1,701,032	626,215	3,151,213
Unrestricted	539,909	770,833	400,004	1,710,746
Total Net Position	<u>1,363,875</u>	<u>2,471,865</u>	<u>1,026,219</u>	<u>4,861,959</u>
Total Liabilities and Net Position	<u>\$ 2,195,530</u>	<u>\$ 3,003,620</u>	<u>\$ 1,353,888</u>	<u>\$ 6,553,038</u>

The Notes to the Financial Statements are an integral part of this statement.

CITY OF SILVER BAY

**STATEMENT OF REVENUES, EXPENSES AND CHANGES
IN NET POSITION - PROPRIETARY FUNDS
For the Year Ended December 31, 2012**

	<u>Water (602)</u>	<u>Sewer (604)</u>	<u>Municipal Liquor Dispensary (609)</u>	<u>Total</u>
SALES AND COST OF SALES				
Sales	\$ -	\$ -	\$ 934,085	\$ 934,085
Cost of Sales	-	-	570,871	570,871
Gross Profit	<u>-</u>	<u>-</u>	<u>363,214</u>	<u>363,214</u>
OPERATING REVENUES				
Charges for Services	830,440	629,479	-	1,459,919
Other Services	6,405	6,982	3,524	16,911
Game Machines	-	-	7,305	7,305
Total Operating Revenues	<u>836,845</u>	<u>636,461</u>	<u>10,829</u>	<u>1,484,135</u>
OPERATING EXPENSES				
Salaries and Benefits	229,537	222,383	233,922	685,842
Materials and Supplies	24,236	61,452	15,414	101,102
Professional Services	13,449	15,009	3,000	31,458
Contracted Services	32,034	18,293	-	50,327
Insurance	14,489	11,411	15,797	41,697
Utilities	74,759	22,773	14,229	111,761
Refuse Charges	158,794	662	1,066	160,522
Telephone	1,836	1,825	1,307	4,968
Depreciation	53,998	118,036	33,877	205,911
Promotion and Advertising	173	163	1,853	2,189
Licenses and Dues	1,684	1,748	2,329	5,761
Conferences and Schools	514	533	88	1,135
Miscellaneous Expenses	216	140	9,812	10,168
Total Operating Expenses	<u>605,719</u>	<u>474,428</u>	<u>332,694</u>	<u>1,412,841</u>
Operating Income	231,126	162,033	41,349	434,508
NONOPERATING REVENUES (EXPENSES)				
Investment Income	2,442	4,271	2,005	8,718
Miscellaneous Revenue	1,586	1,586	-	3,172
Interest Expense	(16,391)	(15,111)	(13,147)	(44,649)
Total Nonoperating Revenues (Expenses)	<u>(12,363)</u>	<u>(9,254)</u>	<u>(11,142)</u>	<u>(32,759)</u>
Change in Net Position	218,763	152,779	30,207	401,749
NET POSITION				
Beginning of Year	<u>1,145,112</u>	<u>2,319,086</u>	<u>996,012</u>	<u>4,460,210</u>
End of Year	<u>\$ 1,363,875</u>	<u>\$ 2,471,865</u>	<u>\$ 1,026,219</u>	<u>\$ 4,861,959</u>

CITY OF SILVER BAY

**STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS
For the Year Ended December 31, 2012**

	Water (602)	Sewer (604)	Municipal Liquor Dispensary (609)	Total
CASH FLOWS - OPERATING ACTIVITIES				
Receipts from Customers and Users	\$ 810,279	\$ 605,742	\$ 943,280	\$ 2,359,301
Payments to Suppliers	(347,298)	(133,938)	(636,272)	(1,117,508)
Payments to Employees	(226,810)	(219,656)	(232,830)	(679,296)
Net Cash Flows - Operating Activities	<u>236,171</u>	<u>252,148</u>	<u>74,178</u>	<u>562,497</u>
CASH FLOWS - NONCAPITAL FINANCING ACTIVITIES				
Miscellaneous Revenue	1,586	1,586	-	3,172
CASH FLOWS - CAPITAL AND RELATED FINANCING ACTIVITIES				
Principal Paid on Debt	(72,000)	(112,838)	(47,832)	(232,670)
Interest Paid on Debt	(16,939)	(16,131)	(13,481)	(46,551)
Acquisition of Capital Assets	(51,276)	(121,842)	(2,495)	(175,613)
Net Cash Flows - Capital and Related Financing Activities	<u>(140,215)</u>	<u>(250,811)</u>	<u>(63,808)</u>	<u>(454,834)</u>
CASH FLOWS - INVESTING ACTIVITIES				
Interest and Dividends Received	<u>2,591</u>	<u>4,868</u>	<u>2,433</u>	<u>9,892</u>
Net Change in Cash and Cash Equivalents	100,133	7,791	12,803	120,727
CASH AND CASH EQUIVALENTS				
Beginning of Year	<u>344,780</u>	<u>727,565</u>	<u>370,150</u>	<u>1,442,495</u>
End of Year	<u><u>\$ 444,913</u></u>	<u><u>\$ 735,356</u></u>	<u><u>\$ 382,953</u></u>	<u><u>\$ 1,563,222</u></u>
RECONCILIATION OF OPERATING INCOME TO NET CASH FLOWS - OPERATING ACTIVITIES				
Operating Income	\$ 231,126	\$ 162,033	\$ 41,349	\$ 434,508
Adjustments to Reconcile Operating Income to Net Cash Flows - Operating Activities:				
Depreciation Expense	53,998	118,036	33,877	205,911
Accounts Receivable	(25,888)	(30,014)	(1,634)	(57,536)
Due from Other Governments	(678)	(705)	-	(1,383)
Prepaid Items	-	-	(220)	(220)
Inventory	(24,424)	174	46	(24,204)
Accounts Payable	(644)	(103)	23	(724)
Due to Other Governmental Units	(46)	-	(355)	(401)
Salaries Payable	243	243	466	952
Compensated Absences Payable	2,484	2,484	626	5,594
Total Adjustments	<u>5,045</u>	<u>90,115</u>	<u>32,829</u>	<u>127,989</u>
Net Cash Flows - Operating Activities	<u><u>\$ 236,171</u></u>	<u><u>\$ 252,148</u></u>	<u><u>\$ 74,178</u></u>	<u><u>\$ 562,497</u></u>

(THIS PAGE LEFT BLANK INTENTIONALLY)

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS December 31, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The City of Silver Bay is a statutory city governed by an elected mayor and four council members. The accompanying financial statements present the government entities for which the government is considered to be financially accountable.

The financial statements present the City and its component units. The City includes all funds, account groups, organizations, institutions, agencies, departments and offices that are not legally separate from such. Component units are legally separate organizations for which the elected officials of the City are financially accountable and are included within the basic financial statements of the City because of the significance of their operational or financial relationships with the City.

The City is considered financially accountable for a component unit if it appoints a voting majority of the organization's governing body and it is able to impose its will on the organization by significantly influencing the programs, projects, activities or level of services performed or provided by the organization or there is a potential for the organization to provide specific financial benefits to or impose specific financial burdens on the City.

As a result of applying the component unit definition criteria above, certain organizations have been defined and are presented in this report as follows:

Blended Component Units – Reported as if they were part of the City.

Related Organization – The relationship of the City with the entity is disclosed.

For each of the categories above, the specific entities are identified as follows:

1. Blended Component Unit

The Silver Bay Economic Development Authority (EDA) is a legal entity separate from the City. Although legally separate, the Silver Bay EDA is reported as if it were part of the primary government because members of its governing body are appointed by the governing body of the primary government and it provides services exclusively for the City.

2. Related Organization

The Silver Bay Fire Relief Association (the "Association") is organized as a nonprofit organization, legally separate from the City, by its members to provide pension and other benefits to such members in accordance with *Minnesota Statutes*. Its Board of Trustees is appointed by the membership of the Association and not by the City Council. All funding is conducted in accordance with *Minnesota Statutes*, whereby state aid flows to the Association, tax levies are determined by the Association and are only reviewed by the City and the Association pays benefits directly to its members. Because the Association is fiscally independent of the City, the financial statements of the Association have not been included within the City's reporting entity.

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS December 31, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

B. Government-Wide and Fund 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 nonfiduciary activities of the City. 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 is offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Interest on general long-term debt is considered an indirect expense and is reported separately in the Statement of Activities. Program revenues include 1) charges to customers or applicants who purchase, use or directly benefit from goods, services or privileges provided by a 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 are not included among program revenues; instead, they are properly reported as general revenues. Internally dedicated revenues are reported as general revenues rather than program revenues.

Separate financial statements are provided for governmental funds and proprietary funds. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

C. Measurement Focus, Basis of Accounting and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the City considers revenues to be available if they are collected within 60 days of the end of the current period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes, franchise taxes, licenses and interest associated with the current period are all considered to be susceptible to accrual and so have been recognized as revenues of the current period. Only the portion of special assessments receivable due within the current period is considered to be susceptible to accrual as revenue of the current period. All other revenue items are considered to be measurable and available only when cash is received by the City.

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS December 31, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

C. Measurement Focus, Basis of Accounting and Financial Statement Presentation (Continued)

Description of Funds:

Major Governmental Funds:

General Fund – This Fund is the City’s primary operating fund. It accounts for all financial resources of the general City, except those required to be accounted for in another fund.

Mary MacDonald Business Center Special Revenue Fund – This Fund accounts for financial resources to be used for the rehabilitation and operation of the Mary MacDonald building. The main revenue source for this fund is grants and charges for services.

Debt Service Fund – This Fund accounts for the resources accumulated and payments made for principal and interest on governmental activities long-term debt.

Public Works Reserve Capital Projects Fund – This Fund accounts for the resources accumulated and payments made for five individual departments. One of the departments is the General Revenue Reserve Fund established pursuant to the provision of the Laws of Minnesota 1971, Chapter 440, also known as the Taconite Reserve Account. The other four departments within the Public Works Reserve Fund are as follows: Business Park, Bell Circle Apartments, Special Projects and Sidewalk Improvements.

Proprietary Funds:

Water Fund – This Fund accounts for the operations of the City’s water utility.

Sewer Fund – This Fund accounts for the operations of the City’s sewer utility.

Municipal Liquor Dispensary Fund – This Fund accounts for the operations of the City’s Municipal Liquor Store.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the GASB. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The City has elected not to follow subsequent private-sector guidance.

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are charges between the City’s sewer function and various other functions of the City. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS December 31, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

C. Measurement Focus, Basis of Accounting and Financial Statement Presentation (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 Municipal Liquor Dispensary, Water and Sewer Enterprise Funds are charges to customers for sales and services. Operating expenses for enterprise 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.

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. When committed, assigned or unassigned resources are available for use, it is the City's policy to first use committed resources, then assigned and the unassigned resources as they are needed.

D. Assets, Liabilities and Net Position or Fund Balance

1. Cash and Investments

The City's cash and cash equivalents are considered to be cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition. Investments are stated at fair value.

Minnesota Statutes authorize the City to invest in obligations of the U.S. Treasury, agencies and instrumentalities, shares of investment companies whose only investments are in the aforementioned securities, obligations of the State of Minnesota or its municipalities, bankers' acceptances, future contracts, repurchase and reverse repurchase agreements and commercial paper of the highest quality with a maturity of no longer than 270 days and in the Minnesota Municipal Investment Pool.

The Minnesota Municipal Investment Pool is an external investment pool not registered with the Securities Exchange Commission (SEC) that follows the same regulatory rules of the SEC under Rule 2.a.7. The fair value of the position in the pool is the same as the value of the pool shares.

Cash and investments at December 31, 2012, were comprised of deposits, including certificates of deposit at a commercial bank and a federal credit union, brokered certificates of deposit and shares in the Minnesota Municipal Money Market (4M Fund). The City has formal policies in place specifically to address the following risks related to deposits and investments.

Custodial Credit Risk – Deposits: In the case of deposits, this is the risk that in the event of a bank failure, the City's deposits may not be returned to it. *Minnesota Statutes* require all deposits be protected by federal deposit insurance, corporate surety bonds or collateral. The market value of collateral pledged must equal 110% of the deposits not covered by Federal Deposit Insurance Corporation (FDIC) insurance or corporate surety bonds. The City's investment policy requires the City to obtain collateral or bond for all uninsured amounts on deposit.

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS December 31, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

D. Assets, Liabilities and Net Position or Fund Balance (Continued)

1. Cash and Investments (Continued)

Interest Rate Risk: This is the risk that market values of securities in a portfolio would decrease due to changes in market interest rates. The City's investment policy states the City will minimize interest rate risk by structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations.

Credit Risk: This is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. *Minnesota Statutes* 118A.04 and 118A.05 limit investments in the top two ratings issued by nationally recognized statistical rating organizations. The City's investment policy limits its investments to those specified in these Statutes.

Concentration of Credit Risk: This is the risk of loss attributed to the magnitude of an investment in a single issuer. Investments should be diversified to avoid incurring unreasonable risks inherent in over investing in specific instruments, individual financial institutions or maturities. The City's investment policy states funds should be diversified according to type and maturity and the portfolio should contain both short-term and long-term investments.

Custodial Credit Risk – Investments: For an investment, this 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 collateral securities that are in the possession of an outside party. The City's investment policy states investment securities will be collateralized.

2. Receivables and Payables

All trade and property tax receivables are shown at a gross amount since both are assessable to the property taxes and are collectible upon the sale of the property.

The City levies its property tax for the subsequent year during the month of December. December 28 is the last day the City can certify a tax levy to the County Auditor for collection the following year. Such taxes become a lien on January 1 and are recorded as receivables by the City at that date. The property tax is recorded as revenue when it becomes measurable and available. Lake County is the collecting agency for the levy and remits the collections to the City three times a year. The tax levy notice is mailed in March with the first half of the payment due on May 15 and the second half due on October 15. Taxes not collected as of December 31 each year are shown as delinquent taxes receivable.

The County Auditor prepares the tax list for all taxable property in the City, applying the applicable tax rate to the tax capacity of individual properties, to arrive at the actual tax for each property. The County Auditor also collects all special assessments, except for certain prepayments paid directly to the City.

The City submits the list of taxes and special assessments to be collected on each parcel of property to the County Treasurer in January of each year.

CITY OF SILVER BAY

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

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

D. Assets, Liabilities and Net Position or Fund Balance (Continued)

3. Inventory and Prepaid Items

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.

Inventory is valued at cost using the first in, first out (FIFO) method. Inventories of governmental funds are recorded as expenditures when consumed rather than when purchased.

4. Capital Assets

Capital assets, which include property, plant, equipment and infrastructure assets (e.g., roads, sidewalks and similar items), are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets are defined by the City as assets with an initial, individual cost of more than \$ 2,000. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized.

Property, plant and equipment of the City are depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Buildings	40
Building Improvements	5-20
Furniture and Equipment	5-10
Light Vehicles	5
Machinery and Equipment	5-10
Fire Trucks	20
Infrastructure	20-70

5. Compensated Absences

City employees earn vacation time based on years of City service with a maximum of two weeks of vacation time to be carried over from one year to the next. City employees also earn sick leave based on years of City service with a maximum of 960 hours of sick leave to be carried over from one year to the next with any additional hours banked for long-term illness.

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS

December 31, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

D. Assets, Liabilities and Net Position or Fund Balance (Continued)

5. Compensated Absences (Continued)

For department heads that separate in good standing, compensated absences payable is calculated as 50%, 60% or 75% of unused sick leave (maximum 960 hours) for 10+ years, 15+ years or 25+ years of service, respectively, plus 15% of banked sick leave (excess of 960 hours) and all unused vacation at the employees current rate of pay. For department heads who retire, compensated absences payable is calculated as 50%, 75% or 100% of unused sick leave (maximum 960 hours) for 10+ years, 15+ years or 25+ years of service, respectively, plus 15% of banked sick leave (excess over 960 hours) and all unused vacation at the employee's current rate of pay. For department heads with fewer than 10 years of service, compensated absences payable is calculated as 50% of unused sick leave (maximum 960 hours), plus 10% of banked sick leave (excess over 960 hours) regardless of whether the employee is retiring or leaving in good standing.

Vacation and sick leave payable are recorded as expenditures or expenses when used in the governmental funds and as earned in the proprietary funds.

6. Employment Health Benefits

Employees will receive a \$ 200 contribution to a Health Savings Account (HSA) every month once they have been employed by the City for 15 years. The maximum amount contributed to the employee's HSA will be \$ 24,000, meaning they can receive contributions for 10 years after reaching the minimum 15 years of employment. Employees who had already been working for the City for at least 15 years as of January 1, 2011 received a lump sum contribution to their HSA, equal to the number of months they have worked for the City in excess of the 15 year minimum, multiplied by \$ 200 per month. Employees who started at the City after January 1, 2011, are not eligible for this benefit.

7. Long-Term Obligations

In the government-wide financial statements and proprietary fund types in the fund 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.

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.

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS December 31, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

D. Assets, Liabilities and Net Position or Fund Balance (Continued)

8. Fund Balance

A. Classification

In the fund financial statements, governmental funds report fund classifications that comprise a hierarchy based primarily on the extent to which the City is bound to honor constraints on the specific purpose for which amounts in those funds can be spent.

- Nonspendable Fund Balance – These are amounts that cannot be spent because they are not in spendable form or are legally or contractually required to be maintained intact.
- Restricted Fund Balance – These are amounts that are restricted to specific purposes either by a) constraints placed on the use of resources by creditors, grantors, contributors or laws or regulations of other governments or b) imposed by law through enabling legislation.
- Committed Fund Balances – These are amounts comprised of unrestricted funds used for a specific purpose pursuant to constraints imposed by formal action of the City Council and that remain binding unless removed by the City Council by subsequent formal action.
- Assigned Fund Balance – These are amounts that are constrained by the City's intent to be used for specific purposes but are neither restricted nor committed and include all remaining amounts (except for negative balances) that are reported in governmental funds, other than the General Fund, that are not classified as nonspendable, restricted or committed. The City Council has delegated authority to assign and remove fund balance assignments to the City Administrator and/or Deputy Clerk.
- Unassigned Fund Balance – These are residual amounts in the General Fund not reported in any other classification. The General Fund is the only fund that can report a positive unassigned fund balance. Other funds would report a negative unassigned fund balance should the total of nonspendable, restricted and committed fund balances exceed the total net resources of that fund.

B. Minimum Fund Balance

The City's target General Fund balance is to maintain 30%-50% of the next year's budgeted General Fund expenditures; however, this need could fluctuate with each year's budget objectives.

9. Net Position

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 statements when there are limitations on their use through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS December 31, 2012

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

D. Assets, Liabilities and Net Position or Fund Balance (Continued)

10. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenue and expenditures/expense during the reporting period. Actual results could differ from those estimates.

NOTE 2 – STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgetary Information

1. In August of each year, City staff submits to the City Council, a proposed operating budget for the year commencing the following January 1. The operating budget includes proposed expenditures and the means of financing them for the upcoming year.
2. Public hearings are conducted to obtain taxpayer comments.
3. The budget is legally enacted through passage of a resolution after obtaining taxpayer comments.
4. Budgets for the governmental funds are adopted on a basis consistent with accounting principles generally accepted in the United States of America.
5. Expenditures may not legally exceed budgeted appropriations at the department level. No fund's budget can be increased without City Council approval. The City Council may authorize transfer of budgeted amounts between departments within any fund. Management may amend budgets within a department level, so long as the total department budget is not changed.
6. Annual appropriated budgets are adopted during the year for the General and Special Revenue Funds.
7. Budgeted amounts are as originally adopted or as amended by the City Council. Individual amendments were not material in relation to the original amounts budgeted. Budgeted expenditure appropriations lapse at year-end.

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS
December 31, 2012

NOTE 2 – STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

B.Excess of Expenditures Over Appropriations

For the year ended December 31, 2012, expenditures exceeded appropriations in the following Funds:

	<u>Expenditures</u>	<u>Appropriations</u>
Major Fund:		
Mary MacDonald Business Center	\$ 139,994	\$ 132,670
Nonmajor Fund:		
Arena	192,209	189,675

C.Deficit Fund Balances

The following Funds had deficit fund balances at December 31, 2012:

Special Revenue:		
Airport		\$ 39,619
Marina		4,099

NOTE 3 – DEPOSITS AND INVESTMENTS

A. Deposits

In accordance with applicable *Minnesota Statutes*, the City maintains deposits at depository banks authorized by the City Council.

Custodial Credit Risk – Deposits: As of December 31, 2012, the City’s bank balance was not exposed to custodial credit risk because it was insured through FDIC and fully collateralized with securities held by the pledging financial institution’s trust department or agent and in the City’s name.

As of December 31, 2012, the City had the following deposits:

Cash and Cash Equivalents	\$ 1,964,711
Certificates of Deposit	<u>1,600,000</u>
 Total Deposits	 <u><u>\$ 3,564,711</u></u>

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS

December 31, 2012

NOTE 3 – DEPOSITS AND INVESTMENTS

B. Investments

As of December 31, 2012, the City had the following investments:

<u>Investment</u>	<u>Maturity</u>	<u>Fair Value</u>	<u>Percentage of Total</u>	<u>Type</u>
4M Money Market	Various	\$ 183,079	23.38%	MM
Goldman Sachs Bank, New York	10/25/13	100,000	12.77%	CD
Discover Bank, Delaware	10/25/13	100,000	12.77%	CD
Discover Bank, Delaware	12/02/13	100,000	12.77%	CD
Ally Bank, VT	06/27/13	100,000	12.77%	CD
State Bank of India, Illinois	08/04/13	100,000	12.77%	CD
State Bank of India, Illinois	11/23/13	100,000	12.77%	CD
 Total		<u>\$ 783,079</u>	<u>100.00%</u>	

Credit Risk: As of December 31, 2012, the City was not exposed to credit risk as the City's investments were comprised of brokered certificates of deposit and investments in the 4M Money Market Fund which do not receive independent credit ratings.

Concentration of Credit Risk – Investments: As indicated by the table above, the City has more than 5% of total investments in any one issuer; therefore, the investments were exposed to concentration of credit risk at December 31, 2012.

The following is a summary of total deposits and investments.

Deposits (Note 3.A.)	\$ 3,564,711
Petty Cash	10,400
Investments	<u>783,079</u>
 Total Deposits and Investments	<u><u>\$ 4,358,190</u></u>

Deposits and investments are presented in the December 31, 2012 basic financial statements as follows:

Statement of Net Position:	
Cash and Investments	\$ 4,333,190
Cash with Fiscal Agent	<u>25,000</u>
 Total	<u><u>\$ 4,358,190</u></u>

CITY OF SILVER BAY

NOTES TO THE 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>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Governmental Activities:				
Capital Assets not being Depreciated:				
Land	\$ 905,793	\$ -	\$ -	\$ 905,793
Construction in Progress	729,061	674,447	1,384,502	19,006
Total Capital Assets not being Depreciated	<u>1,634,854</u>	<u>674,447</u>	<u>1,384,502</u>	<u>924,799</u>
Capital Assets being Depreciated:				
Buildings and Building Improvements	3,568,074	1,384,502	-	4,952,576
Improvements Other than Buildings	3,014,923	-	-	3,014,923
Vehicles, Machinery and Equipment	2,053,244	66,065	18,843	2,100,466
Total Capital Assets being Depreciated	<u>8,636,241</u>	<u>1,450,567</u>	<u>18,843</u>	<u>10,067,965</u>
Less Accumulated Depreciation for:				
Buildings and Building Improvements	1,629,994	102,646	-	1,732,640
Improvements Other than Buildings	1,431,804	140,480	-	1,572,284
Vehicles, Machinery and Equipment	1,352,431	126,575	17,839	1,461,167
Total Accumulated Depreciation	<u>4,414,229</u>	<u>369,701</u>	<u>17,839</u>	<u>4,766,091</u>
Total Capital Assets being Depreciated, Net	<u>4,222,012</u>	<u>1,080,866</u>	<u>1,004</u>	<u>5,301,874</u>
Governmental Activities Capital Position, Net	<u>\$ 5,856,866</u>	<u>\$ 1,755,313</u>	<u>\$ 1,385,506</u>	<u>\$ 6,226,673</u>

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS
December 31, 2012

NOTE 4 – CAPITAL ASSETS

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Business-Type Activities:				
Capital Assets not being Depreciated:				
Land	\$ 37,463	\$ -	\$ -	\$ 37,463
Construction in Progress	<u>5,609</u>	<u>127,809</u>	<u>-</u>	<u>133,418</u>
Total Capital Assets not being Depreciated	<u>43,072</u>	<u>127,809</u>	<u>-</u>	<u>170,881</u>
Capital Assets being Depreciated:				
Buildings and Building Improvements	7,653,939	-	-	7,653,939
Improvements Other than Buildings	400,325	-	-	400,325
Vehicles, Machinery and Equipment	<u>622,259</u>	<u>53,771</u>	<u>17,421</u>	<u>658,609</u>
Total Capital Assets being Depreciated	<u>8,676,523</u>	<u>53,771</u>	<u>17,421</u>	<u>8,712,873</u>
Less Accumulated Depreciation for:				
Buildings and Building Improvements	3,329,843	177,291	-	3,507,134
Improvements Other than Buildings	111,001	7,789	-	118,790
Vehicles, Machinery and Equipment	<u>527,273</u>	<u>20,831</u>	<u>17,421</u>	<u>530,683</u>
Total Accumulated Depreciation	<u>3,968,117</u>	<u>205,911</u>	<u>17,421</u>	<u>4,156,607</u>
Total Capital Assets being Depreciated, Net	<u>4,708,406</u>	<u>(152,140)</u>	<u>-</u>	<u>4,556,266</u>
Business-Type Activities Capital Position, Net	<u>\$ 4,751,478</u>	<u>\$ (24,331)</u>	<u>\$ -</u>	<u>\$ 4,727,147</u>

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

Governmental Activities:	
General Government	\$ 50,583
Public Safety	29,544
Public Works	63,449
Culture and Recreation	120,009
Airport	<u>106,116</u>
Total Depreciation Expense - Governmental Activities	<u>\$ 369,701</u>
Business-Type Activities:	
Water	\$ 53,998
Sewer	118,036
Municipal Liquor Dispensary	<u>33,877</u>
Total Depreciation Expense - Business-Type Activities	<u>\$ 205,911</u>

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS
December 31, 2012

NOTE 5 – INTERFUND BALANCES AND TRANSFERS

A. Interfund Receivables and Payables

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

	Amounts Due to Other Funds
	Nonmajor Governmental Funds
Amounts Due from Other Funds:	
General Fund	\$ 39,588

The interfund balances exist to cover cash deficits in the various funds.

B. Transfers

The composition of interfund transfers as of December 31, 2012 was as follows:

	Transfers In				Total
	General Fund	Debt Service	Public Works Reserve	Nonmajor Governmental Funds	
Transfers Out:					
General Fund	\$ -	\$ -	\$ 34,837	\$ 233,239	\$ 268,076
Public Works Reserve	13,112	55,921	-	20,409	89,442
Nonmajor Governmental Funds	-	-	-	6,810	6,810
Total	\$ 13,112	\$ 55,921	\$ 34,837	\$ 260,458	\$ 364,328

The purpose of the above transfers was to assist with operating costs, move Bell Circle Apartment tax revenue to the Public Works Reserve Fund, capital purchases and debt service payments.

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS

December 31, 2012

NOTE 6 – LONG-TERM DEBT

A. Components of Long-Term Liabilities

	<u>Issue Date</u>	<u>Interest Rates</u>	<u>Original Issue</u>	<u>Final Maturity</u>	<u>Principal Outstanding</u>	<u>Due Within One Year</u>
Long-Term Liabilities:						
Governmental Activities:						
G.O. Bonds:						
G.O. Improvement Bond, Series 2008A	05/14/08	4.92%	\$ 221,000	01/15/19	\$ 155,654	\$ 20,827
G.O. Equipment Certificate 2010	04/30/10	3.75%	109,042	04/30/15	67,817	21,779
G.O. Equipment Certificate 2011	11/01/11	3.75%	167,000	12/01/17	<u>142,179</u>	<u>26,267</u>
Total G.O. Bonds					<u>365,650</u>	<u>68,873</u>
Capital Lease Obligations					43,092	19,566
Compensated Absences					<u>177,054</u>	<u>80,522</u>
Total Governmental Activities					585,796	168,961
Business-Type Activities:						
G.O. Revenue Notes/Bonds:						
G.O. Sewer Revenue Note of 1994	09/23/94	2.82%	1,490,796	02/20/16	324,565	89,510
G.O. Water Revenue Note of 1998	11/19/98	2.56%	642,000	08/20/18	237,000	37,000
G.O. Water Revenue Note of 2007	06/04/07	1.65%	726,450	08/20/26	567,000	36,000
Municipal Liquor Store Revenue Bond of 2008	05/01/08	Variable*	500,000	10/31/17	269,369	49,865
G.O. Sewer Revenue Note Series 2011A	10/17/11	2.60%	203,800	10/17/18	<u>178,000</u>	<u>28,000</u>
Total G.O. Revenue Notes/ Bonds					1,575,934	240,375
Compensated Absences					<u>61,540</u>	<u>32,951</u>
Total Business-Type Activities					<u>1,637,474</u>	<u>273,326</u>
Total all Long-Term Liabilities					<u>\$ 2,223,270</u>	<u>\$ 442,287</u>

*The Municipal Liquor Store Revenue Bond shall bear interest at the annual rate of 4.25% for the first five years of its term. On October 13, 2013, the annual rate of interest on the Bond shall be adjusted to a rate per annum equal to the sum of 1.41% and the five year Treasury Rate in effect on that date; however, in no event shall the adjusted rate be less than 4% or greater than 8% per annum.

Long-term bonded indebtedness listed above was issued to finance acquisition and construction of capital facilities and equipment.

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS
December 31, 2012

NOTE 6 – LONG-TERM DEBT

B. Minimum Debt Payments

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

<u>Year Ending December 31,</u>	Governmental Activities		
	Improvement Bonds		
	Principal	Interest	Total
2013	\$ 20,827	\$ 7,511	\$ 28,338
2014	21,879	6,459	28,338
2015	22,984	5,354	28,338
2016	24,134	4,204	28,338
2017	25,364	2,974	28,338
2018-2019	40,466	2,041	42,507
Total	\$ 155,654	\$ 28,543	\$ 184,197
<u>Year Ending December 31,</u>	Equipment Certificates		
	Principal	Interest	Total
	2013	\$ 48,046	\$ 7,875
2014	49,847	6,073	55,920
2015	51,716	4,204	55,920
2016	29,334	2,264	31,598
2017	31,053	1,164	32,217
Total	\$ 209,996	\$ 21,580	\$ 231,576
<u>Year Ending December 31,</u>	Business-Type Activities		
	Revenue Notes/Bonds		
	Principal	Interest	Total
2013	240,375	39,843	\$ 280,218
2014	247,036	32,913	279,949
2015	255,860	25,765	281,625
2016	212,833	18,368	231,201
2017	166,830	12,854	179,684
2018-2022	277,000	26,383	303,383
2023-2026	176,000	7,309	183,309
Total	\$ 1,575,934	\$ 163,435	\$ 1,739,369

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS
December 31, 2012

NOTE 6 – LONG-TERM DEBT

C.Changes in Long-Term Liabilities

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>Due Within One Year</u>
Governmental Activities:					
Bonds Payable:					
G.O. Improvement Bonds	\$ 175,458	\$ -	\$ 19,804	\$ 155,654	\$ 20,827
G.O. Equipment Certificates	255,809	-	45,813	209,996	48,046
Capital Lease Obligations	61,490	-	18,398	43,092	19,566
Compensated Absences	<u>169,413</u>	<u>103,277</u>	<u>95,636</u>	<u>177,054</u>	<u>80,522</u>
Total Governmental Activities	662,170	103,277	179,651	585,796	168,961
Business-Type Activities:					
Notes/Bonds Payable:					
G.O. Revenue Notes	1,491,403	-	184,838	1,306,565	190,510
Revenue Bonds	317,201	-	47,832	269,369	49,865
Compensated Absences	<u>55,946</u>	<u>44,705</u>	<u>39,111</u>	<u>61,540</u>	<u>32,951</u>
Total Business-Type Activities	<u>1,864,550</u>	<u>44,705</u>	<u>271,781</u>	<u>1,637,474</u>	<u>273,326</u>
Total Long-Term Liabilities	<u>\$ 2,526,720</u>	<u>\$ 147,982</u>	<u>\$ 451,432</u>	<u>\$ 2,223,270</u>	<u>\$ 442,287</u>

The General Fund typically liquidates the liability related to compensated absences.

D. Capital Lease Obligations

The City is obligated under three leases accounted for as capital leases. The assets and liabilities under the capital lease are recorded at the lower of the present value of the minimum lease payments or the fair value of the assets. At December 31, 2012, these assets were valued at \$ 109,373 with accumulated depreciation of \$ 71,012.

Minimum future lease payments under the capital leases in the aggregate are as follows:

<u>Year Ending December 31,</u>	
2013	\$ 21,422
2014	24,480
Net Minimum Lease Payments	<u>45,902</u>
Less Amount Representing Interest	<u>(2,810)</u>
Present Value of Net Minimum Lease Payments	<u>\$ 43,092</u>

CITY OF SILVER BAY

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

NOTE 7 – LOANS RECEIVABLES

Loans receivable at December 31, 2012 are as follows:

Superior View Properties, LLC Promissory Note:

\$ 50,000 promissory note, due in monthly installments
of \$ 277 through September 2023, with interest at 3.00%. \$ 30,343

North Shore Investment Group Promissory Note:

\$ 11,650 promissory note, due in monthly installments
of \$ 154 through November 2017, with interest at 3.0%. 8,302

Silver Bay Country Club Lease Agreement:

\$ 43,697 repayment agreement, due in monthly installments
(from May to October each year) of \$ 1,080 through October 2014. 30,960

Silver Bay Country Club Lease Agreement:

\$ 38,206 repayment agreement, due in annual installments
of \$ 8,657 through September 2013, with interest at 6.469%. 10,042

Total Loans Receivable \$ 79,647

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS
December 31, 2012

NOTE 8 – FUND BALANCES/NET POSITION

A. Fund Balance

Fund equity balances are classified as follows to reflect the limitations and restrictions of the respective funds.

	General	Mary MacDonald Business Center	Public Works Reserve	Debt Service	Nonmajor Governmental Fund	Total
Nonspendable:						
Minnesota Community Capital Fund	\$ -	\$ -	\$ -	\$ -	\$ 25,000	\$ 25,000
Restricted:						
Technology Grant	-	-	-	-	10,819	10,819
Memorial Donation	-	-	-	-	12,884	12,884
Legislative Funding and Donation - Biofuel/Food Greenhouse						
Project and Wind Turbine	-	-	52,531	-	-	52,531
Cemetery-Perpetual Care	-	-	-	-	2,298	2,298
Debt Service	-	-	-	41,952	-	41,952
Committed:						
Fire Truck	112,000	-	-	-	-	112,000
Assigned:						
Mary MacDonald Business Center	-	158,389	-	-	-	158,389
Mary MacDonald Business Center Playground and Ballfield	-	-	-	-	8,265	8,265
Library	-	-	-	-	17,184	17,184
Cemetery	-	-	-	-	18,486	18,486
Arena	-	-	-	-	12,240	12,240
Park and Recreation	-	-	-	-	91,374	91,374
Community Building	-	-	-	-	1,524	1,524
Biofuel/Food Greenhouse Project	-	-	-	-	179,579	179,579
Economic Development	-	-	-	-	193,355	193,355
Community Business Partnership	-	-	-	-	103,695	103,695
Storefront Renovation	-	-	-	-	111,327	111,327
Taconite Reserve/Sidewalk Replacement/Special Projects	-	-	347,654	-	-	347,654
Unassigned	1,360,468	-	-	-	(43,718)	1,316,750
Total	<u>\$ 1,472,468</u>	<u>\$ 158,389</u>	<u>\$ 400,185</u>	<u>\$ 41,952</u>	<u>\$ 744,312</u>	<u>\$ 2,817,306</u>

B. Net Position

Restricted net position is comprised of the total restricted fund balance in the governmental funds plus the effect of the conversion to the government-wide net position.

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS December 31, 2012

NOTE 9 – RISK MANAGEMENT

The City purchases commercial insurance coverage through the League of Minnesota Cities Insurance Trust (LMCIT) with other cities in the state, which is a public entity risk pool currently operating as a common risk management and insurance program. The City pays an annual premium to the LMCIT for its insurance coverage. The LMCIT is self-sustaining through commercial companies for excess claims. The City is covered through the pool for any claims incurred but unreported, however, retains risk for the deductible portion of its insurance policies. The amount of these deductibles is considered immaterial to the financial statements.

There were no significant reductions in insurance from the previous year or settlements in excess of insurance coverage for any of the past three years.

The City's workers' compensation insurance policy is retrospectively rated. With this type of policy, final premiums are determined after loss experience is known. The amount of premium adjustment for 2012 is estimated to be immaterial based on workers' compensation rates and salaries for the year. At December 31, 2012, there were no other claims liabilities reported in the Fund based on the requirements of GASB Statement No. 10, which requires a liability for claims be reported if information prior to the issuance of the financial statements indicates that it is probable that a liability has been incurred at the date of the financial statements and the amount of the loss can be reasonably estimated.

NOTE 10 – JOINT POWERS AGREEMENT

On January 1, 1992, the City entered into a joint powers agreement with Lake County (the "County"), pursuant to *Minnesota Statutes* 471.59, whereby the City agreed to operate Rukavina Arena, which is owned by the County.

The County has agreed to pay the City the sum of \$ 45,000 annually in two equal installments of \$ 22,500 on June 1 and November 1. In addition, the City shall have the right to excess revenues and shall be responsible for excess expenditures, except the County shall provide fire and extended coverage insurance for buildings and grounds.

The agreement automatically renews in one year increments unless otherwise mutually negotiated.

On November 15, 2010, the City entered into a joint powers agreement with the County and other local governments, pursuant to *Minnesota Statutes* 471.59 and 471.656, whereby the County will construct a network of fiber optic cable that will provide advanced data, video and voice communication services in the County, including the City. The County will own the fiber optic network that is constructed.

NOTE 11 – LONG TERM CONTRACTED USE AGREEMENT

As of January 1, 2012, the City entered into a long term contracted use agreement with the University of Minnesota Duluth's Center for Sustainability Community Development (UMDCSCD). The agreement terminates on December 31, 2022. UMDCSCD will operate, manage and maintain the Biofuel/Food Greenhouse for the development of fish, produce and algae for research and educational purposes. UMDCSCD will cover all costs and expenditures related to the management, maintenance and operations of the Greenhouse. The EDA will receive an amount equal to 10% of any grants received for the Greenhouse.

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS December 31, 2012

NOTE 12 – DEFINED BENEFIT PENSION PLANS – STATE-WIDE

Public Employees' Retirement Association

A. Plan Description

All full-time and certain part-time employees of the City are covered by defined benefit plans administered by the Public Employees' Retirement Association of Minnesota (PERA). PERA administers the General Employees' Retirement Fund (GERF) and the Public Employees' Police and Fire Fund (PEPFF), which are cost-sharing, multiple-employer retirement plans. These Plans are established and administered in accordance with *Minnesota Statutes* Chapters 353 and 356.

GERF members belong to either the Coordinated or 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. All police officers, firefighters and peace officers who qualify for membership are covered by the PEPFF.

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

Two methods are used to compute benefits for 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% of average salary for each of the first 10 years of service and 2.7% for each remaining year. The annuity accrual rate for a Coordinated Plan member is 1.2% of average salary for each of the first 10 years and 1.7% for each remaining year. Under Method 2, the annuity accrual rate is 2.7% of average salary for Basic Plan members and 1.7% for Coordinated Plan members for each year of service. For PEPFF members, the annuity accrual rate is 3.0% for each year of service. For all GERF and PEPFF 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 55 for PEPFF members and 65 for Basic and Coordinated Plan members hired prior to July 1, 1989. Normal retirement age is the age for unreduced Social Security benefits capped at 66 for Coordinated Plan 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 yet receiving them, are bound by the provisions in effect at the time they last terminated their public service.

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS December 31, 2012

NOTE 12 – DEFINED BENEFIT PENSION PLANS – STATE-WIDE

Public Employees' Retirement Association (Continued)

A. Plan Description (Continued)

PERA issues a publicly available financial report that includes financial statements and required supplementary information for GERF and PEPFF. 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 (651) 296-7460 or (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. GERF Basic Plan members and Coordinated Plan members were required to contribute 9.1% and 6.25%, respectively, of their annual covered salary in 2012. PEPFF members were required to contribute 9.6% of their annual covered salary in 2012. In 2012, the City was required to contribute the following percentages of annual covered payroll: 11.78% for Basic Plan members, 7.25% for Coordinated Plan members and 14.4% for PEPFF members. The City's contributions to the Public Employees' Retirement Fund for the years ending December 31, 2012, 2011 and 2010 were \$ 79,340, \$ 75,741 and \$ 70,570, respectively. The City's contributions to PEPFF for the years ending December 31, 2012, 2011 and 2010 were \$ 42,845, \$ 47,163 and \$ 45,667, respectively. The City's contributions were equal to the contractually required contributions for each year as set by state statute.

NOTE 13 – DEFINED CONTRIBUTION LUMP SUM SERVICE PENSION PLAN – FIREFIGHTERS' RELIEF ASSOCIATION

A. Plan Description

The City contributes to the Silver Bay Firefighters' Relief Association (the "Association"), a single-employer, defined benefit pension plan. The plan provides retirement, disability and death benefits to volunteer firefighters of the City. Pension benefits are determined by multiplying the accrued liability, as set forth in *Minnesota Statutes* 69.772, Subd. 2, by the ratio of the lump sum service pension amount provided in the bylaws of the Association to a service pension of \$ 1,100 per year of service. The Association's Board of Trustees has the authority to establish and amend benefit provisions. Benefit provisions are also subject to enabling state statutes; therefore, any amendments to benefit provisions are reviewed by the Office of the State Auditor.

The Association issues a publicly available audit report. The report may be obtained by writing to Silver Bay Firefighters' Relief Association at 63 Nelson Drive, Silver Bay, Minnesota 55614 or calling (218) 226-4408.

CITY OF SILVER BAY

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

**NOTE 13 – DEFINED CONTRIBUTION LUMP SUM SERVICE PENSION PLAN –
FIREFIGHTERS’ RELIEF ASSOCIATION**

B. Funding Policy and Annual Pension Cost

Schedules I and II, prepared by the Association and certified to the City Council by August 1 of each year, determine the municipal contribution for the following calendar year. Plan members, the volunteer firefighters, do not contribute to the plan. The state contributes to the plan in the form of state fire aid. Schedules I and II follow enabling state statutes for fire relief associations. Municipalities are required by state statutes to contribute the amount certified on Schedules I and II. The City’s annual contribution for the current year and related information follows:

Date Certified to City Council: August 1, 2011

Statutory Assumptions:

Investment Rate of Return	5.0%
Administrative Expenses Increase	3.5%
State Aid Contribution	100.0%
Amortization of Surplus (Deficit)	10.0%

C. Three Year Trend Information

<u>Year Ended</u>	<u>Statutory Contribution</u>	<u>Actual Contribution</u>	<u>Percentage Contributed</u>	<u>State Contribution</u>	<u>Percentage Contributed</u>
12/31/12	\$ -	\$ -	100%	\$ 12,865	100%
12/31/11	-	-	100%	12,608	100%
12/31/10	-	-	100%	11,750	100%

D. Required Supplementary Information: Schedule of Funding Progress

<u>Valuation Date</u>	<u>Value of Assets (a)</u>	<u>Statutory Accrued Liability (b)</u>	<u>Excess of Assets Over Liabilities (a-b)</u>	<u>Funded Ratio (a/b)</u>	<u>Covered Payroll (c)</u>	<u>Excess as a Percentage of Covered Payroll ((a-b)/c)</u>
12/31/12	\$ 511,620	\$ 390,498	\$ 121,122	131%	N/A	N/A
12/31/11	457,400	391,754	65,646	117%	N/A	N/A
12/31/10	481,106	360,780	120,326	133%	N/A	N/A

CITY OF SILVER BAY

NOTES TO THE FINANCIAL STATEMENTS
December 31, 2012

**NOTE 13 – DEFINED CONTRIBUTION LUMP SUM SERVICE PENSION PLAN –
FIREFIGHTERS’ RELIEF ASSOCIATION**

E. Contributions Required and Contributions Made

Financial requirements of the Association are determined in accordance with *Minnesota Statutes* as follows:

Normal Cost for Next Year (Increase in Pension Benefit Obligation)
Plus Estimated Expenses for Next Year and 10% of Any Deficits
Less Anticipated Income Next Year and 10% of Any Surplus

Contributions totaling \$ 0 were made by the City and \$ 12,865 by the State of Minnesota, in accordance with state statute requirements for the year ended December 31, 2012.

NOTE 14 – SUBSEQUENT EVENTS

The City has evaluated subsequent events through February 28, 2013, the date which the financial statements were available to be issued.

NOTE 15 – CHANGE IN ACCOUNTING PRINCIPLE

For the year ended December 31, 2012, the City implemented GASB Statement No. 63. This action resulted in the establishment of categories outside of assets and liabilities titled deferred outflows and deferred inflows, which were not applicable to the City for 2012. The Statement also retitled Net Assets as Net Position.

SUPPLEMENTARY INFORMATION

CITY OF SILVER BAY

**COMBINING BALANCE SHEET -
NONMAJOR GOVERNMENTAL FUNDS
December 31, 2012**

	Special Revenue			
	Library (211)	Cemetery (215)	Arena (241)	Park and Recreation (251)
ASSETS				
Cash and Investments	\$ 46,567	\$ 20,769	\$ 19,654	\$ 100,070
Cash with Fiscal Agent	-	-	-	-
Accounts Receivable	-	-	372	105
Interest Receivable	-	15	(18)	44
Loan Receivable	-	-	-	-
	\$ 46,567	\$ 20,784	\$ 20,008	\$ 100,219
LIABILITIES AND FUND BALANCES				
Liabilities				
Accounts Payable	\$ 154	\$ -	\$ 122	\$ 580
Due to Other Funds	-	-	-	-
Due to Other Governments	4	-	46	-
Salaries and Benefits Payable	5,522	-	7,600	-
Deferred Revenue	-	-	-	-
Total Liabilities	5,680	-	7,768	580
Fund Balances				
Nonspendable	-	-	-	-
Restricted	23,703	2,298	-	-
Assigned	17,184	18,486	12,240	99,639
Unassigned	-	-	-	-
Total Fund Balances	40,887	20,784	12,240	99,639
Total Liabilities and Fund Balances	\$ 46,567	\$ 20,784	\$ 20,008	\$ 100,219

Special Revenue

Community Building (261)	Economic Development (271)	Community Business Partnership (275)	Storefront Renovation (407)	Marina (601)	Airport (231)	Total Nonmajor Governmental Funds
\$ 1,525	\$ 372,643	\$ 103,620	\$ 111,247	\$ 19,055	\$ -	\$ 795,150
-	25,000	-	-	-	-	25,000
-	-	-	-	452	-	929
(1)	291	75	80	(7)	(31)	448
-	30,343	-	8,302	-	-	38,645
<u>\$ 1,524</u>	<u>\$ 428,277</u>	<u>\$ 103,695</u>	<u>\$ 119,629</u>	<u>\$ 19,500</u>	<u>\$ (31)</u>	<u>\$ 860,172</u>
\$ -	\$ -	\$ -	\$ -	\$ -	-	\$ 856
-	-	-	-	-	39,588	39,588
-	-	-	-	-	-	50
-	-	-	-	-	-	13,122
-	30,343	-	8,302	23,599	-	62,244
-	<u>30,343</u>	-	<u>8,302</u>	<u>23,599</u>	<u>39,588</u>	<u>115,860</u>
-	25,000	-	-	-	-	25,000
-	-	-	-	-	-	26,001
1,524	372,934	103,695	111,327	-	-	737,029
-	-	-	-	(4,099)	(39,619)	(43,718)
<u>1,524</u>	<u>397,934</u>	<u>103,695</u>	<u>111,327</u>	<u>(4,099)</u>	<u>(39,619)</u>	<u>744,312</u>
<u>\$ 1,524</u>	<u>\$ 428,277</u>	<u>\$ 103,695</u>	<u>\$ 119,629</u>	<u>\$ 19,500</u>	<u>\$ (31)</u>	<u>\$ 860,172</u>

CITY OF SILVER BAY

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

	Special Revenue			
	Library (211)	Cemetery (215)	Arena (241)	Park and Recreation (251)
REVENUES				
General Property Taxes	\$ 97,000	\$ -	\$ -	\$ -
Intergovernmental	37,300	-	88,532	44,299
Charges for Services	4,015	320	17,807	22,065
Miscellaneous:				
Investment Income	10	107	(194)	379
Contributions and Donations	17,360	-	-	10,000
Loan Repayments	-	-	-	-
Other	2,401	-	12,159	3,531
Total Revenues	158,086	427	118,304	80,274
EXPENDITURES				
Current				
Culture and Recreation	208,586	2,144	189,036	151,821
Airport	-	-	-	-
Capital Outlay				
Culture and Recreation	6,300	-	3,173	45,408
Total Expenditures	214,886	2,144	192,209	197,229
Excess of Revenues Over (Under) Expenditures	(56,800)	(1,717)	(73,905)	(116,955)
OTHER FINANCING SOURCES (USES)				
Proceeds from Sale of Capital Asset	-	-	-	2,466
Transfers In	51,255	2,000	71,600	124,928
Transfers Out	-	-	-	-
Total Other Financing Sources (Uses)	51,255	2,000	71,600	127,394
Net Change in Fund Balances	(5,545)	283	(2,305)	10,439
FUND BALANCES				
Beginning of Year	46,432	20,501	14,545	89,200
End of Year	\$ 40,887	\$ 20,784	\$ 12,240	\$ 99,639

Special Revenue							
Community Building (261)	Economic Development (271)	Community Business Partnership (275)	Storefront Renovation (407)	Marina (601)	Airport (231)	Total Nonmajor Governmental Funds	
\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 97,000	
-	-	-	-	49,500	21,757	241,388	
9,400	-	-	-	113,820	12,845	180,272	
(3)	2,138	551	588	(97)	(221)	3,258	
-	-	-	-	1,450	-	28,810	
-	3,327	-	1,847	-	-	5,174	
909	-	-	-	5,862	2,527	27,389	
<u>10,306</u>	<u>5,465</u>	<u>551</u>	<u>2,435</u>	<u>170,535</u>	<u>36,908</u>	<u>583,291</u>	
12,749	-	-	-	159,272	-	723,608	
-	-	-	-	-	42,919	42,919	
1,530	-	-	-	-	-	56,411	
<u>14,279</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>159,272</u>	<u>42,919</u>	<u>822,938</u>	
(3,973)	5,465	551	2,435	11,263	(6,011)	(239,647)	
-	-	-	-	-	-	2,466	
4,150	-	-	-	-	6,525	260,458	
-	(6,810)	-	-	-	-	(6,810)	
<u>4,150</u>	<u>(6,810)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>6,525</u>	<u>256,114</u>	
177	(1,345)	551	2,435	11,263	514	16,467	
1,347	399,279	103,144	108,892	(15,362)	(40,133)	727,845	
<u>\$ 1,524</u>	<u>\$ 397,934</u>	<u>\$ 103,695</u>	<u>\$ 111,327</u>	<u>\$ (4,099)</u>	<u>\$ (39,619)</u>	<u>\$ 744,312</u>	

CITY OF SILVER BAY
Lake County, Minnesota

**SCHEDULE OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES -
BUDGET AND ACTUAL - GENERAL FUND
For the Year Ended December 31, 2012**

	<u>Budgeted Amounts</u>		Actual Amounts	Variance with Final Budget - Over (Under)
	<u>Original</u>	<u>Final</u>		
REVENUES				
General Property Taxes	\$ 686,750	\$ 687,405	\$ 663,145	\$ (24,260)
Licenses and Permits	13,240	15,270	15,411	141
Intergovernmental Revenue:				
Local Government Aid	450,020	450,020	450,020	-
Market Value Credit	-	455	455	-
PERA Aid	4,380	4,380	4,383	3
Taconite Homestead Credit	120,400	124,840	124,843	3
Taconite Production Tax	450,000	423,200	423,211	11
Federal Grants and Aids	-	25,000	16,911	(8,089)
Other State Grants and Aids	44,000	55,600	48,310	(7,290)
Other County Grants	13,700	13,700	13,700	-
Other Grants and Aids	2,100	1,300	1,328	28
Total Intergovernmental Revenue	<u>1,084,600</u>	<u>1,098,495</u>	<u>1,083,161</u>	<u>(15,334)</u>
Charges for Services:				
Public Safety	36,025	38,450	62,454	24,004
Public Works	300	2,750	2,919	169
Park and Recreation	500	800	800	-
Total Charges for Services	<u>36,825</u>	<u>42,000</u>	<u>66,173</u>	<u>24,173</u>
Fines and Forfeitures	6,800	5,125	6,060	935
Miscellaneous Revenues:				
Investment Income	6,000	6,000	6,424	424
Contributions and Donations	1,000	1,600	1,680	80
Loan Repayments	17,020	17,020	17,021	1
Other	14,800	28,350	28,593	243
Total Miscellaneous Revenues	<u>38,820</u>	<u>52,970</u>	<u>53,718</u>	<u>748</u>
Total Revenues	<u>1,867,035</u>	<u>1,901,265</u>	<u>1,887,668</u>	<u>(13,597)</u>
EXPENDITURES				
General Government				
Mayor and Council:				
Current	28,800	27,825	27,684	(141)
Administrative and Finance:				
Current	283,220	269,070	268,896	(174)
Capital Outlay	1,000	50	40	(10)
Other General Government:				
Current	156,480	138,605	137,720	(885)
Capital Outlay	1,500	1,600	1,560	(40)
Total General Government	<u>471,000</u>	<u>437,150</u>	<u>435,900</u>	<u>(1,250)</u>

CITY OF SILVER BAY
Lake County, Minnesota

**SCHEDULE OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES -
BUDGET AND ACTUAL - GENERAL FUND
For the Year Ended December 31, 2012**

	Budgeted Amounts			
	Original	Final	Actual Amounts	Variance with Final Budget - Over (Under)
EXPENDITURES				
Public Safety				
Police:				
Current	\$ 449,550	\$ 454,870	\$ 454,309	\$ (561)
Capital Outlay	2,000	5,900	5,830	(70)
Fire:				
Current	67,925	68,700	68,246	(454)
Capital Outlay	6,000	8,300	8,297	(3)
Other:				
Current	12,500	7,770	7,172	(598)
Capital Outlay	100	-	-	-
Total Public Safety	538,075	545,540	543,854	(1,686)
Public Works				
Streets and Highways:				
Street Maintenance and Storm Sewers:				
Current	496,500	451,800	449,233	(2,567)
Capital Outlay	-	13,200	13,112	(88)
Street Lighting:				
Current	27,500	21,350	21,313	(37)
Total Public Works	524,000	486,350	483,658	(2,692)
Culture and Recreation				
Current	18,900	27,200	27,086	(114)
Debt Service				
Principal	18,400	18,400	18,398	(2)
Interest and Other Charges	3,030	3,030	3,024	(6)
Total Debt Service	21,430	21,430	21,422	(8)
Total Expenditures	1,573,405	1,517,670	1,511,920	(5,750)
Excess of Revenues Over (Under) Expenditures	293,630	383,595	375,748	(7,847)
OTHER FINANCING SOURCES (USES)				
Transfers In	-	13,100	13,112	12
Transfers Out	(293,630)	(268,076)	(268,076)	-
Total Other Financing Sources (Uses)	(293,630)	(254,976)	(254,964)	12
Net Change in Fund Balances	\$ -	\$ 128,619	120,784	\$ (7,835)
FUND BALANCES				
Beginning of Year			1,351,684	
End of Year			\$ 1,472,468	

CITY OF SILVER BAY

**ANALYSIS OF CHANGES IN FUND BALANCE -
PUBLIC WORKS RESERVE FUND
For the Year Ended December 31, 2012**

	Business Park (903)	Taconite Revenue Losses (904)	Bell Circle Apartments (905)
	<u> </u>	<u> </u>	<u> </u>
Balance - January 1, 2012	\$ (490,573)	\$ 368,812	\$ (147,048)
General Property Taxes	-	-	-
Intergovernmental Revenue	543,443	-	-
Investment Income	-	-	-
Miscellaneous Revenue	73,285	-	-
Transfers from Other Funds	-	-	34,837
	<u> </u>	<u> </u>	<u> </u>
Total Available	126,155	368,812	(112,211)
Expenditures	(702,595)	-	-
Transfers to Other Funds	-	-	-
	<u> </u>	<u> </u>	<u> </u>
Balance - December 31, 2012	<u><u>\$ (576,440)</u></u>	<u><u>\$ 368,812</u></u>	<u><u>\$ (112,211)</u></u>

Project Notes:

* Taconite reserve has been consistent for the past several years. The five year moving average for taconite taxes is \$ 456,494, indicating approximately \$ 87,682 can be added to the reserve at December 31, 2012.

Special Projects (906)	Sidewalk Improvements (907)	Total
\$ 251,882	\$ 369,759	\$ 352,832
125,915	34,120	160,035
20,946	5,660	570,049
1,184	-	1,184
-	-	73,285
-	-	34,837
399,927	409,539	1,192,222
-	-	(702,595)
(89,442)	-	(89,442)
<u>\$ 310,485</u>	<u>\$ 409,539</u>	<u>\$ 400,185</u>

(THIS PAGE LEFT BLANK INTENTIONALLY)



Expert advice. When you need it.SM

**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

Honorable Mayor and Members
of the City Council
City of Silver Bay
Silver Bay, 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 the City of Silver Bay, 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, and have issued our report thereon dated February 28, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City'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's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

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. *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.



Our consideration of internal control was for the limited purpose described in the first paragraph of this section 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. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Findings and Responses on Internal Control as Audit Findings 06-01 and 06-02 that we consider to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether City'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*.

The City's Response to Findings

The City's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Responses on Internal Control. The City's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

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 City'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 City's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in cursive script that reads "Kern, DeWenter, Viere, Ltd.".

KERN, DEWENTER, VIERE, LTD.
St. Cloud, Minnesota
February 28, 2013



Expert advice. When you need it.SM

REPORT ON LEGAL COMPLIANCE

Honorable Mayor and Members
of the City Council
City of Silver Bay
Silver Bay, Minnesota

We have audited the financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Silver Bay, Minnesota, as of and for the year ended December 31, 2012, which collectively comprise the City's basic financial statements and have issued our report thereon dated February 28, 2013.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the provisions of the *Minnesota Legal Compliance Audit Guide for Political Subdivisions*, promulgated by the State Auditor pursuant to *Minnesota Statutes* Sec. 6.65. Accordingly, the audit included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

The *Minnesota Legal Compliance Audit Guide for Political Subdivisions* covers seven categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, miscellaneous provisions and Tax Increment Financing. Our study included all of the listed categories except Tax Increment Financing.

The results of our tests indicate that for the items tested, the City complied with the material terms and conditions of applicable legal provisions.

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

Kern, DeWenter, Viere, Ltd.

KERN, DEWENTER, VIERE, LTD.
St. Cloud, Minnesota
February 28, 2013

CITY OF SILVER BAY
SCHEDULE OF FINDINGS AND RESPONSES
ON INTERNAL CONTROL
December 31, 2012

CURRENT AND PRIOR YEAR INTERNAL CONTROL FINDINGS:

Significant Deficiencies:

Audit Finding 06-01 – Lack of Segregation of Accounting Duties

During the year ended December 31, 2012, the City had a lack of segregation of accounting duties due to a limited number of office employees.

Management and the City Council are aware of the lack of segregation of accounting duties and have taken certain steps to compensate for the condition, but due to the small staff needed to handle all of the accounting duties, the costs of obtaining desirable segregation of accounting duties can often exceed benefits which could be derived. However, management and the City Council must remain aware of this situation and should continually monitor the accounting system, including changes that occur.

The lack of segregation of accounting duties can be demonstrated in the following areas, which is not intended to be an all inclusive list:

- The Deputy Clerk has full general ledger access, including the ability to write and post journal entries, and is also responsible for review of the financial activities of the City, including preparation of the bank reconciliation.
- Receipting Process
 - The Assistant Deputy Clerk creates and sends invoices, occasionally collects payments as they are received, prepares deposits and enters the receipts into the accounting system.
 - The Assistant Deputy Clerk enters the utility billing into the utility billing register, bills commercial and residential customers and mails the utility bills. The Assistant Deputy Clerk also occasionally receives payments, records the receipts and is also able to make adjustments to the utility billing register.
- Disbursement Process
 - The Assistant Deputy Clerk creates a batch list for City Council approval, enters information for payment on all bills, prints checks, mails checks and creates the paid claims list that is presented to the City Council.

City's Response:

The City is aware of this situation and as the auditors acknowledge, it would not be cost effective to hire additional personnel to correct this issue. The City will continue to monitor the internal controls and adjust them when possible using the current staff.

CITY OF SILVER BAY
SCHEDULE OF FINDINGS AND RESPONSES
ON INTERNAL CONTROL
December 31, 2012

CURRENT AND PRIOR YEAR INTERNAL CONTROL FINDINGS:

Significant Deficiencies: (Continued)

Audit Finding 06-02 – Preparation of Financial Statements

As a function of the audit process, auditors are required to gain an understanding of the City's internal control, including the financial reporting process.

The City does not have an internal control system designed to provide for the preparation of the financial statements being audited. As auditors, we were requested to draft the financial statements and accompanying Notes to the Financial Statements. This circumstance is not unusual in a city of your size.

Even though all management decisions related to financial reporting are made by the City's management and approval of the financial statements lies with management, it is the responsibility of management and those charged with governance to make the decision whether to accept the degree of risk associated with this condition because of cost or other considerations.

City's Response:

This is something the City will work on in the future. Limited staff and budgets contribute to this situation.