

**MANAGEMENT COMMUNICATIONS**

**CITY OF MERRILL, WISCONSIN**

**DECEMBER 31, 2012**

**CITY OF MERRILL, WISCONSIN**  
December 31, 2012

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To the City Council  
City of Merrill  
Merrill, Wisconsin

We have completed our audit of the basic financial statements of the City of Merrill (the "City") as of and for the year ended December 31, 2012. The City's financial statements, including our report thereon dated April 18, 2013, are presented in a separate audit report document. Professional standards require that we provide you with the following information related to our audit.

#### Our Responsibilities Under U.S. Generally Accepted Auditing Standards

As stated in our engagement letter, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement and are fairly presented in accordance with accounting principles generally accepted in the United States of America. Because an audit is designed to provide reasonable, but not absolute, assurance and because we did not perform a detailed examination of all transactions, there is a risk that material errors, fraud, noncompliance with the provisions of laws, regulations, contracts and grants or other illegal acts may exist and not be detected by us.

In planning and performing our audit, we considered the City's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide assurance on the internal control over financial reporting.

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, 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. While our audit provides a reasonable basis for our opinion, it does not provide a legal determination on the City's compliance with those requirements.

#### Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you in our correspondence about planning matters.

#### Significant Audit Findings

##### *Consideration of Internal Control*

In planning and performing our audit of the financial statements of the City as of and for the year ended December 31, 2012, in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control. Our report on internal control over financial reporting and on compliance and other matters is presented on pages 38 - 39 of the annual report.

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

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 financial statements will be not be prevented or detected and corrected on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the following deficiencies to be significant deficiencies in internal control:

Finding 2012-01	Preparation of Annual Financial Report
Finding 2012-02	Financial Reporting for Federal and State Financial Assistance

These findings are described in detail in the schedule of findings and responses on pages 45 - 46 of the annual report.

#### *Qualitative Aspects of Accounting Practices*

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the City are described in Note A to the financial statements. The City implemented GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* and GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities* for the year ended December 31, 2012. We noted no significant transactions entered into by the City during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates included in the financial statements were:

#### Depreciable Life of Capital Assets

- Management's estimate of the depreciable life of the capital assets is based upon analysis of the expected useful life of the capital assets. We evaluated the key factors and assumptions and the consistency in these factors and assumptions used to develop the depreciable life in determining that it is reasonable in relation to the financial statements taken as a whole.

#### Accumulated Sick Leave

- Management's estimate of accumulated sick leave is based upon analysis of the employees sick leave balance. We evaluated the key factors and assumptions and the consistency in these factors and assumptions used to develop the liability in determining that it is reasonable in relation to the financial statements taken as a whole.

#### *Difficulties Encountered in Performing the Audit*

We encountered no significant difficulties in dealing with management in performing and completing our audit.

### *Corrected and Uncorrected Misstatements*

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. The financial statements reflect all accounting adjustments proposed during our audit. Copies of the audit adjustments are available from management.

### *Disagreements with Management*

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditors' report. We are pleased to report that no such disagreements arose during the course of our audit.

### *Management Representations*

We have requested certain representations from management that are included in the management representation letter dated April 18, 2013. The management representation letter follows this communication.

### *Management Consultations with Other Independent Accountants*

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the City's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

### *Other Audit Findings or Issues*

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to conducting the audit. These discussions occurred in the normal course of our professional relationship and our responses were not a condition to completing the services as your auditor.

In addition, during our audit, we noted certain other matters that are presented for your consideration. We will review the status of these comments during our next audit engagement. Our comments and recommendations are intended to improve the internal control or result in other operating efficiencies. We will be pleased to discuss these matters in further detail at your convenience, perform any additional study of these matters, or assist you in implementing the recommendations. Our comments are summarized in the comments and observations section of this report.

This communication, which does not affect our report dated April 18, 2013 on the financial statements of the City, is intended solely for the information and use of the City Council, management, and others within the City, and is not intended to be and should not be used by anyone other than these specified parties.

Sincerely,



Certified Public Accountants  
Green Bay, Wisconsin  
April 18, 2013



# CITY OF MERRILL

## Finance Director/City Treasurer

**Kathy Unertl, Finance Director**

1004 East First Street • Merrill, Wisconsin • 54452

Phone (715) 536-5594 • FAX (715) 539-2668

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April 18, 2013

Schenck SC  
2200 Riverside Drive  
P.O. Box 23819  
Green Bay, WI 54305-3819

This representation letter is provided in connection with your audit of the primary government financial statements of the City of Merrill, Wisconsin, (the "City"), which comprise the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information as of December 31, 2012, and the respective changes in the financial position and where applicable, cash flows for the year then ended, and the related notes to the primary government financial statements for the purpose of expressing opinions as to whether the primary government financial statements are presented fairly, in all material respects, in accordance with accounting principles generally accepted in the United States of America.

Certain representations in this letter are described as being limited to matters that are material. Items in No. 45 are considered material based on the materiality criteria specified in OMB Circular A-133 and the State *Single Audit Guidelines* issued by the Wisconsin Department of Administration. Items are considered material, regardless of size, if they involve an omission or misstatement of accounting information that, in light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would be changed or influenced by the omission or misstatement. An omission or misstatement that is monetarily small in amount could be considered material as a result of qualitative factors.

We confirm, to the best of our knowledge and belief, as of April 18, 2013, the following representations made to you during your audit.

### **Financial Statements**

1. We have fulfilled our responsibilities, as set out in the terms of the audit engagement letter dated October 2, 2012.
2. The primary government's financial statements referred to above are fairly presented in conformity with accounting principles generally accepted in the United States of America and include all properly classified funds and other financial information of the primary government required by accounting principles generally accepted in the United States of America to be included in the financial reporting entity.
3. We acknowledge our responsibility for 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.
4. We acknowledge our responsibility for the design, implementation, and maintenance of internal control to prevent and detect fraud.
5. Significant assumptions we used in making accounting estimates are reasonable.

6. Related party relationships and transactions, including revenues, expenditures/expenses, loans, transfers, leasing arrangements, and guarantees, and amounts receivable from or payable to related parties have been appropriately accounted for and disclosed in accordance with the requirements of accounting principles generally accepted in the United States of America.
7. All events subsequent to the date of the financial statements and for which accounting principles generally accepted in the United States of America requires adjustment or disclosure have been adjusted or disclosed. No events, including instances of noncompliance, have occurred subsequent to the balance sheet date and through the date of this letter that would require adjustment to or disclosure in the aforementioned financial statements or in the schedule of findings and questioned costs.
8. We are in agreement with the adjusting journal entries you have proposed, and they have been posted to the City's accounts.
9. We are not aware of any pending or threatened litigation, claims or assessments or unasserted claims or assessments that are required to be accrued or disclosed in the financial statements, and we have not consulted a lawyer concerning litigation, claims, or assessments.
10. Guarantees, whether written or oral, under which the City is contingently liable, if any, have been properly recorded or disclosed.

**Information Provided**

11. We have provided you with:
  - a. Access to all information, of which we are aware, that is relevant to the preparation and fair presentation of the financial statements, such as records, documentation, and other matters.
  - b. Additional information that you have requested from us for the purpose of the audit.
  - c. Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.
  - d. Minutes of the meetings of the City Council or summaries of actions of recent meetings for which minutes have not yet been prepared.
12. All material transactions have been recorded in the accounting records and are reflected in the financial statements and the schedules of expenditures of federal awards and state financial assistance.
13. We have made an assessment of the risk that the financial statements may be materially misstated as a result of fraud. We have disclosed the results of our assessment as follows:
  - a. We have no knowledge of any fraud or suspected fraud that affects the entity and involves:
    - i. Management,
    - ii. Employees who have significant roles in internal control, or
    - iii. Others where the fraud could have a material effect on the financial statements.
  - b. We have no knowledge of any allegations of fraud or suspected fraud affecting the City's financial statements communicated by employees, former employees, regulators, or others.

14. We have disclosed to you all known instances of noncompliance or suspected noncompliance with provisions of laws, regulations, contracts, or grant agreements, or abuse, whose effects should be considered when preparing financial statements.
15. We are not aware of any pending or threatened litigation, claims, or assessments or unasserted claims or assessments that are required to be accrued or disclosed in the financial statements, and we have not consulted a lawyer concerning litigation, claims, or assessments.
16. We have disclosed to you the identity of the City's related parties and all the related party relationships and transactions of which we are aware.

**Government - specific**

17. We have made available to you all financial records and related data.
18. There have been no communications from regulatory agencies concerning noncompliance with, or deficiencies in, financial reporting practices.
19. We have identified to you any previous audits, attestation engagements, and other studies related to the audit objectives and whether related recommendations have been implemented.
20. We have provided our views on reported findings, conclusions, and recommendations, as well as our planned corrective actions, for the report.
21. The City has no plans or intentions that may materially affect the carrying value or classification of assets, liabilities, or equity.
22. We are responsible for compliance with the laws, regulations, and provisions of contracts and grant agreements applicable to us, including tax or debt limits and debt contracts; and we have identified and disclosed to you all laws, regulations and provisions of contracts and grant agreements that we believe have a direct and material effect on the determination of financial statement amounts, or other financial data significant to the audit objectives, including legal and contractual provisions for reporting specific activities in separate funds.
23. There are no violations or possible violations of budget ordinances, laws and regulations (including those pertaining to adopting, approving, and amending budgets), provisions of contracts and grant agreements, tax or debt limits, and any related debt covenants whose effects should be considered for disclosure in the financial statements, or as a basis for recording a loss contingency, or for reporting on noncompliance.
24. As part of your audit, you assisted with preparation of the financial statements and related notes, state financial report, Public Service Commission annual report, the schedule of expenditures of federal awards, and the schedule of state financial assistance. We have designated an individual with suitable skill, knowledge, or experience to oversee your services and have made all management decisions and performed all management functions. We have reviewed, approved, and accepted responsibility for those financial statements and related notes, state financial report, Public Service Commission annual report, the schedule of expenditures of federal awards, and the schedule of state financial assistance.
25. The City has satisfactory title to all owned assets, and there are no liens or encumbrances on such assets nor has any asset been pledged as collateral.
26. The City has complied with all aspects of contractual agreements that would have a material effect on the financial statements in the event of noncompliance.

27. We have followed all applicable laws and regulations in adopting, approving, and amending budgets.
28. The financial statements include all component units as well as joint ventures with an equity interest, and properly disclose all other joint ventures and other related organizations.
29. The financial statements properly classify all funds and activities.
30. All funds that meet the quantitative criteria in GASB Statement Nos. 34 and 37 for presentation as major are identified and presented as such and all other funds that are presented as major are particularly important to financial statement users.
31. Components of net position (net investment in capital assets, restricted, and unrestricted) and components of fund balance (nonspendable, restricted, committed, assigned and unassigned) are properly classified and, if applicable, approved.
32. Provisions for uncollectible receivables have been properly identified and recorded.
33. Expenses have been appropriately classified in or allocated to functions and programs in the statement of activities, and allocations have been made on a reasonable basis.
34. Revenues are appropriately classified in the statement of activities within program revenues or general revenues.
35. Interfund, internal, and intra-entity activity and balances have been appropriately classified and reported.
36. Deposits and investment securities and derivative transactions are properly classified as to risk and are properly disclosed.
37. Capital assets, including infrastructure and intangible assets, are properly capitalized, reported, and, if applicable, depreciated.
38. We have appropriately disclosed the City's policy regarding whether to first apply restricted or unrestricted resources when an expense is incurred for purposes for which both restricted and unrestricted net position are available and have determined that net position were properly recognized under the policy.
39. We acknowledge our responsibility for presenting the nonmajor fund combining statements, (the supplementary information) in accordance with accounting principles generally accepted in the United States of America, and we believe the supplementary information, including its form and content, is fairly presented in accordance with accounting principles generally accepted in the United States of America. The methods of measurement and presentation of the supplementary information have not changed from those used in the prior period, and we have disclosed to you any significant assumptions or interpretations underlying the measurement and presentation of the supplementary information.
40. The fact that the amount of "uncollateralized" deposits or "uninsured, unregistered securities held by the counterparty, or by its trust department or agent but not in the City's name" during the period significantly exceeded the amounts in those categories as of the balance sheet was properly disclosed in the financial statements.

41. Arrangements with financial institutions involving repurchase, reverse repurchase, or securities lending agreements, compensating balances, or other arrangements involving restrictions on cash balances and line-of-credit or similar arrangements, have been properly recorded or disclosed in the financial statements.
42. The methods and significant assumptions used to determine fair values of financial instruments are as follows: Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. The methods and significant assumptions used result in a measure of fair value appropriate for financial statement measurement and disclosure purposes.
43. Receivables recorded in the financial statements represent valid claims against debtors for transactions arising on or before the balance sheet date and have been appropriately reduced to their estimated net realizable value.
44. Capital assets have been evaluated for impairment as a result of significant and unexpected decline in service utility.
45. With respect to federal and state award programs:
  - a. We are responsible for understanding and complying with and have complied with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* and the *State Single Audit Guidelines* issued by the Wisconsin Department of Administration including requirements relating to preparation of the schedule of federal awards and the schedule of state financial assistance.
  - b. We have prepared the schedule of expenditures of federal awards in accordance with OMB Circular A-133 and the schedule of state financial assistance in accordance with *State Single Audit Guidelines*, and have identified and disclosed in the schedules of expenditures of federal awards and state financial assistance, expenditures made during the audit period for all awards provided by federal and state agencies in the form of grants, cost-reimbursement contracts, loans, loan guarantees, property (including donated surplus property), cooperative agreements, interest subsidies, insurance, food commodities, direct appropriations, and other direct assistance.
  - c. We acknowledge our responsibility for presenting the schedule of expenditures of federal awards (SEFA) in accordance with the requirements of OMB Circular A-133 §310.b and the schedule of state financial assistance (SSFA) in accordance with the requirements of the *State Single Audit Guidelines* and we believe the SEFA and SSFA, including their form and content, are fairly presented in accordance with the Circular and the Guidelines. The methods of measurement and presentation of the SEFA and SSFA have not changed from those used in the prior period and we have disclosed to you any significant assumptions and interpretations underlying the measurement and presentation of the SEFA and SSFA.
  - d. If the SEFA and SSFA are not presented with the audited financial statements, we will make the audited financial statements readily available to the intended users of the SEFA and SSFA information no later than the date we issue the supplementary information and the auditors' report thereon.
  - e. We have identified and disclosed to you all of our government programs and related activities subject to OMB Circular A-133 and the *State Single Audit Guidelines*.

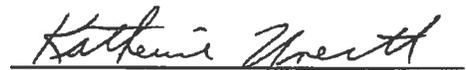
- f. We are responsible for understanding and complying with, and have complied with, the requirements of laws, regulations, and the provisions of contracts and grant agreements related to each of our federal and state programs and have identified and disclosed to you the requirements of laws, regulations, and the provisions of contracts and grant agreements that are considered to have a direct and material effect on each major federal and state program.
- g. We are responsible for establishing and maintaining, and have established and maintained, effective internal control over compliance requirements applicable to federal and state programs that provide reasonable assurance that we are managing our federal and state awards in compliance with laws, regulations, and the provisions of contracts and grant agreements that could have a material effect on our federal and state programs. We believe the internal control system is adequate and is functioning as intended.
- h. We have made available to you all contracts and grant agreements (including amendments, if any) and any other correspondence with federal and state agencies or pass-through entities relating to each major federal and state programs and related activities.
- i. We have received no requests from a federal or state agency to audit one or more specific programs as a major program.
- j. We have complied with the direct and material compliance requirements, (except for noncompliance disclosed to you) including when applicable, those set forth in the *OMB Circular A-133 Compliance Supplement* and the *State Single Audit Guidelines*, relating to federal and state awards and have identified and disclosed to you all amounts questioned and all known noncompliance with the requirements of federal and state awards.
- k. We have disclosed any communications from grantors and pass-through entities concerning possible noncompliance with the direct and material compliance requirements, including communications received from the end of the period covered by the compliance audit to the date of the auditors' report.
- l. We have disclosed to you the findings received and related corrective actions taken for previous audits, attestation engagements, and internal or external monitoring that directly relate to the objectives of the compliance audit, including findings received and corrective actions taken from the end of the period covered by the compliance audit to the date of the auditors' report.
- m. Amounts claimed or used for matching were determined in accordance with relevant guidelines in *OMB Circular A-87, Cost Principles for State, Local, and Tribal Governments*, and *OMB's Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments*.
- n. We have disclosed to you our interpretation of compliance requirements that may have varying interpretations.
- o. We have made available to you all documentation related to compliance with the direct and material compliance requirements, including information related to federal and state program financial reports and claims for advances and reimbursements.
- p. We have disclosed to you the nature of any subsequent events that provide additional evidence about conditions that existed at the end of the reporting period affecting noncompliance during the reporting period.
- q. There are no such known instances of noncompliance with direct and material compliance requirements that occurred subsequent to the period covered by the auditors' report.

- r. No changes have been made in internal control over compliance or other factors that might significantly affect internal control, including any corrective action we have taken regarding significant deficiencies in internal control over compliance (including material weaknesses in internal control over compliance), have occurred subsequent to the date as of which compliance was audited.
  - s. Federal and state program financial reports and claims for advances and reimbursements are supported by the books and records from which the financial statements have been prepared.
  - t. We have charged costs to federal and state awards in accordance with applicable cost principles.
  - u. The copies of federal and state program financial reports provided you are true copies of the reports submitted, or electronically transmitted, to the respective federal and state agency or pass-through entity, as applicable.
  - v. We are responsible for and have accurately prepared the summary schedule of prior audit findings to include all findings required to be included by OMB Circular A-133 and the *State Single Audit Guidelines* and we have provided you with all information on the status of the follow-up on prior audit findings by federal and state awarding agencies and pass-through entities, including all management decisions.
  - w. We are responsible for and have accurately prepared the auditee section of the Data Collection Form as required by OMB Circular A-133.
  - x. We are responsible for preparing and implementing a corrective action plan for each audit finding.
46. We have evaluated and classified any subsequent events as recognized or nonrecognized through the date of this letter. No events, including instances of noncompliance, have occurred subsequent to the balance sheet date and through the date of this letter that would require adjustment to or disclosure in the aforementioned financial statements or in the schedule of findings and questioned costs.

Signed:

  
David Johnson  
City Administrator

Signed:

  
Katherine Unertl  
Finance Director

## SUMMARY FINANCIAL INFORMATION

### 1. City Governmental Fund Balances

Presented below is a summary of the various City governmental fund balances on December 31, 2012, including a comparison to the prior year. This information is provided for assisting management in assessing financial results for 2012 and for indicating financial resources available at the start of the 2013 budget year.

	12/31/12	12/31/11
<b>General Fund</b>		
Nonspendable		
Inventories and prepaid items	\$ 139,085	\$ 138,032
Committed for		
Nonlapsing reserves	478,132	426,345
Assigned for		
Capital improvements	37,856	136,436
Tornado recovery	175,921	12,972
Unassigned	107,292	1,594,870
<b>Total Fund Balance</b>	<b>938,286</b>	<b>2,308,655</b>
<b>Special Revenue Funds</b>		
Community development block grant		
Restricted for community development	367,479	556,982
Library		
Restricted for library endowment	539,280	572,136
Remedial action		
Nonspendable for long-term advances	393,789	410,749
Restricted for landfill monitoring	87,404	73,293
<b>Total Remedial action</b>	<b>481,193</b>	<b>484,042</b>
<b>Total Special Revenue Funds</b>	<b>1,387,952</b>	<b>1,613,160</b>
<b>Debt Service Fund</b>		
Restricted for debt service	6,388	7,089
<b>Capital Projects Funds</b>		
Restricted for TID project plan		
TIF No. 3	264,187	225,810
TIF No. 4	299,008	312,021
Unassigned		
TIF No. 5	(3,221)	(10,792)
TIF No. 6	(502,064)	(388,559)
TIF No. 7	(32,955)	(36,777)
TIF No. 8	(307,599)	(225,310)
<b>Total Capital Projects Funds</b>	<b>(282,644)</b>	<b>(123,607)</b>
<b>Total Governmental Fund Balances</b>	<b>\$ 2,049,982</b>	<b>\$ 3,805,297</b>

## 2. Water Utility Operating Results

A comparative summary of the water utility's operating results for the years ending December 31, 2012 and 2011 follows:

	2012	2011
Operating Revenues		
Charges for services	\$ 1,245,699	\$ 1,271,454
Other	107,935	94,842
Total Operating Revenues	<u>1,353,634</u>	<u>1,366,296</u>
Operating Expenses		
Operation and maintenance	663,573	626,644
Depreciation	321,817	254,916
Total Operating Expenses	<u>985,390</u>	<u>881,560</u>
Operating Income	<u>368,244</u>	<u>484,736</u>
Nonoperating Revenues (Expenses)		
Interest income	6,850	4,271
Merchandising and jobbing	2,573	1,735
Interest and fiscal charges	(10,917)	(11,570)
Total Nonoperating Revenues (Expenses)	<u>(1,494)</u>	<u>(5,564)</u>
Income before transfers and contributions	366,750	479,172
Capital contributions	240,802	4,032
Transfers out - payment in lieu of taxes	<u>(259,011)</u>	<u>(255,237)</u>
Change in Net Position	<u>\$ 348,541</u>	<u>\$ 227,967</u>

The City's water utility reported an operating income of \$368,244 compared to \$484,736 for the prior year. To further evaluate the operating activities, we have calculated the water utility's rate of return below.

Rate of Return - The Public Service Commission of Wisconsin (PSC) de net rate base. Presented below is the calculation of the rates of return for 2012 and 2011 for the water utility based on the format used by the PSC: The PSC operating income differs from the above operating income by the following items:

- The PSC considers the property tax equivalent to be an expense in the year accrued while the property tax equivalent is considered an expense for financial reporting purposes in the year transferred to the City.
- The PSC no longer allows the water utility to recover depreciation on contributed plant from current rates; therefore, this depreciation expense is removed from PSC operating income.

	2012	2011
Rate of Return	<u>2.28%</u>	<u>4.90%</u>

**Summary Comment:** The rate of return generated was lower than the authorized rate of return (6.00%). The water utility reported a cash and investment balance at the December 31, 2012 of \$1,187,645, compared to a balance of \$740,373 at December 31, 2011. The water utility generated cash flows from operations of \$772,495 in 2012 compared to \$679,714 in 2011 and net cash inflow from all activities of \$522,346 in 2012 compared to net cash outflow of \$81,769 in 2011. The positive cash inflow in 2012 was due to the return of an inter-fund advance to the sewer utility and the purchase of capital assets with long term debt.

### 3. Sewer Utility Operating Results

A comparative summary of the sewer utility's operating results for the years ending December 31, 2012 and 2011 follows:

	2012	2011
Operating Revenues		
Charges for services	\$ 1,395,772	\$ 1,386,909
Other	90,894	127,756
Total Operating Revenues	<u>1,486,666</u>	<u>1,514,665</u>
Operating Expenses		
Operation and maintenance	1,242,341	853,629
Depreciation	310,371	305,948
Total Operating Expenses	<u>1,552,712</u>	<u>1,159,577</u>
Operating Income (Loss)	<u>(66,046)</u>	<u>355,088</u>
Nonoperating Revenues (Expenses)		
Interest income	4,604	3,079
Interest expense	(7,715)	(15,348)
Other income	141,089	-
Total Nonoperating Revenues (Expenses)	<u>137,978</u>	<u>(12,269)</u>
Income before contributions	71,932	342,819
Capital contributions	-	5,904
Change in Net Assets	<u>\$ 71,932</u>	<u>\$ 348,723</u>

Because the sewer utility is not regulated by the PSC and treatment plants are typically capital intensive with depreciation expense being a significant component of operating expenses, it is important to consider cash flows when evaluating the sewer utility operating results. For the year ended December 31, 2012, the cash generated by operating activities totaled \$400,062 compared to \$519,415 for 2011. As of December 31, 2012, the sewer utility had a deficit cash from operations of \$166,952, a decrease of \$375,660 from the prior year, and restricted cash and investment balance of \$645,061. The decrease in cash deficit was primarily due to a decrease in 2012 debt service payments. As of December 31, 2012, the future debt services are as follows:

Year Ended December 31	General Obligation	Interest	Total
2013	\$ 29,900	\$ 8,500	\$ 38,400
2014	30,400	7,700	38,100
2015	31,000	6,800	37,800
2016	31,500	6,000	37,500
2017	31,500	6,000	37,500
2018-2022	109,700	12,400	122,100
2023-2026	25,565	2,000	27,565
	<u>\$ 289,565</u>	<u>\$ 49,400</u>	<u>\$ 338,965</u>

## COMMENT AND OBSERVATION

### **GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* and Statement No. 65, *Items Previously Reported as Assets and Liabilities***

For the year ended December 31, 2012, the City implemented Governmental Accounting Standards Board (GASB) Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* and Statement No. 65, *Items Previously Reported as Assets and Liabilities*. These statements are intended to provide users of financial statements with information on how past transactions will impact the City's future financial statements.

The effects on the current year financial statements are to change the classification of "Net Assets" to "Net Position" and to create two additional categories on the Statement of Net Position and the Balance Sheet for deferred outflows and deferred inflows.

A deferred outflow of resources is a consumption of net assets that is applicable to a future reporting period. The only item reported as a deferred outflow in the financial statements occurs in the government-wide and enterprise fund Statements of Net Position for the loss on advance refunding of debt. The City currently does not have any items that qualify for reporting in this category.

A deferred inflow of resources is an acquisition of net assets that is applicable to a future reporting period. The government-wide statement of net position and governmental funds balance sheet report a deferred inflow for the 2013 property tax levy and payment in lieu of taxes. Since the governmental fund financial statements use the modified accrual basis of accounting, there is an additional item reported in those balance sheets for unavailable revenues. The unavailable revenue reported is for special assessments, loans receivables and insurance recovery.

These items have been previously reported in the City's financial statements under "Liabilities", so there is no change to fund balance or net position.

This comment is for informational purposes.