

City of Harbor Springs, Michigan

BASIC FINANCIAL STATEMENTS

December 31, 2014

CITY OF HARBOR SPRINGS, MICHIGAN

ORGANIZATION

MEMBERS OF THE CITY COUNCIL

MAYOR

PRINGLE PFEIFER

MAYOR PRO-TEM

AL DIKA

COUNCIL MEMBER

MATT BUGERA

COUNCIL MEMBER

JEFF JAMES

COUNCIL MEMBER

JOHN CUPPS

APPOINTED OFFICIALS

CITY MANAGER

TOM RICHARDS

CITY CLERK/TREASURER

RON MCRAE

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ANDERSON, TACKMAN & COMPANY, PLC
CERTIFIED PUBLIC ACCOUNTANTS

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INDEPENDENT AUDITOR'S REPORT

Members of the City Council
City of Harbor Springs, Michigan

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 Harbor Springs, Michigan, as of and for the year ended December 31, 2014, 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 Harbor Springs, Michigan, as of December 31, 2014, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, schedule of funding progress and budgetary comparison schedules on pages 4 through 9, page 40 and pages 41 through 44 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Harbor Springs, Michigan's basic financial statements. The combining fund financial statements are presented for purposes of additional analysis and are not a required part of the basic financial statements.

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

Members of the City Council
City of Harbor Springs, Michigan

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated June 12, 2015 on our consideration of the City of Harbor Springs, Michigan's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City of Harbor Springs, Michigan's internal control over financial reporting and compliance.



Anderson, Tackman & Company, PLC
Certified Public Accountants
Kincheloe, Michigan

June 12, 2015

Management's Discussion and Analysis

As management of the City of Harbor Springs, we offer readers of the City's financial statements this narrative overview and analysis of the financial activities of the City for the year ended December 31, 2014.

FINANCIAL HIGHLIGHTS

Our overall financial status improved during the last year. Total net position increased \$101,527 from \$17,593,060 in 2013 to \$17,694,587 in 2014. Net position for the Governmental Activities totaled \$7,448,316, which is a decrease of \$132,636 from the previous year. Net position for the Business-type Activities totaled \$10,246,271, which is an increase of \$234,163 from the previous year.

Governmental activities expenses for the year were \$2,317,250. These activities generated \$361,660 in charges for services, as well as \$203,826 in operating grants and contributions, property taxes of \$1,425,076, business-type activities transfers of \$223,000, state shared revenues of \$91,226, and interest and investment earnings of \$7,982.

Business-type activities operating revenues for the year were \$6,981,472 and operating grants and contributions of \$163,921. Operating expenses were \$6,718,220. Interest and investment earnings were \$17,276 and other revenues were \$12,714. Transfers to governmental activities were \$223,000, made from net revenues and existing assets.

OVERVIEW OF THE FINANCIAL STATEMENTS

The discussion and analysis is intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements are comprised of five components: 1) government-wide financial statements, 2) fund financial statements, 3) notes to the financial statements, 4) required supplementary information, and 5) other information.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

The *government-wide financial statements* are designed to provide readers with a broad overview of the City's finances, in a manner similar to a private-sector business.

The *statement of net position* presents information on all of the City's assets, deferred outflows and liabilities, with the difference between the two reported as *net position*. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the City is improving or deteriorating.

The *statement of activities* presents information showing how the City's net position changed during the year. All changes in net position are reported when the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

Both of the government-wide financial statements distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (*governmental activities*) from functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*). The governmental activities of the City include general government and administration, public safety, public works, and recreation and culture activities. The business-type activities of the City include electric, water and sewer, and waterfront operations.

FUND STATEMENTS

A *fund* is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. All of the funds of the City can be divided into two categories – governmental funds and proprietary funds.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on current sources and uses of spendable resources, as well as on balances of spendable resources available at the end of the year. Such information may be useful in evaluating a government's near-term financing requirements.

The City maintains two types of proprietary funds. Enterprise funds are used to report the same functions as business-type activities in the government-wide financial statements. Internal service funds are an accounting device used to accumulate and allocate costs internally among the City's various functions. The City uses an internal service fund to account for its motor vehicle and equipment usage. Because these services predominately benefit governmental rather than business-type activities function, they have been included with governmental activities in the government-wide financial statements.

FIDUCIARY FUNDS

The City is a trustee or fiduciary for assets that are held for the benefit of third parties. Since these funds cannot be used to address activities or obligations of the City, these funds do not appear in the government-wide financial statements. The City also administers a "Private Purpose Trust Fund". The monies are held in trust for the entities who contribute revenues for the purpose of assisting the University of Michigan with maintaining a Weather Buoy at the mouth of the Little Traverse Bay.

NOTES TO THE FINANCIAL STATEMENTS

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

GOVERNMENT – WIDE FINANCIAL ANALYSIS

The Statement of Net Position, page 10, summarized the City's net position as of December 31, 2014.

At the end of the year, the City of Harbor Springs is able to report positive balances in both categories of net position. A portion of the City's net position is its unrestricted net position, which may be used at the City's discretion to meet on going obligations as well as those designated internally for specific purposes.

The remaining portion of net position is the investment in capital assets (land, buildings, equipment, improvements, construction in progress and infrastructure); less any related debt used to acquire those assets that are still outstanding.

The Statement of Activities, page 11, summarizes the City's operations. The City incurred approximately \$9.0 million in total expenses. These expenses were funded primarily with property taxes, operating grants and contributions, and transfers.

In a condensed format, the table below shows comparison of the net position of the City of Harbor Springs.

**City of Harbor Springs
Statement of Net Position**

	Governmental Activities		Business-type Activities		Total	
	2014	2013	2014	2013	2014	2013
Assets						
Current Assets	\$ 3,942,745	\$ 4,178,533	\$ 6,138,581	\$ 6,351,740	\$ 10,081,326	\$ 10,530,273
Capital Assets and Other	5,222,405	4,999,251	11,960,756	12,223,156	17,183,161	17,222,407
Total Assets	<u>\$ 9,165,150</u>	<u>\$ 9,177,784</u>	<u>\$ 18,099,337</u>	<u>\$ 18,574,896</u>	<u>\$ 27,264,487</u>	<u>\$ 27,752,680</u>
Deferred Outflows of Resources						
Deferred Loss on Refunding Bond	\$ -	\$ -	\$ -	\$ 38,619	\$ -	\$ 38,619
Liabilities						
Current Liabilities	225,647	259,037	750,458	1,189,243	976,105	1,448,280
Noncurrent Liabilities	1,491,187	1,337,795	7,102,608	7,412,164	8,593,795	8,749,959
Total Liabilities	<u>1,716,834</u>	<u>1,596,832</u>	<u>7,853,066</u>	<u>8,601,407</u>	<u>9,569,900</u>	<u>10,198,239</u>
Net Position						
Net Investment in Capital Assets	4,617,405	4,309,251	4,335,700	4,330,794	8,953,105	8,640,045
Unrestricted	2,830,911	3,271,701	5,910,571	5,681,314	8,741,482	8,953,015
Total Net Position	<u>\$ 7,448,316</u>	<u>\$ 7,580,952</u>	<u>\$ 10,246,271</u>	<u>\$ 10,012,108</u>	<u>\$ 17,694,587</u>	<u>\$ 17,593,060</u>

Following is a comparison of the City's changes in net position for the current and prior years:

**City of Harbor Springs
Statement of Activities**

	Governmental Activities		Business-type Activities		Total	
	2014	2013	2014	2013	2014	2013
Program Revenues						
Charges for Services	\$ 361,660	\$ 341,913	\$ 6,981,472	\$ 6,931,428	\$ 7,343,132	\$ 7,273,341
Operating Grants and Contributions	203,826	193,016	163,921	510,206	367,747	703,222
General Revenues						
Property Taxes	1,425,076	1,420,020	-	-	1,425,076	1,420,020
State Shared Revenues	91,226	88,761	-	-	91,226	88,761
Investment Earnings	7,982	8,801	17,276	16,076	25,258	24,877
Other	-	-	12,714	48,101	12,714	48,101
Total Revenues	2,089,770	2,052,511	7,175,383	7,505,811	9,265,153	9,558,322
Program Expenses						
Legislative	936	1,126	-	-	936	1,126
General Government	160,206	376,102	-	-	160,206	376,102
Public Safety	807,725	803,213	-	-	807,725	803,213
Community and Economic Development	36,556	35,765	-	-	36,556	35,765
Public Works	869,093	699,305	-	-	869,093	699,305
Recreation and Culture	305,686	273,850	-	-	305,686	273,850
Other	137,048	105,368	-	-	137,048	105,368
Electric	-	-	4,179,948	4,008,800	4,179,948	4,008,800
Water and Sewer	-	-	1,841,298	1,728,013	1,841,298	1,728,013
Waterfront	-	-	696,974	856,958	696,974	856,958
Total Expenses	2,317,250	2,294,729	6,718,220	6,593,771	9,035,470	8,888,500
Changes in Net Position Before Transfers	(227,480)	(242,218)	457,163	912,040	229,683	669,822
Transfers - Net	223,000	223,000	(223,000)	(223,000)	-	-
Changes in Net Position	(4,480)	(19,218)	234,163	689,040	229,683	669,822
Net Position - Beginning	7,580,952	7,600,170	10,012,108	9,323,068	17,593,060	16,923,238
Prior Period Adjustment	(128,156)	-	-	-	(128,156)	-
Net Position - Ending	\$ 7,448,316	\$ 7,580,952	\$ 10,246,271	\$ 10,012,108	\$ 17,694,587	\$ 17,593,060

FUND ANALYSIS

At the end of the year, the governmental funds reported a combined fund balance of \$2,657,501, which was \$184,155 lower than at the beginning of the year.

The proprietary funds net position increased \$234,163 to \$10,246,271. The Electric Fund generated revenues of \$4,652,986, the Water and Sewer Fund generated revenues of \$1,955,798 and the Waterfront Fund generated revenues of \$566,599.

GENERAL FUND BUDGETARY HIGHLIGHTS

Overall revenues were \$9,502 less than budgeted and expenditures were \$111,993 less than budgeted. Combined, the General Fund has a favorable budget variance of \$102,491, excluding transfers.

CAPITAL ASSETS AND LONG-TERM DEBT ACTIVITY

At the end of the year the capital assets, net of accumulated depreciation and long-term debt (excluding vested employee benefits and discounts) were:

Capital Assets

Governmental Activities:	\$	5,222,405
Business-type Activities:	\$	11,718,389

Long-Term Debt

Governmental Activities:	\$	605,000
Business-type Activities	\$	7,425,000

At the end of 2014, the City had \$5,222,405 invested in a broad range of capital assets, including land, buildings and improvements, utility systems improvements and equipment.

The City reduced its total debt load by \$355,000 in principal payments in fiscal year 2014, ending with a total debt balance of \$8,030,000 excluding vested employee benefits and bond discounts.

FACTORS AFFECTING FUTURE OPERATIONS AND ECONOMIC CONDITIONS OF THE CITY

The City has several capital improvement projects planned for 2015. The first is a street and utility project with an estimated cost of \$550,000. The City also has several electric system projects planned for 2015. Those projects have an estimated cost of \$392,000. The City also has budgeted approximately \$275,000 in vehicle and equipment purchases.

During 2016, the City is planning an upgrade on East Third Street for the Electric System. As yet we do not have an estimated cost.

The City is committed to maintaining its assets. Further, because the City believes that its Street Funds will be at a low cash level at the end of 2015, the City is going to put a ballot question before the taxpayers at the November General Election to levy up to one (1) mill for street maintenance, construction and design purposes. One mill will generate approximately \$237,000. The City plans to only levy what it needs to build up the cash balance to address the projects that may come along.

CONTACTING THE CITY'S MANAGEMENT

This financial report is intended to provide our citizens, taxpayers, customers and investors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have any questions about this report or need additional information, we welcome you to contact the City at (231) 526-2104.

Basic Financial Statements

**Statement of Net Position
December 31, 2014**

	Primary Government		Totals
	Governmental Activities	Business-type Activities	
ASSETS:			
Cash and Equivalents - Unrestricted	\$ 3,192,903	\$ 4,890,321	\$ 8,083,224
Cash and Equivalents - Restricted	-	150,878	150,878
Receivables:			
Interest	922	1,261	2,183
Accounts	31,000	762,300	793,300
Due from Governmental Units	374,176	-	374,176
Due from Others	247,630	554	248,184
Internal Loans	14,810	(14,810)	-
Inventory	54,107	314,856	368,963
Prepaid Items	27,197	33,221	60,418
MPPA Working Capital Advance	-	242,367	242,367
Capital Assets (Not Depreciated)	1,214,067	446,301	1,660,368
Capital Assets (Net of Accumulated Depreciation)	4,008,338	11,272,088	15,280,426
TOTAL ASSETS	\$ 9,165,150	\$ 18,099,337	\$ 27,264,487
LIABILITIES:			
Accounts Payable	\$ 52,000	\$ 141,693	\$ 193,693
Accrued Liabilities	61,342	137,349	198,691
Deposits Payable	-	150,878	150,878
Due to Governmental Units	32,305	-	32,305
Due to Others	-	116	116
Unearned Revenue	-	25,422	25,422
Bonds Payable - Due within one year	80,000	295,000	375,000
Bonds Payable - Due in more than one year	525,000	7,087,689	7,612,689
Other Post Employment Benefits - Due in more than one year	919,784	-	919,784
Vested Employee Benefits - Due in more than one year	46,403	14,919	61,322
TOTAL LIABILITIES	1,716,834	7,853,066	9,569,900
NET POSITION:			
Net Investment in Capital Assets	4,617,405	4,335,700	8,953,105
Unrestricted	2,830,911	5,910,571	8,741,482
TOTAL NET POSITION	\$ 7,448,316	\$ 10,246,271	\$ 17,694,587

City of Harbor Springs, Michigan

Statement of Activities For the Year Ended December 31, 2014

Functions/Programs	Expenses	Program Revenues		Net (Expense) Revenue and Changes in Net Position		
		Charges for Services	Operating Grants and Contributions	Primary Government		
				Governmental Activities	Business-type Activities	Total
Primary Government:						
Governmental Activities:						
Legislative	\$ 936	\$ -	\$ -	\$ (936)	\$ -	\$ (936)
General Government	160,206	33,637	1,933	(124,636)	-	(124,636)
Public Safety	807,725	137,016	-	(670,709)	-	(670,709)
Community and Economic Development	36,556	-	-	(36,556)	-	(36,556)
Public Works	869,093	72,058	201,893	(595,142)	-	(595,142)
Recreation and Culture	305,686	22,658	-	(283,028)	-	(283,028)
Other	137,048	96,291	-	(40,757)	-	(40,757)
Total Governmental Activities	<u>2,317,250</u>	<u>361,660</u>	<u>203,826</u>	<u>(1,751,764)</u>	<u>-</u>	<u>(1,751,764)</u>
Business-type activities:						
Electric	4,179,948	4,633,958	-	-	454,010	454,010
Water and Sewer	1,841,298	1,946,925	-	-	105,627	105,627
Waterfront	696,974	400,589	163,921	-	(132,464)	(132,464)
Total Business-type Activities	<u>6,718,220</u>	<u>6,981,472</u>	<u>163,921</u>	<u>-</u>	<u>427,173</u>	<u>427,173</u>
Total Primary Government	<u>\$ 9,035,470</u>	<u>\$ 7,343,132</u>	<u>\$ 367,747</u>	<u>(1,751,764)</u>	<u>427,173</u>	<u>(1,324,591)</u>
General Revenues and Transfers:						
Property Taxes						
Operating				1,425,076	-	1,425,076
State Shared Revenue				91,226	-	91,226
Investment Earnings				7,982	17,276	25,258
Transfers				223,000	(223,000)	-
Other				-	12,714	12,714
Total General Revenues and Transfers				<u>1,747,284</u>	<u>(193,010)</u>	<u>1,554,274</u>
Changes in Net Position				(4,480)	234,163	229,683
Net Position - Beginning				7,580,952	10,012,108	17,593,060
Prior Period Adjustment				(128,156)	-	(128,156)
Net Position - Ending				<u>\$ 7,448,316</u>	<u>\$ 10,246,271</u>	<u>\$ 17,694,587</u>

See accompanying notes to financial statements.

City of Harbor Springs, Michigan

Balance Sheet Governmental Funds December 31, 2014

	General	Major Streets	Local Streets	Nonmajor Downtown Development Authority	Total Governmental Funds
ASSETS:					
Cash and Equivalents - Unrestricted	\$ 1,596,911	\$ 148,961	\$ 298,303	\$ -	\$ 2,044,175
Receivables:					
Interest	469	36	82	-	587
Accounts	1,955	23,051	5,994	-	31,000
Due from Other Funds	71,254	15,620	5,987	5	92,866
Due from Others	247,630	-	-	-	247,630
Due from Governmental Units	374,176	-	-	-	374,176
Inventory	54,107	-	-	-	54,107
Prepaid Items	22,861	97	52	251	23,261
TOTAL ASSETS	\$ 2,369,363	\$ 187,765	\$ 310,418	\$ 256	\$ 2,867,802
LIABILITIES:					
Accounts Payable	\$ 43,965	\$ 3,911	\$ 3	\$ -	\$ 47,879
Accrued Liabilities	52,776	1,213	1,003	-	54,992
Due to Other Funds	21,100	10,444	43,576	5	75,125
Due to Governmental Units	32,305	-	-	-	32,305
TOTAL LIABILITIES	150,146	15,568	44,582	5	210,301
FUND BALANCES:					
Nonspendable	76,968	97	52	251	77,368
Committed	46,403	-	-	-	46,403
Restricted	-	172,100	265,784	-	437,884
Assigned	67,792	-	-	-	67,792
Unassigned	2,028,054	-	-	-	2,028,054
TOTAL FUND BALANCES	2,219,217	172,197	265,836	251	2,657,501
TOTAL LIABILITIES AND FUND BALANCES	\$ 2,369,363	\$ 187,765	\$ 310,418	\$ 256	

Reconciliation to amounts reported for governmental activities in the statement of net position:

Capital assets used by governmental activities	3,988,835
Long term bonds payable for governmental activities	(605,000)
Internal Service Funds included in governmental activities	2,373,167
Other post employment benefits liability	(919,784)
Vested employee benefits liability	(46,403)
Net position of governmental activities	\$ 7,448,316

City of Harbor Springs, Michigan

Statement of Revenues, Expenditures, and Changes in Fund Balance - Governmental Funds For the Year Ended December 31, 2014

	General	Major Streets	Local Streets	Nonmajor Downtown Development Authority	Totals Governmental Funds
REVENUES:					
Taxes	\$ 1,425,076	\$ -	\$ -	\$ -	\$ 1,425,076
Licenses and Permits	6,391	-	-	-	6,391
State Sources	93,159	143,731	58,162	-	295,052
Administrative Fees	377,827	-	-	-	377,827
Charges for Services	179,639	-	-	-	179,639
Fines and Forfeitures	3,613	-	-	-	3,613
Interest	6,034	407	1,541	-	7,982
Other Revenue	99,959	71,770	288	-	172,017
TOTAL REVENUES	2,191,698	215,908	59,991	-	2,467,597
EXPENDITURES:					
Legislative	936	-	-	-	936
General Government	627,471	-	-	-	627,471
Public Safety	782,408	-	-	-	782,408
Public Works	317,634	413,453	134,456	-	865,543
Community and Economic Development	30,176	-	-	6,380	36,556
Recreation and Culture	316,634	-	-	-	316,634
Debt Service	101,560	-	-	-	101,560
Other Expenditures	35,488	-	-	-	35,488
TOTAL EXPENDITURES	2,212,307	413,453	134,456	6,380	2,766,596
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	(20,609)	(197,545)	(74,465)	(6,380)	(298,999)
OTHER FINANCING SOURCES (USES):					
Operating Transfers In	276,000	191,500	50,000	6,631	524,131
Operating Transfers Out	(95,131)	-	(186,000)	-	(281,131)
TOTAL OTHER FINANCING SOURCES (USES)	180,869	191,500	(136,000)	6,631	243,000
EXCESS (DEFICIENCY) OF REVENUES AND OTHER FINANCING SOURCES OVER EXPENDITURES AND OTHER FINANCING USES	160,260	(6,045)	(210,465)	251	(55,999)
FUND BALANCES, JANUARY 1	2,187,113	178,242	476,301	-	2,841,656
Prior Period Adjustment	(128,156)	-	-	-	(128,156)
FUND BALANCES, DECEMBER 31	\$ 2,219,217	\$ 172,197	\$ 265,836	\$ 251	\$ 2,657,501

**Reconciliation of the Statement of Revenues, Expenditures,
and Changes in Fund Balances of Governmental Funds
to the Statement of Activities
For the Year Ended December 31, 2014**

Net Changes in fund balances - total governmental funds \$ (55,999)

The change in net position reported for governmental activities in the statement of activities is different because:

Governmental funds reported capital outlays as expenditures.

However, in the statement of activities the cost of those assets is capitalized and the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.

This is the amount by which capital outlay of \$607,295 exceeded depreciation expense of (\$211,611) and a deduction of construction in progress of (\$272,143) in the current period.

123,541

Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net position.

Principal payments

85,000

An internal service fund is used by management to charge the costs of certain activities, such as equipment costs, to individual funds. The net revenue (expense) of the internal service funds is reported with governmental activities.

76,370

Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the funds:

Vested employee benefits

(12,158)

Other post employment benefits

(221,234)

Changes in net position of governmental activities

\$ (4,480)

**Statement of Net Position
Proprietary Funds
December 31, 2014**

	Business-type Activities Enterprise Funds				Governmental Activities	
	Electric	Water & Sewer		Waterfront	Totals	Internal Service
ASSETS:						
Cash and Equivalents - Unrestricted	\$ 2,681,180	\$ 1,666,686	\$ 542,455	\$ 4,890,321	\$ 1,148,728	
Cash and Equivalents - Restricted	109,833	15,550	25,495	150,878	-	
Receivables:						
Interest	723	432	106	1,261	335	
Accounts	584,664	177,636	-	762,300	-	
Due from Others	-	-	554	554	-	
Due from Other Funds	5,508	43,947	115	49,570	2,282	
Inventory	274,923	39,933	-	314,856	-	
Prepaid Expenses	14,117	10,732	8,372	33,221	3,936	
MPPA Working Capital Advance	242,367	-	-	242,367	-	
Capital Assets (Not Depreciated)	1,294	125,928	319,079	446,301	36,640	
Capital Assets (Net of Accumulated Depreciation)	2,078,994	8,570,583	622,511	11,272,088	1,196,930	
TOTAL ASSETS	<u>5,993,603</u>	<u>10,651,427</u>	<u>1,518,687</u>	<u>18,163,717</u>	<u>2,388,851</u>	
LIABILITIES:						
Accounts Payable	\$ 88,674	\$ 37,010	\$ 16,009	\$ 141,693	\$ 4,121	
Accrued Liabilities	34,839	102,066	444	137,349	6,350	
Deposits Payable	109,833	15,550	25,495	150,878	-	
Due to Other Funds	31,101	27,127	6,152	64,380	5,213	
Due to Others	-	116	-	116	-	
Unearned Revenue	-	25,422	-	25,422	-	
Vested Employee Benefits - Due in more than one year	13,574	1,345	-	14,919	-	
Bonds Payable - Due within one year	-	295,000	-	295,000	-	
Bonds Payable - Due in more than one year	-	7,087,689	-	7,087,689	-	
TOTAL LIABILITIES	<u>278,021</u>	<u>7,591,325</u>	<u>48,100</u>	<u>7,917,446</u>	<u>15,684</u>	
NET POSITION:						
Net Investment in Capital Assets	2,080,288	1,313,822	941,590	4,335,700	1,233,570	
Unrestricted	3,635,294	1,746,280	528,997	5,910,571	1,139,597	
TOTAL NET POSITION	<u>\$ 5,715,582</u>	<u>\$ 3,060,102</u>	<u>\$ 1,470,587</u>	<u>\$ 10,246,271</u>	<u>\$ 2,373,167</u>	

**Statement of Revenues, Expenses, and
Changes in Net Position - Proprietary Funds
For the Year Ended December 31, 2014**

	Business-type Activities			Governmental Activities	
	Enterprise Funds				
	Electric	Water & Sewer	Waterfront		Totals
OPERATING REVENUES:					
Charges for Services	\$ 4,633,958	\$ 1,946,925	\$ 400,589	\$ 6,981,472	\$ 445,037
Total Operating Revenues	<u>4,633,958</u>	<u>1,946,925</u>	<u>400,589</u>	<u>6,981,472</u>	<u>445,037</u>
OPERATING EXPENSES:					
Personal Services	485,266	279,972	125,051	890,289	65,358
Purchased Power	2,921,387	-	-	2,921,387	-
Metered Sewage	-	344,048	-	344,048	-
Contractual Services	119,115	65,403	335,422	519,940	52,546
Other Supplies and Expenses	439,855	213,938	128,274	782,067	138,249
Insurance	5,574	3,511	2,295	11,380	15,565
Utilities	60,534	37,714	39,775	138,023	10,734
Depreciation	148,217	324,562	66,157	538,936	78,930
Total Operating Expenses	<u>4,179,948</u>	<u>1,269,148</u>	<u>696,974</u>	<u>6,146,070</u>	<u>361,382</u>
OPERATING INCOME (LOSS)	<u>454,010</u>	<u>677,777</u>	<u>(296,385)</u>	<u>835,402</u>	<u>83,655</u>
NON-OPERATING REVENUES (EXPENSES):					
Interest Income	10,049	5,648	1,579	17,276	4,667
Interest Expense	-	(572,150)	-	(572,150)	-
State Grants	-	-	163,921	163,921	-
Gain on Sale of Capital Assets	-	-	-	-	7,001
Other Revenue	8,979	3,225	510	12,714	1,047
Total Non-Operating Revenues (Expenses)	<u>19,028</u>	<u>(563,277)</u>	<u>166,010</u>	<u>(378,239)</u>	<u>12,715</u>
Income (Loss) before transfers	473,038	114,500	(130,375)	457,163	96,370
Transfers Out	<u>(223,000)</u>	<u>-</u>	<u>-</u>	<u>(223,000)</u>	<u>(20,000)</u>
CHANGES IN NET POSITION	250,038	114,500	(130,375)	234,163	76,370
NET POSITION, JANUARY 1	<u>5,465,544</u>	<u>2,945,602</u>	<u>1,600,962</u>	<u>10,012,108</u>	<u>2,296,797</u>
NET POSITION, DECEMBER 31	<u><u>\$ 5,715,582</u></u>	<u><u>\$ 3,060,102</u></u>	<u><u>\$ 1,470,587</u></u>	<u><u>\$ 10,246,271</u></u>	<u><u>\$ 2,373,167</u></u>

**Statement of Cash Flows
Proprietary Funds
For the Year Ended December 31, 2014**

	Business-type Activities			Governmental	
	Enterprise Funds			Activities	
	Electric	Water & Sewer	Waterfront	Internal Service	
CASH FLOWS FROM OPERATING ACTIVITIES:					
Receipts from Customers	\$ 4,605,985	\$ 2,100,172	\$ 737,728	\$ 7,443,885	\$ 443,972
Payments to Suppliers	(3,640,377)	(776,104)	(888,063)	(5,304,544)	(231,665)
Payments to Employees	(487,147)	(202,824)	(126,399)	(816,370)	(63,185)
Net Cash Provided (Used) by Operating Activities	<u>478,461</u>	<u>1,121,244</u>	<u>(276,734)</u>	<u>1,322,971</u>	<u>149,122</u>
CASH FLOWS FROM NONCAPITAL AND RELATED FINANCING ACTIVITIES:					
Transfers In (Out)	(223,000)	-	-	(223,000)	(20,000)
State Grants	-	-	163,921	163,921	-
Gain on Sale of Capital Assets	-	-	-	-	7,001
Other Revenue	8,979	3,225	510	12,714	1,047
Net Cash Provided (Used) by Noncapital and Related Financing Activities	<u>(214,021)</u>	<u>3,225</u>	<u>164,431</u>	<u>(46,365)</u>	<u>(11,952)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:					
Purchase/Disposal of Capital Assets	(62,035)	(133,347)	(81,155)	(276,537)	(178,543)
Interest Payments	-	(572,150)	-	(572,150)	-
Principal Payments	-	(224,995)	-	(224,995)	-
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>(62,035)</u>	<u>(930,492)</u>	<u>(81,155)</u>	<u>(1,073,682)</u>	<u>(178,543)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:					
Interest Income	10,049	5,648	1,579	17,276	4,667
Net Cash Provided (Used) by Investing Activities	<u>10,049</u>	<u>5,648</u>	<u>1,579</u>	<u>17,276</u>	<u>4,667</u>
Net Increase (Decrease) in Cash and Equivalents	212,454	199,625	(191,879)	220,200	(36,706)
Balances - Beginning of the Year	<u>2,578,559</u>	<u>1,482,611</u>	<u>759,829</u>	<u>4,820,999</u>	<u>1,185,434</u>
Balances - End of the Year	<u>\$ 2,791,013</u>	<u>\$ 1,682,236</u>	<u>\$ 567,950</u>	<u>\$ 5,041,199</u>	<u>\$ 1,148,728</u>
Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities:					
Operating Income (Loss)	\$ 454,010	\$ 677,777	\$ (296,385)	\$ 835,402	\$ 83,655
Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities:					
Depreciation Expense	148,217	324,562	66,157	538,936	78,930
Change in Assets and Liabilities:					
(Increase) Decrease in Assets:					
Accounts Receivable	(24,421)	(5,912)	338,850	308,517	56
Interest Receivable	(561)	(270)	(19)	(850)	(197)
Due from Others	-	11	554	565	(1,628)
Due from Other Funds	(2,991)	(9,271)	(333)	(12,595)	-
Inventory	(418)	908	-	490	-
Prepaid Expenses	(4,750)	(4,308)	(1,913)	(10,971)	704
Bond Issue and Discount	-	172,089	-	172,089	-
Increase (Decrease) in Liabilities:					
Accounts Payable	(58,408)	(71,578)	(383,305)	(513,291)	(13,248)
Deposits Payable	2,763	-	(1,810)	953	-
Accrued Expenses	(2,588)	95,105	(1,348)	91,169	2,173
Compensated Absences	707	(17,957)	-	(17,250)	-
Due to Other Funds	(33,099)	2,818	2,818	(27,463)	(1,323)
Unearned Revenue	-	(42,730)	-	(42,730)	-
Net Cash Provided (Used) by Operating Activities	<u>\$ 478,461</u>	<u>\$ 1,121,244</u>	<u>\$ (276,734)</u>	<u>\$ 1,322,971</u>	<u>\$ 149,122</u>

**Statement of Fiduciary Net Position
Fiduciary Funds
December 31, 2014**

	Private Purpose	
	Weather	
	Buoy Trust	Agency Funds
ASSETS:		
Cash and Equivalents - Unrestricted	\$ 7,254	\$ 836,244
Accrued Interest	2	-
Accounts Receivable	-	6,234
Due from Others	-	116
Taxes Receivable	-	1,794,876
TOTAL ASSETS	\$ 7,256	\$ 2,637,470
LIABILITIES:		
Accounts Payable	\$ 324	\$ 5,092
Due to County	-	134,705
Due to School	-	1,186,002
Due to State	-	60,067
Due to ISD	-	499,665
Due to College	-	445,072
Due to Cemetery	-	10,687
Due to Ambulance and EMS	-	44,910
Due to Others	4,503	251,270
TOTAL LIABILITIES	4,827	\$ 2,637,470
NET POSITION:		
Restricted for Private Purpose	\$ 2,429	

**Statement of Changes in Fiduciary Net Position
Fiduciary Fund
For the Year Ended December 31, 2014**

	<u>Private Purpose Weather Buoy Trust</u>
ADDITIONS:	
Contributions	\$ 4,000
Interest Income	28
Miscellaneous	<u> 2</u>
 Total Additions	 <u> 4,030</u>
 DEDUCTIONS:	
Contractual Services	<u> 1,601</u>
 Change in Net Position	 2,429
 Net Position - Beginning Balance	 <u> -</u>
 Net Position - Ending Balance	 <u><u> \$ 2,429</u></u>

Notes to Financial Statements

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

The City of Harbor Springs (the City) was incorporated October 6, 1932, under the provisions of Act 279, P.A. 1909, as amended (Home Rule City Act). The City operates under a Council-Manager form of government and provides the following services as authorized by its charter: public safety (police and fire), highways and streets, sanitation, health and social services, culture and recreation, public improvements, planning and zoning, and general administrative services.

Reporting Entity

In accordance with the provisions of the Governmental Accounting Standards Board (GASB) Statement No. 14, as amended by GASB No. 39 and 61; no other governmental organizations are considered to be part of the reporting entity for financial statement purposes. The criteria established by GASB Statement No. 14, as amended by GASB No. 39 and 61; for various governmental organizations to be included in the reporting entity's financial statement include legal separation, financial accountability and fiscal dependency.

Jointly Governed Organization

The Harbor Springs Area Sewage Disposal Authority (the "Authority") was created as a corporate instrumentality in 1969 under provisions of Act 233, Michigan Public Acts of 1955, as amended. The local governmental units comprising the Authority include the City of Harbor Springs, the Village of Alanson, and Little Traverse and Littlefield Townships. The Authority owns and operates a sewage disposal utility system consisting of a site, a treatment plant, a collection system and a related water system. In addition, the Authority operates sewage disposal utility systems belonging to Springvale-Bear Creek Sewage Disposal Authority and West Traverse Township and a water system belonging to Little Traverse Township under terms of operating contracts.

The Harbor Springs Area Fire Authority (the "Authority") was created as a corporate instrumentality in 1992 under provisions of Act 57, Michigan Public Acts of 1988. The local governments comprising the Authority include the City of Harbor Springs, Little Traverse, West Traverse and Pleasantview Townships. The Authority provides fire protection, equipment and services to these municipalities. The Authority is not included in any other governmental "reporting entity" as defined by GASB 14, since none of these governmental units appoint a majority of the Authority's board, the board members have decision making authority, the authority to set rates, the power to designate management, the ability to significantly influence operations and primary accountability for fiscal matters.

The Harbor-Petoskey Area Airport Authority (the "Authority") is a nonprofit Michigan corporation created January 13, 1988, under the authority of Act 206, Michigan Public Acts of 1957, as amended. The purpose of the Authority is to plan, promote, construct, improve, own (or lease), maintain and operate an airport for the benefit of the participating local units of government by providing services to airport users. A Board consisting of one member from each of the following local units of government, all located in Emmet County, Michigan, governs the Authority:

- | | |
|------------------------|-----------------------------|
| City of Petoskey | Township of Little Traverse |
| City of Harbor Springs | Township of West Traverse |
| Township of Bear Creek | Township of Pleasantview |

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (Continued)

Basis of Presentation

Government-wide Statements: The statement of net position and the statement of activities display information about the primary government (the City). These statements include the financial activities of the overall government, except for fiduciary activities. Eliminations have been made to minimize the double counting of internal activities. These statements distinguish between the *governmental* and *business-type activities* of the City. Governmental activities generally are financed through taxes, intergovernmental revenues, and other nonexchange transactions. Business-type activities are financed in whole or in part by fees charged to external parties.

The statement of activities presents a comparison between direct expenses and program revenues for the different business-type activities of the City and for each function of the City's governmental activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function. Indirect expense allocations that have been made in the funds have been reversed for the statement of activities. Program revenues include (a) fees, fines, and charges paid by the recipients of goods or services offered by the programs and (b) grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues.

Fund Financial Statements: The fund financial statements provide information about the City's funds, including its fiduciary-funds. Separate statements for each fund category – *governmental*, *proprietary*, and *fiduciary* – are presented. The emphasis of fund financial statements is on major governmental and enterprise funds, each displayed in a separate column. All remaining funds are aggregated and reported as nonmajor funds.

Proprietary fund operating revenues, such as charges for services and sales, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Non-operating revenues, such as subsidies and investment earnings, result from nonexchange transactions or ancillary activities.

The City reports the following major governmental funds:

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

Major and Local Streets. The Streets Funds account for the operation of the street departments. Primary financing is provided by the City's share of state gasoline taxes. State law requires these gasoline taxes be used to maintain streets.

The City reports the following major enterprise funds:

Electric. This fund is financed and operated in a manner similar to a private enterprise. The intent is that costs (expenses, including depreciation) of providing electricity to the general public are recovered through user charges.

Water and Sewer. This fund is financed and operated in a manner similar to a private enterprise. The intent is that costs (expenses, including depreciation) of providing water and sewer services to the general public are recovered through user charges.

Waterfront. This fund is financed and operated in a manner similar to a private enterprise. The intent is that costs (expenses, including depreciation) of providing City boat docking and mooring services to the general public are recovered through user charges.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (Continued)

The City reports the following nonmajor governmental funds:

Downtown Development Authority Fund. This fund accounts for amounts collected and services provided to downtown development.

The City reports the following internal service fund:

Motor Vehicle and Equipment Fund. The Motor Vehicle and Equipment fund accounts for the cost of acquiring, maintaining and providing vehicle and equipment usage to various City departments.

The City reports the following fiduciary funds:

The fiduciary funds are used to account for assets held by the City in a trustee or agent capacity. Since, by definition, these assets are held for the benefit of a third party (other local government, private parties, pension participants, etc.) and cannot be used to address activities or obligations of the government, these funds are not incorporated into the government-wide statements.

Agency funds use the accrual basis of accounting; however report only assets and liabilities.

Tax Collection Fund. This fund accounts for the collection and payment of property tax levies.

West Traverse Township Water Fund. The West Township Water Fund accounts for the Township's usage of the City's water system.

Trust funds use the accrual basis of accounting, reporting assets, liabilities, net position and changes in net position.

Weather Buoy Fund. The Weather Buoy Fund accounts for funding provided by the City's of Charlevoix, Petoskey and Harbor Springs as well as Bay Harbor Lake Marina, Irish Boat Ship, Walstrom Marine, and the members of Bay Harbor and Little Traverse Yacht Clubs. The funding is used to maintain a University of Michigan weather buoy.

Measurement Focus, Basis of Accounting

Government-wide, Proprietary, and Fiduciary Fund Financial Statements. The government-wide, proprietary, and fiduciary fund financial statements are reported using the economic resources measurement focus. The government-wide and proprietary fund financial statements are reported using the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place. Nonexchange transactions, in which the City gives (or receives) value without directly receiving (or giving) equal value in exchange, include taxes, grants, entitlements, and donations. On an accrual basis, revenue from taxes is recognized in the fiscal year for which taxes are levied. Revenue from grants, entitlements, and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (Continued)

Governmental Fund Financial Statements. Governmental funds are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Under this method, revenues are recognized when measurable and available. The City considers all revenues reported in the governmental funds to be available if the revenues are collected within sixty days after year-end. Property taxes, sales taxes, franchise taxes, licenses, and interest are considered to be susceptible to accrual. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on long-term debt, claims and judgments, and compensated absences, which are recognized as expenditures to the extent they have matured. General capital asset acquisitions are reported as expenditures in governmental funds. Proceeds of long-term debt and acquisitions under capital leases are reported as other financing sources.

Under the terms of grant agreements, the City funds certain programs by a combination of specific cost-reimbursement grants, categorical block grants, and general revenues. Thus, when program expenses are incurred, there is both restricted and unrestricted net position available to finance the program. It is the City's policy to first apply cost-reimbursement grant resources to such programs, followed by categorical block grants, and then by general revenues.

Cash and Equivalents

The City considers cash and cash equivalents to be cash on hand and demand deposits and investments with a maturity of 90 days or less. Pooled investment income from all funds is allocated to each fund based on average cash balance. Deposits are recorded at cost.

Interfund Receivables and Payables

In general, outstanding balances between funds are reported as "due to/from other funds." Activity between funds that is representative of lending/borrowing arrangements outstanding at the end of the fiscal year is referred to as "advances to/from other funds. Any residual balances outstanding between the governmental activities and the business-type activities are reported in the government-wide financial statements as "internal balances."

Inventories

Inventories are valued at cost using the first-in/first-out (FIFO) method. The costs of governmental fund-type inventories are recorded as expenditures when consumed rather than when purchased. Inventory in the Historical Commission consists of books and essay's which are recorded as expenditures when sold rather than when purchased.

Receivables

All receivables are reported at their gross value.

The City has not established an allowance for uncollectible accounts since, in the opinion of management the amount is not significant.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (Continued)

Capital Assets

Capital assets, which include property, buildings, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks and similar items), are reported in the applicable governmental or business-type activities column in the government-wide financial statements. Capital assets are recorded by the City when the initial individual costs are equal to or greater than the following amounts:

<u>Asset Type</u>	<u>Amount</u>
Land	\$ 1
Equipment	3,000
Buildings & Building Improvements	10,000
Infrastructure	10,000

Capital 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.

Capital assets of the primary government are depreciated using the straight-line method over the following estimated useful lives:

Buildings	40 to 60 years
Building Improvements	20 to 60 years
Water and Sewer Lines	50 to 75 years
Streets, Curbs and Gutters	10 to 30 years
Electric Lines and Appurtenances	30 to 50 years
Vehicles (Pickup Trucks & Automobiles)	3 to 7 years
Vehicles (Large Trucks and Fire Trucks)	10 to 25 years
Construction Equipment (Front End Loaders)	5 to 15 years
Office Equipment	5 to 7 years
Office Furniture	5 to 15 years

Deferred Outflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense/expenditure) until then. The City has no items that qualify for reporting in this category.

Deferred Inflows of Resources

In addition to liabilities, the statement of net position and governmental funds balance sheet will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The City has no items that qualify for reporting in this category.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (Continued)**Use of Estimates**

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and affect the disclosure of contingent assets and liabilities at the date of financial statements. These estimates and assumptions also affect the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Long-Term Obligations

In the government-wide financial statements and the proprietary fund financial statements, long-term debt and other long-term obligations are reported as liabilities. Bond premiums and discounts, are deferred and amortized over the life of the bonds.

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 reports as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts are reported as other financing uses.

Vested Employee Benefits (Vacation and Sick Time)

Vacation days not used during the year may be carried over with limits for union and nonunion employees. Nonunion employees may convert unused vacation days to sick leave. Due to contract years differing from the City's fiscal year, unpaid vacation time represents unused, but not accumulated, vacation time. Sick time not used during the year may be accumulated. Upon retirement or death of an employee, he/she or his/her beneficiary is eligible to receive accumulated sick leave pay, up to a maximum dollar amount. All vacation, sick pay and other employee benefit amounts accrue when earned in the government-wide and proprietary fund financial statements. Sick and vacation pay are recognized in the governmental fund financial statements when the time is used.

Fund Balance Classification

The governmental fund financial statements present fund balances based on classifications that comprise a hierarchy that is based primarily on the extent to which the City is bound to honor constraints on the specific purposes for which amounts in the respective governmental funds can be spent. The classifications used in the governmental fund financial statements are as follows:

- **Nonspendable**: This classification includes amounts that cannot be spent because they are either (a) not in spendable form or (b) are legally or contractually required to be maintained intact. The City has classified Inventories and Prepaid Items as being Nonspendable as these items are not expected to be converted to cash within the next year.
- **Restricted**: This classification includes amounts for which constraints have been placed on the use of the resources either (a) externally imposed by creditors (such as through a debt covenant), grantors, contributors, or laws or regulations of other governments, or (b) imposed by law through constitutional provisions or enabling legislation.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (Continued)

- Committed: This classification includes amounts that can be used only for specific purposes pursuant to constraints imposed by formal action of the City. These amounts cannot be used for any other purpose unless the City removes or changes the specified use by taking the same type of action that was employed when the funds were initially committed. This classification also includes contractual obligations to the extent that existing resources have been specifically committed for use in satisfying those contractual requirements. The City has vested employee benefits classified in this category.
- Assigned: This classification includes amounts that are constrained by the City's intent to be used for a specific purpose but are neither restricted nor committed. This intent can be expressed by the City through the budgetary process. This classification also includes the remaining positive fund balance for all governmental funds except for the General Fund.
- Unassigned: This classification includes the residual fund balance for the General Fund. The unassigned classification also includes negative residual fund balance of any other governmental fund that cannot be eliminated by offsetting of Assigned fund balance amounts.

The City would typically use Restricted fund balances first, followed by Committed resources, and then Assigned resources, as appropriate opportunities arise, but reserves the right to selectively spend Unassigned resources first to defer the use of these other classified funds.

NOTE 2 - STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY:

Annual budgets are adopted on a basis consistent with generally accepted accounting principles for all operating funds of the City except for the agency funds. Budgetary control is legally maintained at the fund level.

The City follows these procedures in establishing the budgetary data reflected in the financial statements:

1. Prior to December 1, the City Manager submits to the City Council a proposed operating budget for the fiscal year commencing the following January 1. The operating budget includes proposed expenditures/expenses and the means of financing them.
2. A public hearing is conducted at City Hall to obtain taxpayer comments.
3. Prior to January 1, the fund budgets are legally enacted through passage of resolutions.
4. The City Manager is authorized to transfer budgeted amounts between departments within any fund; however, any revisions that alter the total expenditures/expenses of any fund must be approved by the City Council.
5. Formal budgetary integration is employed as a management control device during the year for the General and Special Revenue Funds.
6. Budgeted amounts are as originally adopted, or as amended by the City Council.
7. All appropriations lapse at year-end.

The General Fund Budgetary information includes administrative charges by the General Fund to various other funds as revenue of the General Fund. They have been offset against General Fund expenditures in the preparation of the basic financial statements as reimbursements. These reimbursements remain as administrative expenditures/expenses of the various funds charged in the basic financial statements.

NOTE 3 - CASH AND EQUIVALENTS:

	<u>Primary Government</u>	<u>Fiduciary Funds</u>
Cash and Equivalents:		
- Unrestricted	\$ 8,083,224	\$ 843,498
- Restricted	<u>150,878</u>	<u>-</u>
Total	<u>\$ 8,234,102</u>	<u>\$ 843,498</u>
Imprest	\$ 720	\$ -
CD's, Savings and Checking	8,186,564	843,498
MBIA Class Investment	<u>46,818</u>	<u>-</u>
Total	<u>\$ 8,234,102</u>	<u>\$ 843,498</u>

Cash and Equivalents – Restricted:

The following funds have restricted cash for various purposes:

Primary Government:

<u>Fund Type/Fund</u>	<u>Purpose</u>	<u>Amount</u>
Electric:	Customer Deposits	\$ 109,833
Water/Sewer:	Customer Deposits	15,550
Waterfront:	Customer Deposits	<u>25,495</u>
		<u>\$ 150,878</u>

Investment and Deposit Risk

Interest rate risk. State law limits the allowable investments and the maturities of some of the allowable investments as identified in the following list of authorized investments. The City's investment policy does not have specific limits in excess of state law on investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit risk. The City's investment policy does not have specific limits in excess of state law on investment credit risk. The City's investment in MBIA's Michigan Class Investment pool of \$46,818 was rated AA by Standard and Poors.

Custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the City's deposits may not be returned. State law does not require and the City does not have a policy for deposit custodial credit risk. As of year end, \$6,754,289 of the City's bank balance of \$7,754,389 was exposed to credit risk because it was uninsured and uncollateralized.

NOTE 3 - CASH AND EQUIVALENTS: (Continued)

Custodial investment credit risk. For investments, custodial credit risk is the risk that, in the event of the failure of the counterparty, the City will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. As of December 31, 2014, none of the City's investments are held in the City's name by the counter party.

Statutory Authority:

Public Act 152, entitled "An act relative to the investment of funds of public corporations of the state; and to validate certain investments," by amending section 1 (MCL 129.91), as amended by 2009 PA 21.

Except as provided in section 5, the governing body by resolution may authorize its investment officer to invest the funds of that public corporation in one or more of the following:

- a. Bonds, securities, and other obligations of the United States or an agency or instrumentality of the United States.
- b. Certificates of deposit, savings accounts, or depository receipts of a financial institution, but only if the financial institution complies with subsection (2); certificates of deposit obtained through a financial institution as provided in subsection (5); or deposit accounts of a financial institution as provided in subsection (6).
- c. Commercial paper rated at the time of purchase within the two highest classifications established by not less than two standard rating services and matures not more than 270 days after the date of purchase.
- d. Repurchase agreements consisting of instruments listed in subdivision (a).
- e. Bankers' acceptances of United States banks.
- f. Obligations of this state or any of its political subdivisions that at the time of purchase are rated as investment grade by not less than one standard rating service.
- g. Mutual funds registered under the investment company act of 1940, 15 USC 80a-1 to 80a-64, with authority to purchase only investment vehicles that are legal for direct investment by a public corporation. However, a mutual fund is not disqualified as a permissible investment solely by reason of any of the following:
 - (i) The purchase of securities on a when-issued or delayed delivery basis.
 - (ii) The ability to lend portfolio securities as long as the mutual fund receives collateral at all times equal to at least 100% of the value of the securities loaned.
 - (iii) The limited ability to borrow and pledge a like portion of the portfolio's assets for temporary or emergency purposes.
- h. Obligations described in subdivisions (a) through (g) if purchased through an interlocal agreement under the urban cooperation act of 1967, 1967 (Ex Sess) PA 7, MCL 124.501 to 124.512.
- i. Investment pools organized under the surplus funds investment pool act, 1982 PA 367, MCL 129.111 to 129.118.
- j. The investment pools organized under the local government investment pool act, 1985 PA 121, MCL 129.141 to 129.150.

NOTE 4 - INTERFUND RECEIVABLES, PAYABLES, AND TRANSFERS:

The City of Harbor Springs reports interfund balances between many of its funds. Some of the balances are considered immaterial and are aggregated into a single column or row. The total of all balances agrees with the sum of interfund balances presented in the statements of net position/balance sheet for governmental funds, proprietary funds, and fiduciary funds.

Interfund balances at December 31, 2014 consisted of the following:

		DUE FROM								
DUE TO		General	Major	Local	Nonmajor		Water		Internal	
		Fund	Streets	Streets	Governmental	Electric	and Sewer	Waterfront	Service	Total
	General Fund	\$ 6,631	\$ 5,709	\$ 131	\$ -	\$ 4,073	\$ 3,185	\$ 115	\$ 1,256	\$ 21,100
	Major Streets	3,848	-	5,856	-	-	-	-	740	10,444
	Local Streets	2,556	-	-	-	-	40,762	-	258	43,576
	Nonmajor Governmental	-	-	-	5	-	-	-	-	5
	Electric	31,101	-	-	-	-	-	-	-	31,101
	Water and Sewer	15,772	9,911	-	-	1,435	-	-	9	27,127
	Waterfront	6,133	-	-	-	-	-	-	19	6,152
	Internal Service	5,213	-	-	-	-	-	-	-	5,213
	Total	<u>\$ 71,254</u>	<u>\$ 15,620</u>	<u>\$ 5,987</u>	<u>\$ 5</u>	<u>\$ 5,508</u>	<u>\$ 43,947</u>	<u>\$ 115</u>	<u>\$ 2,282</u>	<u>\$ 144,718</u>

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

NOTE 4 - INTERFUND RECEIVABLES, PAYABLES, AND TRANSFERS: (Continued)

Interfund transfers for the year ended December 31, 2014 consisted of the following:

		TRANSFERS (OUT)				
		General Fund	Local Streets	Electric	Internal Service	Total
TRANSFERS IN	General Fund	\$ 33,000	\$ -	\$ 223,000	\$ 20,000	\$ 276,000
	Major Streets	5,500	186,000	-	-	191,500
	Local Streets	50,000	-	-	-	50,000
	Nonmajor Governmental	6,631	-	-	-	6,631
	Total	<u>\$ 95,131</u>	<u>\$ 186,000</u>	<u>\$ 223,000</u>	<u>\$ 20,000</u>	<u>\$ 524,131</u>

Transfers are used to (1) move revenues from the fund that statute or budget requires to collect them to the fund that statute or budget requires to expend them, (2) moves receipts restricted to debt service from the funds collecting the receipts to the debt service fund as debt service payments become due, and (3) use unrestricted revenues collected in the general fund to finance various programs accounted for in other funds in accordance with budgetary authorizations.

NOTE 5 - CAPITAL ASSETS:

Capital asset activity for the year ended December 31, 2014, was as follows:

	<u>Beginning Balances</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balances</u>
Governmental Activities:				
<i>Capital assets not depreciated:</i>				
Land	\$ 937,904	\$ 260,000	\$ -	\$ 1,197,904
Construction in progress	288,306	-	(272,143)	16,163
Subtotal	<u>1,226,210</u>	<u>260,000</u>	<u>(272,143)</u>	<u>1,214,067</u>
<i>Capital assets being depreciated:</i>				
Buildings and improvements	3,369,300	22,107	-	3,391,407
Street, curbs, sidewalks and storm sewers	4,731,479	312,484	-	5,043,963
Office furniture and equipment	225,744	-	(65,290)	160,454
Machinery and equipment	1,724,444	191,247	(87,231)	1,828,460
Subtotal	<u>10,050,967</u>	<u>525,838</u>	<u>(152,521)</u>	<u>10,424,284</u>

NOTE 5 - CAPITAL ASSETS: (Continued)

	<u>Beginning Balances</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balances</u>
Governmental Activities: (Continued)				
<i>Less accumulated depreciation for:</i>				
Buildings and improvements	(847,750)	(74,605)	-	(922,355)
Street, curbs, sidewalks & storm sewers	(3,865,913)	(139,231)	-	(4,005,144)
Office furniture & equipment	(184,173)	(16,913)	65,290	(135,796)
Machinery & equipment	(1,380,090)	(59,792)	87,231	(1,352,651)
Subtotal	<u>(6,277,926)</u>	<u>(290,541)</u>	<u>152,521</u>	<u>(6,415,946)</u>
Net Capital Assets Being Depreciated	<u>3,773,041</u>	<u>235,297</u>	<u>-</u>	<u>4,008,338</u>
Capital Assets – Net	<u>\$ 4,999,251</u>	<u>\$ 495,297</u>	<u>\$ (272,143)</u>	<u>\$ 5,222,405</u>

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

Governmental Activities:		
General Government		\$ 113,804
Public Safety		25,317
Public Works		140,261
Recreation and Culture		<u>11,159</u>
Total Governmental Activities		<u>\$ 290,541</u>

	<u>Beginning Balances</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balances</u>
Business-type Activities:				
<i>Capital assets not depreciated:</i>				
Land	\$ 357,201	\$ 17,093	\$ -	\$ 374,294
Construction in progress	<u>90,091</u>	<u>96,909</u>	<u>(114,993)</u>	<u>72,007</u>
Subtotal	<u>447,292</u>	<u>114,002</u>	<u>(114,993)</u>	<u>446,301</u>
<i>Capital assets being depreciated:</i>				
Buildings and improvements	2,237,488	32,705	-	2,270,193
Utility system improvements	15,805,941	244,823	-	16,050,764
Equipment	<u>105,738</u>	<u>-</u>	<u>-</u>	<u>105,738</u>
Subtotal	<u>18,149,167</u>	<u>277,528</u>	<u>-</u>	<u>18,426,695</u>
<i>Less accumulated depreciation for:</i>				
Buildings and improvements	(1,558,581)	(66,128)	-	(1,624,709)
Utility system improvements	(4,977,612)	(465,979)	-	(5,443,591)
Equipment	<u>(79,478)</u>	<u>(6,829)</u>	<u>-</u>	<u>(86,307)</u>
Subtotal	<u>(6,615,671)</u>	<u>(538,936)</u>	<u>-</u>	<u>(7,154,607)</u>
Net Capital Assets Being Depreciated	<u>11,533,496</u>	<u>(261,408)</u>	<u>-</u>	<u>11,272,088</u>
Capital Assets – Net	<u>\$ 11,980,788</u>	<u>\$ (147,406)</u>	<u>\$ (114,993)</u>	<u>\$ 11,718,389</u>

NOTE 5 - CAPITAL ASSETS: (Continued)

Depreciation was charged to the business-type activities as follows:

Business-type Activities:	
Electric	\$ 148,217
Water and Sewer	324,562
Waterfront	<u>66,157</u>
Total Business-type Activities	<u>\$ 538,936</u>

NOTE 6 - LONG-TERM DEBT:

General Long-Term Debt - The bonds payable reflected in the basic financial statements consist of general obligation notes incurred by the City of Harbor Springs. The City has pledged the general full faith and credit of the City for the payment of principal and interest on the bonds.

Changes in long-term debt during the twelve months ending December 31, 2014 are summarized as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Deductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Governmental Activities:					
\$800,000, 2012 Harbor Springs Refunding LTGO bonds, due in annual installments of \$50,000 to \$85,000 through October 1, 2022; interest at 2.4%	\$ 690,000	\$ -	\$ 85,000	\$ 605,000	\$ 80,000
Vested Employee Benefits – net addition	<u>34,245</u>	<u>12,158</u>	<u>-</u>	<u>46,403</u>	<u>-</u>
Total Governmental Activities	<u>724,248</u>	<u>12,158</u>	<u>85,000</u>	<u>651,403</u>	<u>80,000</u>
Business-type Activities:					
\$1,875,000, 2012 Harbor Springs General Obligation Bonds, due in annual installments of \$25,000 to \$150,000 through October 1, 2031; interest ranging from 2.00% to 3.10%.	1,850,000	-	50,000	1,800,000	50,000
\$2,200,000, 2011 Harbor Springs General Obligation Bonds, due in annual installments of \$50,000 to \$200,000 through October 1, 2030; interest ranging from 2.50% to 4.0%.	2,150,000	-	50,000	2,100,000	75,000
\$2,300,000, 2009 Harbor Springs General Obligation Bonds, due in annual installments of \$50,000 to \$200,000 through October 1, 2029; interest ranging from 2.50% to 4.00%.	2,100,000	-	100,000	2,000,000	100,000

NOTE 6 - LONG-TERM DEBT: (Continued)

	Beginning Balance	Additions	Deductions	Ending Balance	Due Within One Year
Business-type Activities: (Continued)					
\$1,595,000, 2013 Harbor Springs Refunding LTGO Bonds, due in annual installments of \$70,000 to \$120,000 through October 1, 2030; interest at 3.45%.	1,595,000	-	70,000	1,525,000	70,000
Discounts	(45,005)	-	2,694	(42,311)	-
Vested Employee Benefits – net deduction	32,169	-	17,250	14,919	-
Total Business-type Activities	<u>7,682,164</u>	<u>-</u>	<u>289,944</u>	<u>7,397,608</u>	<u>295,000</u>
TOTAL LONG TERM DEBT	<u>\$ 8,406,409</u>	<u>\$ 12,158</u>	<u>\$ 374,944</u>	<u>\$ 8,049,011</u>	<u>\$ 375,000</u>

Annual debt service requirements to maturity for the above obligations are as follows:

Year End December 31	Governmental Activities		Business-type Activities	
	Principal	Interest	Principal	Interest
2015	\$ 80,000	\$ 14,520	\$ 295,000	\$ 250,863
2016	80,000	12,600	300,000	242,823
2017	80,000	10,680	325,000	234,360
2018	75,000	8,760	360,000	225,398
2019	75,000	6,960	360,000	215,215
2020-2024	215,000	10,200	2,250,000	886,300
2025-2029	-	-	2,915,000	449,204
2030-2031	-	-	620,000	26,690
Total	<u>\$ 605,000</u>	<u>\$ 63,720</u>	<u>\$ 7,425,000</u>	<u>\$ 2,530,853</u>

NOTE 7 - LEASE OBLIGATIONS:

The City has entered into lease agreements with the Harbor Springs Area Fire Authority for fire protection services. The City uses the land, building, and equipment to provide fire protection service to the constituent municipalities making up the Harbor Springs Area Fire Authority.

The current lease agreements with the Authority call for annual lease payments from the Authority to the City of \$50 for the land and building lease, and annual payments for the City to the Authority of \$5 for the sublease of land and buildings, and \$5 for the lease of fire protection equipment.

The City has a lease agreement with the Harbor-Petoskey Area Airport Authority for airport related services. The City leases real and personal property to the Authority in consideration for those airport services as well as \$1 per year. The lease term of 25 years is extended each year unless either the leaser or tenant gives notice to fix the term.

NOTE 7 - LEASE OBLIGATIONS: (Continued)

The City has a lease agreement with the State of Michigan Department of Natural Resources ('DNR') for a parcel of Lake Michigan bottomland where the City's East Dock is located. The original lease terms call for annual payments to the DNR. The terms allow for annual renewal at the City's option. The lease amount for the year ending December 31, 2014 was \$5,423.

The City also has a lease agreement with the State of Michigan Department of Natural Resources ('DNR') for the mooring fields and extends until 2031. The lease fees are 10% of annual mooring revenues, payable each January 1st. For the year ended December 31, 2014, the lease fees were \$7,645.

The City has a lease agreement with the State of Michigan Department of Environmental Quality ('DEQ') for a parcel of land where the City's courtesy dock is located, and extends until 2022.

The City has entered into a lease agreement with the Harbor Springs Historical Society. The City leases the old Historic City Hall to the society for purposes of a museum. The term of the lease is for 25 years with an option to renew for an extended two years. Rent is ten dollars a year and is payable on May 1.

NOTE 8 - VESTED EMPLOYEE BENEFITS:

A summary of vested employee benefits payable at December 31, 2014 is as follows:

	<u>Beginning Balance</u>	<u>Additions/ (Decreases) (net)</u>	<u>Ending Balance</u>
Sick Leave Payable	\$ <u>66,414</u>	\$ <u>(5,092)</u>	\$ <u>61,322</u>

Accumulated unpaid sick leave for police and other City employees is recorded in the basic financial statements. Based upon union contracts and personnel policies, as of December 31, 2014, the liability totaled \$61,322.

NOTE 9 - PROPERTY TAXES:

City property taxes are attached as an enforceable lien on property as of December 31 of the prior year. Real property taxes not collected as of March 1 are transferred to Emmet County for collection, which advances the City 100% for the delinquent taxes. Collection of delinquent personal property taxes remains the responsibility of the City Treasurer.

Property taxes levied in July of each year are recognized as revenue in that year.

The taxable value of real and personal property located in the City at December 31, 2014 totaled \$231,807,967. The tax levy for that year was based on the following rates:

	<u>Millage Rate</u>
General Operating	5.7600

NOTE 10- DEFINED BENEFIT PENSION PLAN:

The City of Harbor Springs participates in a statewide government agent multiple-employer public pension plan which covers substantially all employees.

Plan Description

The City contributes to the Municipal Employees Retirement System, an agent multiple employer public employee retirement system that acts as a common investment and administrative agent for units of local government in Michigan. The system provides the following provisions: normal retirement, deferred retirement and service retirement to plan members and their beneficiaries. All full-time employees become a member of the System on the first day of employment, and are completely vested after 10 years of service. Service retirement allowances are based upon percentages ranging from 1 to 2.5 percent of 3 to 5-year final average compensation depending on benefit program selected and social security coverage, etc. The most recent period of which actuarial data was available was for the fiscal year ended December 31, 2013.

MERS was organized pursuant to Section 12a of Act #156, Public Acts of 1851 (MSA 5.333 (a); MCLA 46.12 (a), as amended, State of Michigan. MERS is regulated under Act No. 427 of Public Acts of 1984, sections of which have been approved by the State Pension Commission. MERS issues a publicly available financial report that includes financial statements and required supplementary information for the system. That report may be obtained by writing to the MERS at 1134 Municipal Way, Lansing, Michigan 48917-9755.

Funding Policy

The obligation to contribute to and maintain the system for these employees was established by negotiation with the City's collective bargaining unit and personnel policy, which requires employees to contribute to the plan. The City is required to contribute at an actuarially determined rate.

The contribution rate as a percentage of payroll at December 31, 2013 is as follows:

General – All Employees	10.71%
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Annual Pension Cost

During the fiscal year ended December 31, 2014, the City's contributions totaling \$138,878 were made in accordance with contribution requirement determined by an actuarial valuation of the plan as of December 31, 2012. The employer contribution rate is limited to 10% of the City's gross wages per employee. Under the entry age normal cost funding method, the total employer contribution is comprised of the normal cost plus the level annual percentage of payroll payment required to amortize the unfunded actuarial accrued liability over 26 years. The employer normal cost is, for each employee, the level of percentage of payroll contribution (from entry age to retirement) required to accumulate sufficient assets at the members retirement to pay for this projected benefit. Significant actuarial assumptions used include a long-term investment yield rate of 8 percent and annual salary increases of 1.0 percent based on an age-related scale to reflect merit, longevity, and promotional salary increases.

NOTE 10 - DEFINED BENEFIT PENSION PLAN: (Continued)

Three year trend information as of December 31 follows:

Year Ended Dec 31	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
2012	\$ 129,721	100%	0
2013	129,792	100%	0
2014	138,878	100%	0

NOTE 11 - COMMITMENTS AND CONTINGENCIES:

Grant Assistance - The City received significant financial assistance from state and federal agencies in the form of various grants. The disbursement of funds received under these programs generally requires compliance with terms and conditions specified in the grant agreement and are subject to audit by the grantor agency. Any disallowed claims resulting from such audits could become a liability of the applicable fund of the City. However, in the opinion of management, any such disallowed claims will not have a material effect on any of the financial statements of the individual fund types included herein or on the overall financial position of the City at December 31, 2014.

Bonds Payable - The City has pledged its full faith and credit for payment of principal and interest of the various bond issues of the Water and Sewer Fund. The general obligation bonds payable for the Water and Sewer Fund are recorded as liabilities in the Enterprise Fund.

Property Taxes - In accordance with an agreement, Emmet County annually purchases real property taxes and delinquent special assessments (included on the tax bills) which have not been paid as of March 1 from the City. The County has recourse against the City for amounts which remain unpaid.

NOTE 12 - RISK MANAGEMENT:

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City was unable to obtain general liability insurance at a cost it considered to be economically justifiable. The City joined together with other governments and created a public entity risk pool currently operating as a common risk management and insurance program. The government pays an annual premium to the pool for its automobile, property, general liability, and Worker’s Compensation insurance coverage. The agreement provides that the pool will be self-sustaining through member premiums and will reinsure through commercial companies for claims in excess of \$250 for each insured event.

The City continues to carry commercial insurance for all other risks of loss. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

The pooling agreement allows for the pool to make additional assessments to make the pool self-sustaining. The City is unable to provide an estimate of the amounts of any potential additional assessments.

NOTE 13 - RELATED PARTIES:

The Harbor Springs Area Sewage Disposal Authority, (the “Authority”) was created by the City of Harbor Springs and the Village of Alanson, Little Traverse Township, and Littlefield Township to provide sewer services for the municipalities. In 2005, the Bear Creek Township became a member of the Authority. The five units bill and collect charges to the public for the private use of the system. The Authority in turn bills the five municipalities for use and debt service fees. During 2014, the City was billed for sewer services and debt service in the amount of \$146,500.

NOTE 14- OTHER POST EMPLOYMENT BENEFITS:

Plan Description. The City provides post-employment health care benefits to all retired employees and/or their spouse and life insurance benefits for one retiree only. The benefits are provided in accordance with the union agreement, which includes the provision that upon a retiree and/or spouse’s eligibility for Medicare, the City agrees to pay for the supplemental health insurance coverage for both.

For all employees the City agrees to pay the premium for each employee and their spouse at time of retirement. Employees may elect to have coverage provided to children at the employee’s expense.

In order for an employee to be eligible for health care benefits at retirement, the employee must retire from active service with the City at age 60 with 10 years of service for Division 1 (general) or at age 50 with 25 years of service for Division 2 (police). The City pays one year of Post Retirement Benefits for every 5 years of service.

Funding Policy. Contribution requirements also are negotiated between the City and employees. The City contributes a portion of the cost of current-year premiums for eligible retired plan members. For fiscal year 2014, the City contributed \$7,336 to the plan. Total member contributions were \$0.

Annual OPEB Cost and Net OPEB Obligation. The City’s annual other post employment benefit (OPEB) cost (expense) is calculated based on the annual required contribution of the employer (ARC). The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. The following table shows the components of the City’s annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the City’s net OPEB obligation to the Retiree Health Plan:

Annual required contribution	\$ 218,727
Interest on net OPEB obligation	<u>9,843</u>
Annual OPEB cost (expense)	228,570
Contributions made	<u>(7,336)</u>
Increase in net OPEB obligation	221,234
Net OPEB obligation – beginning of year	<u>698,550</u>
Net OPEB obligation – end of year	<u>\$ 919,784</u>

NOTE 14- OTHER POST EMPLOYMENT BENEFITS (Continued)

The City’s annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for fiscal years 2012, 2013, and 2014 are as follows:

<u>Fiscal Year End</u>	<u>Annual OPEB Cost</u>	<u>Percentage of Annual OPEB Cost Contributed</u>	<u>Net Increase In OPEB Obligation</u>
2012	\$ 223,384	11%	\$ 197,821
2013	222,921	6%	209,821
2014	228,570	3%	221,234

Funded Status and Funding Progress. As of December 31, 2011, the actuarial accrued liability for benefits was \$1,569,585, all of which was unfunded. The covered payroll (annual payroll of active employees covered by the plan) was unavailable, and the ratio of the unfunded actuarial accrued liability to the covered payroll was unavailable.

Actuarial valuation of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Actuarial Methods and Assumptions. Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan member to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the December 31, 2011, actuarial valuation, the entry age actuarial cost method was used. The actuarial assumptions included a 8.0% investment rate of return (net of administrative expenses), which is a blended rate of the expected long-term investment returns on plan assets and on the employer’s own investments calculated based on the funded level of the plan at the valuation date, and an annual healthcare cost trend rate of 10% initially, reduced by decrements to an ultimate rate of 4.5% after ten years. Both rates included a percent inflation assumptions. The actuarial value of assets was determined using techniques that spread the effects of short-term volatility in the market value of investments over a five-year period. The UAAL is being amortized as a level percentage of projected payroll on an open basis.

NOTE 15 - SUBSEQUENT EVENTS:

During February 2015, the City approved purchases of various equipment and repair/construction contracts in the amount of \$113,000. Also, the City awarded the construction contract for the Beach Drive Project in the amount of \$708,000. Total costs incurred as of the opinion date for this project amounted to \$180,000.

NOTE 16 - PRIOR PERIOD ADJUSTMENT:

The fund balance of the General Fund was decreased by \$128,156 due to an error in posting fire authority fees. The cumulative effect on prior excess revenues was also \$128,156.

Required Supplementary Information

Required Supplementary Information
Employee Retirement and Benefit Systems
Schedule of Funding Progress
December 31, 2014

Pension:

Three year trend information as of December 31 follows:

	<u>2011</u>	<u>2012</u>	<u>2013</u>
Actuarial Value of Assets	\$ 2,746,761	\$ 2,933,041	\$ 3,179,074
Actuarial Accrued Liability	4,102,915	4,370,513	4,639,988
Unfunded AAL	1,356,154	1,437,472	1,460,914
Funded Ratio	67%	67%	69%
Covered Payroll	1,282,871	1,337,109	1,352,958
UAAL as a Percentage of Covered Payroll	106%	108%	108%

Health Plan:

<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets (a)</u>	<u>Actuarial Liability (AAL) - Entry Age (b)</u>	<u>Unfunded AAL (UAAL) (b - a)</u>	<u>Funded Ratio (a / b)</u>	<u>Covered Payroll (c)</u>	<u>UAAL as a Percent of Covered Payroll ((b - a) / c)</u>
2008	\$ -	\$ 1,761,852	\$ 1,761,852	0%	Unavailable	0%
2011	\$ -	\$ 1,569,585	1,569,585	0%	Unavailable	0%

Required Supplementary Information
Budgetary Comparison Schedule
General Fund
For the Year Ended December 31, 2014

	Budgeted Amounts		Actual Amounts	Variance with
	Original	Final		Final Budget - Positive (Negative)
REVENUES:				
Taxes	\$ 1,424,800	\$ 1,452,200	\$ 1,425,076	\$ (27,124)
Licenses and Permits	4,900	6,300	6,391	91
State Sources	90,500	88,900	93,159	4,259
Administrative Fees	386,400	386,400	377,827	(8,573)
Charges for Services	197,300	197,400	179,639	(17,761)
Fines and Forfeitures	5,100	5,200	3,613	(1,587)
Interest	3,900	3,900	6,034	2,134
Other Revenue	26,700	60,900	99,959	39,059
TOTAL REVENUES	2,139,600	2,201,200	2,191,698	(9,502)
EXPENDITURES:				
Legislative:				
City Council	2,700	1,100	936	164
General Government:				
Manager	122,000	123,900	120,078	3,822
Elections	14,200	13,200	9,411	3,789
Accounting	115,900	115,200	109,673	5,527
Assessing	51,000	43,600	40,543	3,057
Legal Services	62,000	46,100	51,674	(5,574)
Clerk	173,800	173,300	172,396	904
Finance Treasurer	63,900	64,500	72,230	(7,730)
City Hall and Grounds	49,800	55,700	51,466	4,234
Total General Government	652,600	635,500	627,471	8,029
Public Safety:				
Police Department	635,700	629,700	601,321	28,379
Fire Department	224,400	210,200	181,087	29,113
Total Public Safety	860,100	839,900	782,408	57,492
Public Works:				
Cost of Sales and Services	1,400	1,400	333	1,067
Brush and Refuse Pick Up	51,700	46,800	38,480	8,320
Leaf Pickup	46,600	42,900	31,952	10,948
Sidewalks	33,200	30,700	26,432	4,268
Parking Lots	32,400	40,600	40,460	140
D.P.W. Administration	161,200	167,000	171,316	(4,316)
Airport Activities	8,800	8,800	8,661	139
Total Public Works	335,300	338,200	317,634	20,566
Community and Economic Development:				
Planning and Zoning	38,200	35,400	30,176	5,224
Recreation and Culture:				
SK-8 Park	64,200	66,200	65,532	668
Beach	44,000	37,300	35,864	1,436
Sledhill Program	5,700	6,200	6,557	(357)
Ice Rink	37,500	34,700	37,963	(3,263)
Parks and Grounds	129,000	127,700	110,393	17,307
Deer Park	8,300	9,000	7,419	1,581
Tree Maintenance	27,900	23,200	16,602	6,598
Community Promotion	15,400	14,700	13,105	1,595
Historical Society	36,600	27,600	23,199	4,401
Total Recreation and Culture	368,600	346,600	316,634	29,966

**Required Supplementary Information
Budgetary Comparison Schedule
General Fund
For the Year Ended December 31, 2014**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget - Positive (Negative)
	Original	Final		
Debt Service:				
City Hall and Grounds	101,600	101,600	101,560	40
Other Expenditures:				
Other	23,400	26,000	35,488	(9,488)
TOTAL EXPENDITURES	2,382,500	2,324,300	2,212,307	111,993
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	(242,900)	(123,100)	(20,609)	102,491
OTHER FINANCING SOURCES (USES):				
Operating Transfers In	276,000	276,000	276,000	-
Operating Transfers Out	(93,000)	(94,300)	(95,131)	(831)
EXCESS (DEFICIENCY) OF REVENUES AND OTHER FINANCING SOURCES OVER EXPENDITURES AND OTHER FINANCING USES	<u>\$ (59,900)</u>	<u>\$ 58,600</u>	160,260	<u>\$ 101,660</u>
FUND BALANCE, JANUARY 1			2,187,113	
Prior Period Adjustment			(128,156)	
FUND BALANCE, DECEMBER 31			<u>\$ 2,219,217</u>	

**Required Supplementary Information
Budgetary Comparison Schedule
Major Streets Fund
For the Year Ended December 31, 2014**

	Budgeted Amounts		Actual Amounts	Variance with
	Original	Final		Final Budget - Positive (Negative)
REVENUES:				
State Sources	\$ 124,000	\$ 145,000	\$ 143,731	\$ (1,269)
Interest	500	300	407	107
Other Revenue	80,000	5,800	71,770	65,970
TOTAL REVENUES	204,500	151,100	215,908	64,808
EXPENDITURES:				
Public Works	418,900	513,300	413,453	99,847
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	(214,400)	(362,200)	(197,545)	164,655
OTHER FINANCING SOURCES (USES):				
Operating Transfers In	274,300	293,200	191,500	(101,700)
EXCESS (DEFICIENCY) OF REVENUES AND OTHER FINANCING SOURCES OVER EXPENDITURES AND OTHER FINANCING USES	\$ 59,900	\$ (69,000)	(6,045)	\$ 62,955
FUND BALANCE, JANUARY 1			178,242	
FUND BALANCE, DECEMBER 31			\$ 172,197	

**Required Supplementary Information
Budgetary Comparison Schedule
Local Streets Fund
For the Year Ended December 31, 2014**

	Budgeted Amounts		Actual Amounts	Variance with
	Original	Final		Final Budget - Positive (Negative)
REVENUES:				
State Sources	\$ 43,000	\$ 52,000	\$ 58,162	\$ 6,162
Interest	4,000	1,500	1,541	41
Other Revenue	300	300	288	(12)
TOTAL REVENUES	<u>47,300</u>	<u>53,800</u>	<u>59,991</u>	<u>6,191</u>
EXPENDITURES:				
Public Works	109,000	141,500	134,456	7,044
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	(61,700)	(87,700)	(74,465)	13,235
OTHER FINANCING SOURCES (USES):				
Operating Transfers In	50,000	50,000	50,000	-
Operating Transfers Out	(265,300)	(222,400)	(186,000)	36,400
TOTAL OTHER FINANCING SOURCES (USES)	<u>(215,300)</u>	<u>(172,400)</u>	<u>(136,000)</u>	<u>36,400</u>
EXCESS (DEFICIENCY) OF REVENUES AND OTHER FINANCING SOURCES OVER EXPENDITURES AND OTHER FINANCING USES	<u>\$ (277,000)</u>	<u>\$ (260,100)</u>	(210,465)	<u>\$ 49,635</u>
FUND BALANCE, JANUARY 1			<u>476,301</u>	
FUND BALANCE, DECEMBER 31			<u>\$ 265,836</u>	

Other Information

**Combining Balance Sheet
General Funds
December 31, 2014**

	General	Historical Society	Totals
ASSETS:			
Cash and Equivalents - Unrestricted	\$ 1,528,921	\$ 67,990	\$ 1,596,911
Receivables:			
Interest	448	21	469
Accounts	847	1,108	1,955
Due from Other Funds	71,254	-	71,254
Due from Others	247,630	-	247,630
Due from Governmental Units	374,176	-	374,176
Inventory	25,216	28,891	54,107
Prepaid Items	22,732	129	22,861
TOTAL ASSETS	\$ 2,271,224	\$ 98,139	\$ 2,369,363
LIABILITIES:			
Accounts Payable	\$ 43,379	\$ 586	\$ 43,965
Accrued Liabilities	52,035	741	52,776
Due to Other Funds	21,100	-	21,100
Due to Governmental Units	32,305	-	32,305
TOTAL LIABILITIES	148,819	1,327	150,146
FUND BALANCES:			
Nonspendable	47,948	29,020	76,968
Committed	46,403	-	46,403
Assigned	-	67,792	67,792
Unassigned	2,028,054	-	2,028,054
TOTAL FUND BALANCES	2,122,405	96,812	2,219,217
TOTAL LIABILITIES AND FUND BALANCES	\$ 2,271,224	\$ 98,139	\$ 2,369,363

**Combining Statement of Revenues, Expenditures, and
Changes in Fund Balance - General Funds
For the Year Ended December 31, 2014**

	General	Historical Society	Totals
REVENUES:			
Taxes	\$ 1,425,076	\$ -	\$ 1,425,076
Licenses and Permits	6,391	-	6,391
State Sources	93,159	-	93,159
Administrative Services	377,827	-	377,827
Charges for Services	179,639	-	179,639
Interest	5,782	252	6,034
Fines and Forfeitures	3,613	-	3,613
Other Revenue	97,036	2,923	99,959
TOTAL REVENUES	2,188,523	3,175	2,191,698
EXPENDITURES:			
Legislative	936	-	936
General Government	627,471	-	627,471
Public Safety	782,408	-	782,408
Public Works	317,634	-	317,634
Community Development	30,176	-	30,176
Recreation and Culture	293,435	23,199	316,634
Debt Service	101,560	-	101,560
Other Expenditures	35,488	-	35,488
TOTAL EXPENDITURES	2,189,108	23,199	2,212,307
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	(585)	(20,024)	(20,609)
OTHER FINANCING SOURCES (USES):			
Operating Transfers In	243,000	33,000	276,000
Operating Transfers Out	(95,131)	-	(95,131)
EXCESS (DEFICIENCY) OF REVENUES AND OTHER FINANCING SOURCES OVER EXPENDITURES AND OTHER FINANCING USES	147,284	12,976	160,260
FUND BALANCES, JANUARY 1	2,103,277	83,836	2,187,113
Prior Period Adjustment	(128,156)	-	(128,156)
FUND BALANCES, DECEMBER 31	\$ 2,122,405	\$ 96,812	\$ 2,219,217

Combining Statement of Net Position

Fiduciary Funds

December 31, 2014

	West Traverse Township Water	Tax Collection	Total Agency Funds
ASSETS:			
Cash and Equivalents - Unrestricted	\$ -	\$ 836,244	\$ 836,244
Accounts Receivable	6,234	-	6,234
Due from Others	116	-	116
Taxes Receivable	-	1,794,876	1,794,876
TOTAL ASSETS	\$ 6,350	\$ 2,631,120	2,637,470
LIABILITIES:			
Accounts Payable	\$ 5,092	\$ -	\$ 5,092
Due to County	-	134,705	134,705
Due to School	-	1,186,002	1,186,002
Due to State	-	60,067	60,067
Due to ISD	-	499,665	499,665
Due to College	-	445,072	445,072
Due to Cemetery	-	10,687	10,687
Due to Ambulance & EMS	-	44,910	44,910
Due to Others	1,258	250,012	251,270
TOTAL LIABILITIES	\$ 6,350	\$ 2,631,120	\$ 2,637,470

Report on Compliance



ANDERSON, TACKMAN & COMPANY, PLC
CERTIFIED PUBLIC ACCOUNTANTS

KINROSS OFFICE

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**MEMBER AICPA
DIVISION FOR CPA FIRMS**

MEMBER MACPA

**OFFICES IN
MICHIGAN & WISCONSIN**

**INDEPENDENT AUDITOR'S 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**

Members of the City Council
City of Harbor Springs, Michigan

We have audited, in accordance with the 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 Harbor Springs, Michigan as of and for the year ended December 31, 2014, and the related notes to the financial statements, which collectively comprise the City of Harbor Springs, Michigan's basic financial statements and have issued our report thereon dated June 12, 2015.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City of Harbor Springs, Michigan's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City of Harbor Springs, Michigan's internal control. Accordingly, we do not express an opinion on the effectiveness of the City of Harbor Springs, Michigan'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 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. 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.

Members of the City Council
City of Harbor Springs, Michigan

Compliance and Other Matters

As part of obtaining reasonable assurance about whether City of Harbor Springs, Michigan'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*.

Purpose of this Report

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



Anderson, Tackman & Company, PLC
Certified Public Accountants
Kincheloe, Michigan

June 12, 2015



ANDERSON, TACKMAN & COMPANY, PLC
CERTIFIED PUBLIC ACCOUNTANTS

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MEMBER MACPA

**OFFICES IN
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COMMUNICATION WITH THOSE CHARGED WITH GOVERNANCE

Members of the City Council
City of Harbor Springs, Michigan

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 Harbor Springs, Michigan for the year ended December 31, 2014, and have issued our report thereon dated June 12, 2015. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. Professional standards also require that we communicate to you the following information related to our audit.

Our Responsibility under U.S. Generally Accepted Auditing Standards and *Government Auditing Standards*

As stated in our engagement letter dated May 26, 2015, our responsibility, as described by professional standards, is to express opinions about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities.

As part of our audit, we considered the internal control of the City of Harbor Springs, Michigan. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we will also perform tests of the City of Harbor Springs, Michigan's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our tests was not to provide an opinion on compliance with such provisions.

Generally accepted accounting principles provide for certain required supplementary information (RSI) to supplement the basic financial statements. Our responsibility with respect to the management's discussion and analysis and budgetary comparison schedules, which supplement(s) the basic financial statements, is to apply certain limited procedures in accordance with generally accepted auditing standards. However, the RSI will not be audited and, because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance, we will not express an opinion or provide any assurance on the RSI.

We have been engaged to report on combining fund financial statements, which accompany the financial statements but are not RSI. Our responsibility for this other information, as described by professional standards, is to evaluate the presentation of the other information in relation to the financial statements as a whole and to report on whether the other information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you in our letter about planning matters dated May 26, 2015.

Significant Audit Findings

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 of Harbor Springs, Michigan are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies were not changed during the year. We noted no transactions entered into by the governmental unit during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

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 affecting the financial statements were:

- Management's estimate of the depreciation expense is based on estimated lives. We evaluated the key factors and assumptions used to develop the estimate to determine that it is reasonable in relation to the financial statements taken as a whole.
- Management's estimate of the vested employee benefits is based on current hourly rates and policies regarding payment of sick and vacation banks.
- Management's estimate of the allowance for uncollectible accounts receivable is based on past experience and future expectations for collection of various account balances and has been determined to be zero.
- Management's estimate of the Annual Required Contribution for OPEB Obligations and pension benefits were based on various assumptions regarding life expectancies, inflation, premium increases, and investment rates.

The financial statement disclosures are neutral, consistent and clear.

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 clearly trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to the financial statements taken as a whole.

Disagreement with Management

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's 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 June 12, 2015.

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 governmental unit'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 as to determine 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 retention as the governmental unit's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Comments and Recommendations

Depreciation (Prior Year)

We noted a few errors calculating depreciation essentially manually. Again, these errors were insignificant. We support your decision to begin using an asset software module. We encourage you to implement this as soon as possible.

Status: Uncorrected.

Employee Files (Prior Year)

It was noted during our testing of controls over payroll that on multiple occasions employee files had incomplete or missing statutorily required forms. We recommend that all required paper work be completed at the beginning of employment.

Status: Corrected.

Credit Card (Prior Year)

It was noted during our testing over credit card disbursements, that on two occasions credit card purchases did not have receipts supporting purchases on credit card statement as the credit card policy requires. We recommend that all purchases incurred with credit cards be supported by receipts as the policy requires.

Status: Corrected.

Policies

The City currently does not have policies for ACH/EFT payments, GASB 54 fund balance, conflict of interest, and bid/purchasing. It is recommended that the City adopt a policy regarding these items.

Fraud Policy

With the implementation of Statement of Auditing Standards No. 99, auditors are required to assess policies and procedures regarding fraud risks with a governmental entity. The City does not have a “fraud policy” which would address fraud or suspected fraud and related board actions. We recommend the City adopt a fraud policy in compliance with SAS No. 99.

Obsolete Inventory

The City has accumulated outdated and obsolete inventory, which should be scrapped or sold. Removal of old and unused inventory items reduces handling time and costs and more accurately reports inventory levels.

Cash

During testing, it was noted that there were some long outstanding checks still accounted for in the bank reconciliation. It is recommended that the bank reconciliation be checked for “stale” checks and that they are voided, escheated, or reissued if needed.

Pension Reporting

In June 2012, the Governmental Accounting Standards Board (GASB) approved a pair of related Statements that implement substantial changes to the accounting and financial reporting of pensions by state and local governments and pension plans. Statement No. 67, *Financial Reporting for Pension Plans* and Statement No. 68, *Accounting and Financial Reporting for Pensions*, establishes new accounting and financial reporting requirements. These requirements include a provision for reporting net pension liabilities on the accrual based statement of net position and measuring investments at fair value as well as additional footnote and required supplementary information disclosures.

The Board and Management should review the procedures for implementation of these new standards effective in fiscal 2014 and assess the impact on the local unit of government’s financial reporting.

Uniform Administrative Requirements

During December 2013, the Office of Management and Budget released its final version of the “*Uniform Administrative Requirements, Cost Principles and Audit Requirements for Federal Awards*.” The guidance is applicable to federal grants and cooperative agreements and provides a comprehensive consolidation and revision of OMB Circulars which currently govern Federal and some non-Federal entities. The guidance combines A-110 and A-102 into a single set of administrative rules, combines A-21, A-87 and A-122 into a single set of consolidated cost principles and revises the language of A-133. This publication is designed to provide a single document which will serve as a “one-stop shop” for financial assistance regulatory requirements for all awarding agencies. The new requirements will be effective and applicable for audits of years beginning on or after December 26, 2014.

Revisions Related to Single Audit Requirements

The Office of Management and Budget set forth new consolidated audit standards for entities receiving Federal financial assistance awards and replaces OMB Circular A-133. The changes within the final guidance primarily combine the guidance in OMB A-133 and A-50 on audit follow-up. The guidance reflects a movement to focus these audits and oversight efforts on higher dollar, higher risk awards and focus oversight on improper payments, waste, fraud, and abuse.

Most significantly, the threshold triggering a single audit or program-specific audit requirements is increased to \$750,000 or more in annual Federal awards. These requirements apply equally to recipients and sub-recipients under Federal programs. The final guidelines incorporate an exception to these audit requirements for non-U.S.-based entities expending Federal awards.

Further, the final guidance increases the minimum threshold for reporting questioned costs from \$10,000 to \$25,000 to focus on the audit findings presenting the greatest risk. OMB believes this will eliminate smaller-dollar audit findings, which require utilization of resources for follow-up audits that are unlikely to indicate significant weaknesses in internal controls.

These changes necessitate a careful review and analysis of an organization’s current business practices. Although OMB has raised certain thresholds for audit and materiality, it has also improved mechanisms of oversight related to mandatory disclosures, pre-award review of risks, standards for financial and program management, sub-recipient monitoring, and remedies for noncompliance. The revisions are effective for audits of years beginning on or after December 26, 2014.

Public Act 298 of 2012 “Performance Audit”

Public Act 298 of 2012 allows the Department of Transportation to request the local agency (road commission, county, city or village expending Act 51 monies) to engage an auditor to conduct a “performance audit” of whether it has expended funds in compliance with Act 51 of 1951, as amended (Act 51). A “performance audit” is different in scope than a “financial audit”. A “performance audit” by definition is an independent examination of a program, function, operation or the management systems and procedures of a governmental entity to assess whether the entity is achieving economy, efficiency, and effectiveness in the employment of available resources. All local agencies will be required to have a Performance Audit for periods beginning October 1, 2015. The performance audit under Public Act 298 of 2012 must be performed by an independent certified public accountant that is currently licensed to practice in the State of Michigan or by an employee of the Department of Transportation.

Other Matters

We applied certain limited procedures to the management's discussion and analysis and budgetary comparison schedules, which are required supplementary information (RSI) that supplements the basic financial statements. Our procedures consisted of inquires of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquires, the basic financial statements, and our knowledge we obtained during our audit of the basic financial statements. We did not audit the RSI and do not express an opinion or provide any assurance on the RSI.

We were engaged to report on the combining fund financial statements, which accompany the financial statements but are not RSI. With respect to this other information, we made certain inquires of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the other information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

Conclusion

We would like to express our appreciation, as well as that of our staff, for the excellent cooperation we received while performing the audit. If we can be of assistance in implementing the above recommendations, please contact us.

This report is intended solely for the information and use of the City Council, management, federal awarding agencies, pass-through entities and others within the organization and is not intended to be and should not be used by anyone other than these specified parties.



Anderson, Tackman & Company, PLC
Certified Public Accountants
Kincheloe, Michigan

June 12, 2015