

VILLAGE OF KALKASKA, MICHIGAN

ANNUAL FINANCIAL REPORT

YEAR ENDED FEBRUARY 28, 2014



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INDEPENDENT AUDITOR'S REPORT

Honorable Village President
and Members of the Village Council
Village of Kalkaska
Kalkaska, Michigan

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the Village of Kalkaska, Michigan (the "Village") as of and for the year ended February 28, 2014, and the related notes to the financial statements, which collectively comprise the Village'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, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the Village of Kalkaska, Michigan, as of February 28, 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, the schedules of funding progress and employer contributions for the pension and other postemployment benefits plans, and budgetary comparison information as listed in the table of contents be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Village's basic financial statements. The combining and individual fund financial statements as listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The combining and individual fund financial statements are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing

standards generally accepted in the United States of America. In our opinion, the combining and individual fund financial statements are fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated August 20, 2014, on our consideration of the Village of Kalkaska, 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 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 Village's internal control over financial reporting and compliance.

A handwritten signature in dark ink that reads "Gabridge & Company". The signature is written in a cursive, flowing style.

Gabridge & Company, PLC
Grand Rapids, Michigan
August 20, 2014

Management's Discussion and Analysis

As management of the Village of Kalkaska, Michigan (The "Village" or "government") we offer readers of the Village's financial statements this narrative overview and analysis of the financial activities of the Village for the fiscal year ended February 28, 2014. We encourage readers to consider the information presented here in conjunction with the financial statements.

Financial Highlights

- The assets of the Village exceeded its liabilities at the close of the most recent fiscal year by \$7,775,088 (net position). Of this amount, \$1,171,149 represents unrestricted net position, which may be used to meet the government's ongoing obligations to citizens and creditors.
- At the close of the current fiscal year, the Village's governmental funds reported combined fund balances of \$1,104,936, an increase of \$73,571 in comparison with the prior year. Approximately 24% of this amount (\$283,214) is available for spending at the government's discretion (*unassigned fund balance*).
- At the end of the current fiscal year, unassigned fund balance for the general fund was \$283,214, or approximately 35% of total general fund expenditures and transfers out.

Overview of the Financial Statements

The discussion and analysis provided here is intended to serve as an introduction to the Village's basic financial statements. The Village's basic financial statements consist of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) the notes to financial statements. This report also includes supplementary information intended to furnish additional detail to support the basic financial statements themselves.

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

The *statement of net position* presents financial information on all of the Village's assets and liabilities, with the difference 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 Village is improving or deteriorating.

The *statement of activities* presents information showing how the Village's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported for some items that will only result in cash flows in future fiscal periods (e.g., accrued but unpaid other postemployment benefits and earned but unused vacation leave).

Both of the government-wide financial statements distinguish functions of the Village that are principally supported by taxes and intergovernmental revenues (governmental activities) from other 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 Village include general government, police and fire protection, streets, health and welfare, community and economic development, and recreation and culture. The business-type activities of the Village include water and sewer services.

The government-wide financial statements can be found on pages 15 – 16 of this report.

The government-wide financial statements include not only the Village of Kaskaskia itself (known as the primary government), but also a legally separate Downtown Development Authority for which the Village is financially accountable. Financial information for this component unit is reported separately from the financial information presented for the primary government itself.

The Downtown Development Authority's (component unit) financial statements can be found on pages 59 - 60 of this report.

Fund Financial 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. The Village, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the Village can be divided into two categories: governmental funds and proprietary funds.

Governmental 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 *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year. Such information may be useful in assessing a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*.

The Village maintains five individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the general fund and the major street fund, which are considered to be major funds. Data from the local street fund, drug enforcement fund, and the justice training fund is presented as a separate column as they are considered nonmajor funds.

The Village adopts an annual appropriated budget for the general fund and each special revenue fund. A budgetary comparison schedule for the general fund and each major special revenue fund has been provided to demonstrate compliance with these budgets.

The basic governmental fund financial statements can be found on pages 17 – 20 of this report.

Proprietary Funds. The Village maintains two types of proprietary funds. *Enterprise funds* are used to report the same functions presented as *business-type activities* in the government-wide financial statements. The Village uses enterprises funds to account for its water and sewer operations. *Internal service funds* are an accounting device used to accumulate and allocate costs internally among the Village's various functions.

The Village uses internal service funds to account for motor vehicle and retiree healthcare costs and allocating the cost to the funds that are using the resources. Because these services predominantly benefit governmental rather than business-type functions, they have been included within the governmental activities in the government-wide financial statements.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statements provide separate information for the water and sewer operations, both of which are considered to be major funds of the Village. The internal service fund data is presented in the proprietary fund financial statements.

The basic proprietary fund financial statements can be found on pages 21 – 24 of this report.

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

The notes to the financial statements can be found on pages 26 - 43 of this report.

Other Information. In addition to the basic financial statements and accompanying notes, this report also presents *required supplementary information* concerning the Village's budgetary comparison schedules and the Villages schedules of funding progress and employer contributions for the pension and other postemployment benefits plans.

Required supplementary information can be found on pages 45 - 49 of this report.

This report also presents other supplementary information which includes the nonmajor fund combining and individual statements. The combining statements are presented immediately following the required supplementary information on pensions.

Combining and individual fund statements and schedules can be found on pages 52 - 60 of this report.

Government-wide Overall Financial Analysis

As noted earlier, net position over time, may serve as a useful indicator of a government's financial position. In the case of the Village, assets exceeded liabilities by \$7,775,088, at the close of the most recent fiscal year.

Village of Kalkaska Statement of Net Position as of February 28, 2014 and February 28, 2013

	Governmental Activities		Business-type Activities		Total Primary Government	
	2014	2013	2014	2013	2014	2013
ASSETS						
<i>Current Assets</i>						
Cash & Cash Equivalents	\$ 1,415,033	\$ 1,345,138	\$ 1,474,510	\$ 1,252,622	\$ 2,889,543	\$ 2,597,760
Accounts Receivable	9,191	1,468	139,604	170,634	148,795	172,102
Due from Other Governments	79,470	115,074	-	-	79,470	115,074
Inventories & Land Held for Resale	1,240	1,299	33,349	35,390	34,589	36,689
Prepaid Items	43,439	42,325	8,788	8,487	52,227	50,812
Internal Balances	-	(59,631)	-	59,631	-	-
Total Current Assets	1,548,373	1,445,673	1,656,251	1,526,764	3,204,624	2,972,437
<i>Noncurrent Assets</i>						
Restricted Cash	-	-	854,087	565,850	854,087	565,850
Capital Assets, net	1,578,138	1,570,675	8,299,780	8,544,057	9,877,918	10,114,732
Total Assets	3,126,511	3,016,348	10,810,118	10,636,671	13,936,629	13,653,019
LIABILITIES						
<i>Current Liabilities</i>						
Accounts Payable	89,674	51,829	34,437	18,407	124,111	70,236
Accrued Payroll Liabilities	6,790	16,514	4,623	8,390	11,413	24,904
Accrued Interest Payable	-	-	37,917	39,481	37,917	39,481
Current Portion of Long-term Debt	-	-	179,000	163,650	179,000	163,650
Total Current Liabilities	96,464	68,343	255,977	229,928	352,441	298,271
<i>Noncurrent Liabilities</i>						
Compensated Absences	32,320	35,299	8,176	8,927	40,496	44,226
Long-term Debt, net	-	-	4,818,650	4,997,650	4,818,650	4,997,650
Other Postemployment Benefits Obligation	664,584	649,579	285,370	278,927	949,954	928,506
Total Liabilities	793,368	753,221	5,368,173	5,515,432	6,161,541	6,268,653
NET POSITION						
Net Investment in Capital Assets	1,578,138	1,570,675	3,302,130	3,382,757	4,880,268	4,953,432
Restricted	869,584	802,454	854,087	565,850	1,723,671	1,368,304
Unrestricted	(114,579)	(110,002)	1,285,728	1,172,632	1,171,149	1,062,630
Total Net Position	\$ 2,333,143	\$ 2,263,127	\$ 5,441,945	\$ 5,121,239	\$ 7,775,088	\$ 7,384,366

By far, the largest portion of the Village's net position (\$4,880,268, or 63%) reflects its investment in capital assets (e.g., land, buildings, machinery, equipment, vehicles, and infrastructure), less any related outstanding debt that was used to acquire those assets. The Village uses these capital assets to provide a variety of services to its citizens. Accordingly, these assets are not available for future spending. Although the Village's investment in capital assets is reported net of related debt, it should be noted that the resources used to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

An additional portion of the Village's net position (\$1,723,671, or 22%) represents resources that are subject to external restrictions on how they may be used. The remaining balance of

\$1,171,149 is unrestricted and may be used to meet the government's ongoing obligations to its citizens and creditors.

At the end of the current fiscal year, the Village is able to report positive balances in all reported categories of net position, both for the government as a whole, as well as for its separate governmental and business-type activities. The same situation held true for the prior fiscal year.

Due from other governments decreased from \$115,074 as of February 28, 2013 to \$79,470 as of February 28, 2014. This is a result of the Village collecting \$13,516 of delinquent property taxes in February of 2014 and another \$26,927 of state revenue sharing funds also in February 2014. These payments have historically arrived after year-end and, accordingly, were reflected as due from other governments on prior year financial statements.

Restricted cash increased from \$565,850 as of February 28, 2013 to \$854,087 as of February 28, 2014. This is a result of increasing bond restrictions as set forth in the original bond agreements.

The Village's overall net position increased \$390,722 from the prior fiscal year. The reasons for this overall increase are discussed in the following sections for governmental activities and business-type activities.

Governmental Activities. Governmental activities increased the Village's net position by \$109,277. The total increase was impacted by a one-time \$77,950 land donation in August of 2013 as a result of the Kalkaska IDC dissolving.

Property taxes continued to decline for the Village due to a diminished tax base. Property tax revenues in the governmental activities were \$658,489 for the year ending February 28, 2013 and decreased to \$627,489 for the year ending February 28, 2014. The Village is hopeful that the state-wide trend of stabilizing tax bases will be reflected in the Village's tax base in the upcoming years.

Business-type Activities. Business-type activities increased the Village's net position by \$281,445. The total increase was impacted by a one-time \$110,638 donation in August of 2013 as a result of the Kalkaska IDC dissolving. In addition, the Village Council has taken a pro-active stance to improve the financial position of the water and sewer funds by implementing a multi-year plan of increasing utility rates incrementally so as to minimize the financial impact on its customers.

Village of Kalkaska
Change in Net Position for Fiscal Years Ended February 28, 2014 and February 28, 2013

	Governmental Activities		Business-type Activities		Total Government	
	2014	2013	2014	2013	2014	2013
Revenue						
Program Revenues						
Charges for Services	\$ 105,128	\$ 110,725	\$ 1,372,603	\$ 1,325,814	\$ 1,477,731	\$ 1,436,539
Operating Grants & Contributions	229,433	211,237	110,638	4,938	340,071	216,175
Capital Grants & Contributions	77,950	62,000	-	-	77,950	62,000
Total Program Revenues	412,511	383,962	1,483,241	1,330,752	1,895,752	1,714,714
General Revenues						
Property Taxes	627,489	658,489	-	-	627,489	658,489
Intergovernmental	166,196	155,661	-	-	166,196	155,661
Other Revenue	1,197	22,982	-	23,073	1,197	46,055
Interest Income	558	1,269	4,825	2,333	5,383	3,602
Transfers In (Out)	(39,261)	20,000	39,261	(20,000)	-	-
Total General Revenues & Transfers	756,179	858,401	44,086	5,406	800,265	863,807
Total Revenues	1,168,690	1,242,363	1,527,327	1,336,158	2,696,017	2,578,521
Expenses						
Legislative	27,569	24,378	-	-	27,569	24,378
General Government	138,200	122,290	-	-	138,200	122,290
Public Safety	212,400	204,757	-	-	212,400	204,757
Public Works	357,980	338,575	-	-	357,980	338,575
Community & Economic Development	21,887	-	-	-	21,887	-
Recreation & Culture	10,422	21,668	-	-	10,422	21,668
Other Functions	330,216	272,408	-	-	330,216	272,408
Water & Sewer Operations	-	-	1,206,621	1,100,998	1,206,621	1,100,998
Total Expenses	1,098,674	984,076	1,206,621	1,100,998	2,305,295	2,085,074
Change in Net Position	70,016	258,287	320,706	235,160	390,722	493,447
Net Position at the Beginning of Period	2,263,127	2,004,840	5,121,239	4,886,079	7,384,366	6,890,919
Net Position at the End of Period	\$ 2,333,143	\$ 2,263,127	\$ 5,441,945	\$ 5,121,239	\$ 7,775,088	\$ 7,384,366

Financial Analysis of Governmental Funds

As noted earlier, the Village uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds. The focus of the Village's *governmental funds* is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the Village's financing requirements. In particular, unassigned fund balance may serve as a useful measure of a government's net resources available for discretionary use as they represent the portion of fund balance which has not yet been limited to use for a particular purpose by either an external party, the Village itself, or a group or individual that has been delegated authority to assign resources for use for particular purposes by the Village's Council.

At February 28, 2014, the Village's governmental funds reported combined fund balances of \$1,178,507, an increase of \$73,571 in comparison with the prior year. Approximately 24% of this amount (\$283,214) constitutes *unassigned fund balance*, which is available for spending at the government's discretion. The remainder of the fund balance is either *nonspendable*, *assigned*,

or restricted to indicate that it is 1) not in spendable form (\$25,709 for inventories and prepaid items), or 2) restricted for particular purposes (\$869,584 for major and local streets and public safety programs).

The general fund is the chief operating fund of the Village. At the end of the current fiscal year, unassigned fund balance of the general fund was \$283,214. As a measure of the general fund's liquidity, it may be useful to compare unassigned fund balance to total general fund expenditures and transfers out. Unassigned fund balance represents approximately 35 percent of total general fund expenditures and transfers out.

The fund balance of the Village's general fund increased by \$2,365 during the current fiscal year. The Village Council monitors the expenditures of the general fund closely to ensure that spending does not exceed the Village's available resources.

The major streets fund, a major fund, had a \$40,649 increase in fund balance during the current fiscal year which put the overall fund balance at \$580,876. This increase in fund balance is due to the originally budgeted preventative maintenance expenditures coming in significantly under budget, creating an increase in fund balance whereas the original budget showed a budgeted decrease of \$84,474 in the major streets fund balance for the year.

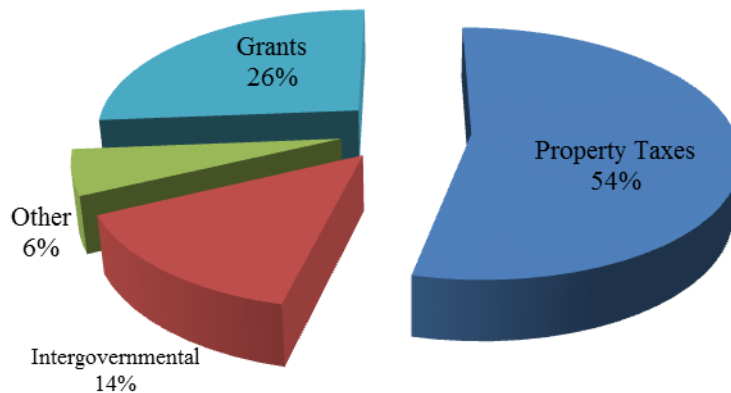
Proprietary Funds. The Village's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail.

Unrestricted net position at the end of the year was \$647,765 for the water fund and \$637,963 for the sewer fund. The increase in net position was \$126,652 for the water fund and \$154,793 for the sewer fund. The change in net position for both funds was consistent with prior years, although the current year increase in net position was aided by a one-time donation of \$110,638 (\$64,042 was allocated to the water fund and \$46,596 was allocated to the sewer fund) as a result of the Kalkaska IDC dissolving and donating its remaining resources.

Governmental Activities

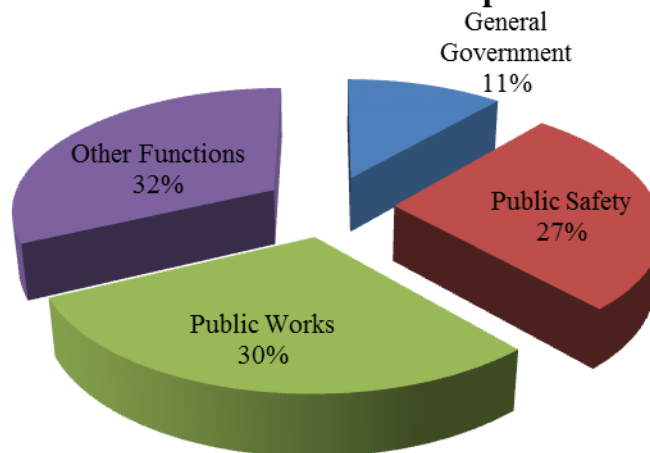
The following chart summarizes the revenue sources for the governmental activities of the Village for the most recent fiscal year end.

Governmental Activities Revenues



The following chart summarizes the expenses for the governmental activities of the Village for the most recent fiscal year end.

Governmental Activities Expenses



General Fund Budgetary Highlights

Original budget compared to final budget. During the year there was a need to adjust expenditures in the final budget to \$928,912 from the originally budgeted expenditures of \$897,012. This is a result of increased estimated expenditures in the police department of approximately \$12,000 and increased estimated expenditures on employee insurance of approximately \$20,000. All other budget amendments during the year were relatively minor.

Final budget compared to actual results. During the current fiscal year the Village had no budget variances between the final amended budget compared to actual results at the functional level.

Capital Assets and Debt Administration

Capital assets. The Village's investment in capital assets for its governmental and business-type activities as of February 28, 2014, amounts to \$9,877,918 (net of accumulated depreciation). This investment in capital assets includes land, buildings, machinery, equipment, vehicles, park facilities, sidewalks, and water and sewer infrastructure. The following summarizes the Village's capital assets:

	Governmental Activities	Business-type Activities	Total Primary Government
Land	\$ 246,371	\$ 87,934	\$ 334,305
Buildings	491,232	14,401	505,633
Land Improvements	385,273	359,594	744,867
Equipment & Vehicles	29,427	49,972	79,399
Water & Sewer System	-	7,787,879	7,787,879
Infrastructure	425,835	-	425,835
Subtotal	<u>\$ 1,578,138</u>	<u>\$ 8,299,780</u>	<u>\$ 9,877,918</u>

More detailed information about the Villages' capital assets can be found in Note 4.

Long-term Debt

As described in Note 6 to the financial statements, the Village had \$4,997,650 in bonds outstanding and settlement payments at the end of the fiscal year. The Village was in process of issuing a new bond as of year end. The Village is well under its legal debt limit as of year-end.

Economic Condition and Outlook

Management estimates that \$800,000 of revenues will be available for appropriation in the general fund in the upcoming year. The Village continues to review all budget line items for opportunities to reduce expenditures when possible. The budget will be monitored during the year to identify any necessary amendments. In 2015, the Village plans again to use current revenues to provide essential services and to maintain the Village's financial reserves at similar levels. Property tax revenues are expected to change minimally reflecting fairly stable property values.

The Village expects to begin a series of sewer improvement project in 2015 at an estimated cost of \$1,675,000 to be financed with Village funds of \$197,000 and a USDA low-interest 40 year loan in the amount of \$1,478,000. The project would replace three sewer pump stations, replace pump station discharge force main, installation of storm sewers and sewer main, extend sewer to donated property, and to perform an infiltration and inflow study.

In March of 2014 the Village was awarded a Downtown Improvement Grant in the amount of \$750,000 to finance its streetscape project. The project is expected to be complete in 2014.

The Village also passed a resolution on May 19, 2014 that discontinued the retirees' health insurance benefits with an effective date of August 19, 2014 in an effort to restore the declining financial position of the governmental activities of the Village into a surplus, rather than its current \$114,579 deficit balance.

All of these upcoming major projects, infrastructure needs, and the current economic conditions, have been included in the upcoming budget for the Village.

Contacting the Village

This financial report is designed to provide a general overview of the Village's finances to its citizens, customers, investors, and creditors and to demonstrate the Village's accountability for the resources it receives. Questions regarding any information provided in this report or requests for additional financial information should be addressed to:

The Village of Kalkaska
212 Water Street
Kalkaska, MI 48851

BASIC FINANCIAL STATEMENTS

**Village of Kalkaska
Statement of Net Position
February 28, 2014**

	Primary Government			
	Governmental Activities	Business-type Activities	Total	Component Units
ASSETS				
Current Assets				
Cash & Cash Equivalents	\$ 1,415,033	\$ 1,474,510	\$ 2,889,543	\$ 997,632
Accounts Receivable	9,191	139,604	148,795	--
Due from Other Governments	79,470	--	79,470	--
Inventories & Land Held for Resale	1,240	33,349	34,589	--
Prepaid Items	43,439	8,788	52,227	55
Total Current Assets	1,548,373	1,656,251	3,204,624	997,687
Noncurrent Assets				
Restricted Cash	--	854,087	854,087	--
Capital Assets not being Depreciated	246,371	87,934	334,305	--
Capital Assets being Depreciated, net	1,331,767	8,211,846	9,543,613	--
Total Assets	3,126,511	10,810,118	13,936,629	997,687
LIABILITIES				
Current Liabilities				
Accounts Payable	89,674	34,437	124,111	11,783
Accrued Payroll Liabilities	6,790	4,623	11,413	--
Accrued Interest Payable	--	37,917	37,917	--
Current Portion of Long-term Debt	--	179,000	179,000	--
Total Current Liabilities	96,464	255,977	352,441	11,783
Noncurrent Liabilities				
Compensated Absences	32,320	8,176	40,496	--
Long-term Debt, net	--	4,818,650	4,818,650	--
Other Postemployment Benefits Obligation	664,584	285,370	949,954	--
Total Liabilities	793,368	5,368,173	6,161,541	11,783
NET POSITION				
Net Investment In Capital Assets	1,578,138	3,302,130	4,880,268	--
Restricted for:				
Major & Local Streets	865,693	--	865,693	--
Public Safety Programs	3,891	--	3,891	--
Debt Service	--	854,087	854,087	--
Unrestricted	(114,579)	1,285,728	1,171,149	985,904
Total Net Position	\$ 2,333,143	\$ 5,441,945	\$ 7,775,088	\$ 985,904

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

**Village of Kalkaska
Statement of Activities
For the Year Ended February 28, 2014**

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue			Component Units
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Government			
					Governmental Activities	Business-type Activities	Total	
Primary Government								
Governmental Activities:								
Legislative	\$ 27,569	\$ --	\$ --	\$ --	\$ (27,569)	\$ --	\$ (27,569)	\$ --
General Government	138,200	100,988	12,500	77,950	53,238	--	53,238	--
Public Safety	212,400	4,140	500	--	(207,760)	--	(207,760)	--
Public Works	357,980	--	216,433	--	(141,547)	--	(141,547)	--
Recreation & Culture	10,422	--	--	--	(10,422)	--	(10,422)	--
Community & Economic Development	21,887	--	--	--	(21,887)	--	(21,887)	--
Other	330,216	--	--	--	(330,216)	--	(330,216)	--
<i>Total Governmental Activities</i>	<u>1,098,674</u>	<u>105,128</u>	<u>229,433</u>	<u>77,950</u>	<u>(686,163)</u>	<u>--</u>	<u>(686,163)</u>	<u>--</u>
Business-type Activities:								
Water	401,724	463,098	64,042	--	--	125,416	125,416	--
Sewer	804,897	909,505	46,596	--	--	151,204	151,204	--
<i>Total Business-type Activities</i>	<u>1,206,621</u>	<u>1,372,603</u>	<u>110,638</u>	<u>--</u>	<u>--</u>	<u>276,620</u>	<u>276,620</u>	<u>--</u>
<i>Total Primary Government</i>	<u>\$ 2,305,295</u>	<u>\$ 1,477,731</u>	<u>\$ 340,071</u>	<u>\$ 77,950</u>	<u>\$ (686,163)</u>	<u>\$ 276,620</u>	<u>\$ (409,543)</u>	<u>--</u>
Component Units								
DDA	\$ 206,866	\$ --	\$ --	\$ --	--	--	--	(206,866)
<i>Total Component Units</i>	<u>\$ 206,866</u>	<u>\$ --</u>	<u>\$ --</u>	<u>\$ --</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>(206,866)</u>
General Purpose Revenues and Transfers:								
Revenues								
					627,489	--	627,489	136,609
					166,196	--	166,196	--
					1,197	--	1,197	2,402
					558	4,825	5,383	2,194
Transfers								
					--	--	--	--
<i>Total General Revenues and Transfers</i>					<u>795,440</u>	<u>4,825</u>	<u>800,265</u>	<u>141,205</u>
<i>Change in Net Position</i>					<u>109,277</u>	<u>281,445</u>	<u>390,722</u>	<u>(65,661)</u>
<i>Net Position at Beginning of Period</i>					<u>2,223,866</u>	<u>5,160,500</u>	<u>7,384,366</u>	<u>1,051,565</u>
<i>Net Position at End of Period</i>					<u>\$ 2,333,143</u>	<u>\$ 5,441,945</u>	<u>\$ 7,775,088</u>	<u>\$ 985,904</u>

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

**Village of Kalkaska
Balance Sheet
Governmental Funds
February 28, 2014**

		<u>Special Revenue</u>		
	<u>General</u>	<u>Major Streets</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
ASSETS				
Cash & Cash Equivalents	\$ 298,268	\$ 548,914	\$ 285,207	\$ 1,132,389
Accounts Receivable	9,191	--	--	9,191
Due from Other Governments	23,536	41,122	14,812	79,470
Inventories	--	422	818	1,240
Prepaid Items	22,633	918	918	24,469
Total Assets	\$ 353,628	\$ 591,376	\$ 301,755	\$ 1,246,759
LIABILITIES				
Accounts Payable	\$ 42,918	\$ 9,687	\$ 9,263	\$ 61,868
Accrued Payroll Liabilities	4,863	813	708	6,384
Total Liabilities	47,781	10,500	9,971	68,252
FUND BALANCE				
Nonspendable	22,633	1,340	1,736	25,709
Restricted	--	579,536	290,048	869,584
Unassigned	283,214	--	--	283,214
Total Fund Balance	305,847	580,876	291,784	1,178,507
Total Liabilities and Fund Balance	\$ 353,628	\$ 591,376	\$ 301,755	\$ 1,246,759

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

Village of Kalkaska
Reconciliation of Governmental Funds Balance Sheet to the Statement of Net Position
February 28, 2014

Total Fund Balance - Governmental Funds	\$ 1,178,507
Net position of internal service funds that are treated as proprietary in the fund level statements are treated as governmental in the entity-wide statements	297,927
Capital assets used in governmental activities are not financial resources, and therefore are not reported in the fund statements.	1,552,835
Certain liabilities, such as compensated absences and other postemployment benefit obligations, are not due and payable in the current period, and therefore are not reported in the funds.	(696,126)
Total Net Position - Governmental Funds	\$ <u>2,333,143</u>

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

Village of Kalkaska
Statement of Revenues, Expenditures, and Changes in Fund Balance
Governmental Funds
For the Year Ended February 28, 2014

		<u>Special Revenue</u>		
	<u>General</u>	<u>Major Streets</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Revenues				
Property Taxes	\$ 532,946	\$ 21,009	\$ 73,534	\$ 627,489
Licenses & Permits	1,785	--	--	1,785
Intergovernmental	178,696	161,741	55,192	395,629
Charges for Services	17,729	--	--	17,729
Fines & Forfeitures	2,912	--	--	2,912
Rentals	69,353	--	--	69,353
Other Revenue	602	118	--	720
Interest Income	142	132	82	356
Total Revenues	<u>804,165</u>	<u>183,000</u>	<u>128,808</u>	<u>1,115,973</u>
Expenditures				
Legislative	27,569	--	--	27,569
General Government	127,086	--	--	127,086
Public Safety	211,705	--	250	211,955
Public Works	68,668	142,351	98,001	309,020
Recreation & Culture	9,674	--	--	9,674
Community & Economic Development	21,887	--	--	21,887
Other	315,211	--	--	315,211
Total Expenditures	<u>781,800</u>	<u>142,351</u>	<u>98,251</u>	<u>1,022,402</u>
Excess of Revenues Over (Under) Expenditures	<u>22,365</u>	<u>40,649</u>	<u>30,557</u>	<u>93,571</u>
Other Financing Sources (Uses)				
Transfers In	--	--	--	--
Transfers Out	(20,000)	--	--	(20,000)
Net Other Financing Sources (Uses)	<u>(20,000)</u>	<u>--</u>	<u>--</u>	<u>(20,000)</u>
Net Change in Fund Balance	2,365	40,649	30,557	73,571
Fund Balance at Beginning of Period	<u>303,482</u>	<u>540,227</u>	<u>261,227</u>	<u>1,104,936</u>
Fund Balance at End of Period	<u>\$ 305,847</u>	<u>\$ 580,876</u>	<u>\$ 291,784</u>	<u>\$ 1,178,507</u>

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

Village of Kalkaska
Reconciliation of Governmental Funds Statement of Revenues, Expenditures, and
Changes in Fund Balance with Statement of Activities
For the Year Ended February 28, 2014

Total Net Change in Fund Balances - Governmental Funds	\$ 73,571
Changes in net position of internal service funds that are treated as enterprise fund changes in net position in the fund level statements are treated as governmental fund changes in net position in the entity-wide statements	34,028
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount that donated capital assets (land) of \$77,950 exceeds depreciation expense of \$64,176 during the current year.	13,774
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 governmental funds. This represents the current year change in the accrual of compensated absences and the current year change in the net other postemployment benefits liability.	(12,096)
Changes in Net Position - Governmental Funds	\$ <u>109,277</u>

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

**Village of Kalkaska
Statement of Net Position
Proprietary Funds
February 28, 2014**

	Business-type Activities - Enterprise Funds			Governmental Activities Internal Service Funds
	Water	Sewer	Total Enterprise Funds	
ASSETS				
<i>Current Assets</i>				
Cash & Cash Equivalents	\$ 799,101	\$ 675,409	\$ 1,474,510	\$ 282,644
Accounts Receivable	39,833	99,771	139,604	--
Inventories & Land Held for Resale	8,620	24,729	33,349	--
Prepaid Items	4,967	3,821	8,788	18,970
Total Current Assets	852,521	803,730	1,656,251	301,614
<i>Noncurrent Assets</i>				
Restricted Cash	--	854,087	854,087	--
Capital Assets not being Depreciated	--	87,934	87,934	--
Capital Assets being Depreciated, net	2,543,245	5,668,601	8,211,846	25,303
Total Assets	3,395,766	7,414,352	10,810,118	326,917
LIABILITIES				
<i>Current Liabilities</i>				
Accounts Payable	14,143	20,294	34,437	27,806
Accrued Payroll Liabilities	1,842	2,781	4,623	406
Accrued Interest Payable	792	37,125	37,917	--
Current Portion of Long-term Debt	54,900	124,100	179,000	--
Total Current Liabilities	71,677	184,300	255,977	28,212
<i>Noncurrent Liabilities</i>				
Compensated Absences	2,539	5,637	8,176	778
Long-term Debt, net	28,600	4,790,050	4,818,650	--
Other Postemployment Benefits Obligation	185,440	99,930	285,370	--
Total Liabilities	288,256	5,079,917	5,368,173	28,990
NET POSITION				
Net Investment In Capital Assets	2,459,745	842,385	3,302,130	25,303
<i>Restricted for:</i>				
Debt Service	--	854,087	854,087	--
<i>Unrestricted</i>	647,765	637,963	1,285,728	272,624
Total Net Position	\$ 3,107,510	\$ 2,334,435	\$ 5,441,945	\$ 297,927

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

Village of Kalkaska
Statement of Revenues, Expenses, and Changes in Net Position
Proprietary Funds
For the Year Ended February 28, 2014

	Business-type Activities - Enterprise Funds			Governmental Activities Internal Service Funds
	Water	Sewer	Total Enterprise Funds	
Operating Revenues				
Charges for Services	\$ 454,435	\$ 909,505	\$ 1,363,940	\$ 274,850
Other Revenue	8,663	--	8,663	477
Total Operating Revenues	463,098	909,505	1,372,603	275,327
Operating Expenses				
Personnel Services	168,394	226,407	394,801	193,900
Contractual Services	48,258	71,047	119,305	4,198
Supplies	11,801	3,307	15,108	22,552
Materials	15,239	4,813	20,052	--
Utilities & Maintenance	42,706	66,816	109,522	--
Repair & Maintenance	1,700	20,125	21,825	25,418
Equipment Rental	5,672	864	6,536	--
Depreciation	100,851	182,885	283,736	15,433
Total Operating Expenses	394,621	576,264	970,885	261,501
Operating Income (Loss)	68,477	333,241	401,718	13,826
Non-Operating Revenues (Expenses)				
Interest Income	1,236	3,589	4,825	202
Donations	64,042	46,596	110,638	--
Interest Expense	(7,103)	(228,633)	(235,736)	--
Net Non-Operating Revenues (Expenses)	58,175	(178,448)	(120,273)	202
Income Before Contributions and Transfers	126,652	154,793	281,445	14,028
Transfers In	--	--	--	20,000
Transfers Out	--	--	--	--
Change In Net Position	126,652	154,793	281,445	34,028
<i>Net Position at Beginning of Period</i>	<i>2,980,858</i>	<i>2,179,642</i>	<i>5,160,500</i>	<i>263,899</i>
Net Position at End of Period	\$ 3,107,510	\$ 2,334,435	\$ 5,441,945	\$ 297,927

The Notes to the Financial Statements are an integral part of these Financial Statements

Village of Kalkaska
Statement of Cash Flows
Proprietary Funds
For the Year Ended February 28, 2014

	<u>Business-type Activities - Enterprise Funds</u>			Governmental Activities
	<u>Water</u>	<u>Sewer</u>	<u>Total Enterprise Funds</u>	<u>Internal Service Fund</u>
Cash Flows from Operating Activities				
Cash Received from Charges for Service	\$ 472,183	\$ 931,450	\$ 1,403,633	\$ -
Cash Received from Interfund Services Provided	-	-	-	275,345
Cash Payments to Employees for Services and Fringe Benefits	(166,137)	(226,739)	(392,876)	(194,443)
Cash Payments to Suppliers for Good and Services	(112,859)	(161,719)	(274,578)	(32,999)
Total Cash Flows from Operating Activities	<u>193,187</u>	<u>542,992</u>	<u>736,179</u>	<u>47,903</u>
Cash Flows from Non-capital Financing Activities				
Donations Available for Operating Purposes	64,042	46,596	110,638	-
Operating Transfers In (Out)	-	-	-	20,000
Total Cash Flows from Non-capital Financing Activities	<u>64,042</u>	<u>46,596</u>	<u>110,638</u>	<u>20,000</u>
Cash Flows from Capital and Related Financing Activities				
Purchases of Capital Assets	-	(39,459)	(39,459)	(9,122)
Principal Payments on Bonds	(50,800)	(112,850)	(163,650)	-
Interest Payments on Bonds	(7,562)	(229,738)	(237,300)	-
Total Cash Flows from Capital and Related Financing Activities	<u>(58,362)</u>	<u>(382,047)</u>	<u>(440,409)</u>	<u>(9,122)</u>
Cash Flows from Investing Activities				
Collection of Interfund Balances	-	98,892	98,892	16,643
Interest Income	1,236	3,589	4,825	202
Total Cash Flows from Investing Activities	<u>1,236</u>	<u>102,481</u>	<u>103,717</u>	<u>16,845</u>
Net Increase (Decrease) in Cash and Cash Equivalents	200,103	310,022	510,125	75,626
Cash and Cash Equivalents - Beginning of Year	<u>598,998</u>	<u>1,219,474</u>	<u>1,818,472</u>	<u>207,018</u>
Cash and Cash Equivalents - End of Year	<u>\$ 799,101</u>	<u>\$ 1,529,496</u>	<u>\$ 2,328,597</u>	<u>\$ 282,644</u>

The Notes to the Financial Statements are an integral part of these Financial Statements

Village of Kalkaska
Statement of Cash Flows
Proprietary Funds
For the Year Ended February 28, 2014

	<u>Business-type Activities - Enterprise Funds</u>			Governmental Activities
	<u>Water</u>	<u>Sewer</u>	<u>Total Enterprise Funds</u>	<u>Internal Service Fund</u>
Statement of Net Position Classification of Cash and Cash Equivalents				
Cash & Cash Equivalents	\$ 799,101	\$ 675,409	\$ 1,474,510	\$ 282,644
Restricted Cash	-	854,087	854,087	-
Cash & Cash Equivalents	<u>\$ 799,101</u>	<u>\$ 1,529,496</u>	<u>\$ 2,328,597</u>	<u>\$ 282,644</u>
 Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities				
Operating Income	\$ 68,477	\$ 333,241	\$ 401,718	\$ 13,826
Adjustments to Reconcile Operating Income to Net Cash				
Provided (Used) by Operating Activities				
Depreciation Expense	100,851	182,885	283,736	15,433
Changes in Assets & Liabilities				
Accounts Receivable	9,085	21,945	31,030	18
Prepaid Items	202	(503)	(301)	(2,484)
Inventory	1,988	53	2,041	-
Accounts Payable	10,327	5,703	16,030	21,653
Accrued Payroll Liabilities	2,257	(332)	1,925	(543)
Net Cash Provided by Operating Activities	<u>\$ 193,187</u>	<u>\$ 542,992</u>	<u>\$ 736,179</u>	<u>\$ 47,903</u>

The Notes to the Financial Statements are an integral part of these Financial Statements

NOTES TO THE FINANCIAL STATEMENTS

Village of Kalkaska

Notes to the Financial Statements

Note 1 – Summary of Significant Accounting Policies

The Village of Kalkaska (the “Village” or “government”) is a municipal corporation governed by an elected Council (7 members) and provides services to its more than 2,000 residents in many areas including law enforcement, street development and maintenance, parks, and sewer and water services. The accounting policies of the Village conform to generally accepted accounting principles, as applicable to governments. The following is a summary of the more significant policies.

Reporting Entity

As required by generally accepted accounting principles, these financial statements present the Village and its component unit, an entity for which the Village is considered to be financially accountable. The discretely presented component unit, on the other hand, is reported in a separate column in the government-wide financial statements to emphasize they are legally separate from the Village.

Discretely Presented Component Unit

Downtown Development Authority

The members of the governing board of the Downtown Development Authority are appointed by the Village Council. The budgets and expenditures of the Downtown Development Authority must be approved by the Village Council. The Village also has the ability to significantly influence operations of the Downtown Development Authority. Complete financial statements for the component unit are not separately prepared.

Brownfield Redevelopment Authority

The members of the governing board of the Brownfield Redevelopment Authority are appointed by the Village Council. The budgets and expenditures of the Brownfield Redevelopment Authority must be approved by the Village Council. The Village also has the ability to significantly influence operations of the Brownfield Redevelopment Authority. Complete financial statements for the component unit are not separately prepared.

Government-wide and Fund Financial Statements

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

Village of Kalkaska

Notes to the Financial Statements

separately from the legally separate component unit for which the primary government is financially accountable.

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

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

Measurement Focus, Basis of Accounting and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund and fiduciary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. After March 1st of the subsequent year, the delinquent real property taxes are paid to the Village by the County, which is responsible for collecting any outstanding real property taxes as of that date. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Village considers revenues to be available if they are collected within 60 days of the end of the current fiscal period or within one year for expenditure driven grants. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service and accrued employee benefit expenditures are recorded only when payment is due.

Property taxes, intergovernmental revenue, charges for services and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. All other revenue items are considered to be measurable and available only when cash is received by the Village.

Village of Kalkaska

Notes to the Financial Statements

The Village of Kalkaska reports the following major governmental funds:

The ***general fund*** is the Village's primary operating fund. It accounts for all financial resources of the general government, except those accounted for and reported in another fund.

The ***major streets fund*** accounts for the revenue received from the State of Michigan under Act 51 which is specifically earmarked for construction and maintenance of roads designated as major streets in Village.

The Village of Kalkaska reports the following major proprietary funds:

The ***water fund*** accounts for the cost of providing water services to Village residents. Revenues are primarily from charges to customers for water usage. These revenues are used to pay operating costs and principal and interest on revenue bonds and general obligation bonds which were used to finance improvements to the system.

The ***sewer fund*** accounts for the cost of collecting and treating wastewater. Revenues are primarily from service charges to customers. These revenues are also used to pay principal and interest on revenue bonds and general obligation bonds which were used to finance improvements to the system.

Additionally, the government reports the following fund types:

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

Internal Service Funds account for the financing of goods or services provided by the Village to other departments or funds on a cost reimbursement basis.

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

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

Village of Kalkaska

Notes to the Financial Statements

Assets, Liabilities, and Equity

Cash and Cash Equivalents

The Village's cash and cash equivalents include amounts in demand deposit accounts, certificates of deposit and short-term investments with original maturities of three months or less from the date of acquisition. Certificates of deposit are carried at cost plus accrued interest, since the original maturity dates are less than one year.

Restricted Assets

Assets which are restricted for specified uses by bond debt requirements are classified as restricted assets. Liabilities payable for such restricted assets are separately classified.

Receivables

All receivables are reported at their gross value and, where appropriate, are reduced by the estimated portion that is expected to be uncollectible. No amounts outstanding at February 28, 2014 were identified by as being uncollectible.

Inventories, Land Held for Resale, and Prepaids

Inventories consist of meters and parts for the water and sewer enterprise funds and are valued at cost on the first-in/first-out (FIFO) method. Inventories are recorded as expenditures when consumed rather than when purchased.

Land held for resale consists of parcels in the Kalkaska Industrial Park, purchased through a promissory note with the Kalkaska County Industrial Development Corporation.

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

Capital Assets

Capital assets, which include property, plant, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items), are reported in the governmental and business-type activities columns in the government-wide financial statements. Capital assets are defined by the government as assets with n initials, individual cost of more than \$5,000 and an estimated useful life in excess of one year. Such assets are valued at cost where historical records are available and at an estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

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

Village of Kalkaska

Notes to the Financial Statements

improvement are capitalized and depreciated over the remaining useful lives of the related capital assets, as applicable.

No interest expense has been incurred or capitalized on capital assets reported in proprietary funds.

Depreciation on capital, assets (including infrastructure) of the primary government is computed using the straight-line method over the following estimated useful lives:

Description	Life
Buildings	30 - 50 Years
Equipment & Vehicles	5 - 30 Years
Land Improvements	30 Years
Water & Sewer System	10 - 50 Years
Infrastructure	20 - 50 Years

The Village reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset exceeds its fair value. If it is determined that an impairment loss has occurred, the asset is written down to its net realizable value and a current charge to income is recognized.

Compensated Absences

Under terms of Village policies, eligible employees are granted vacation, sick, and compensatory time in varying amounts based on length of service. Sick and vacation pay is accrued when incurred in the government-wide and proprietary fund financial statements. A liability for these amounts is reported in governmental funds only if they have maturity, for example, as a result of employee resignations and retirements.

Long-term Obligations

In the government-wide financial statements and proprietary fund types in the fund financial statements, the long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type statement of net position. For new bond issuances of governmental funds after the implementation of GASB Statement No. 34 and all proprietary fund bond premiums and discounts are deferred and amortized over the life of the bonds using the straight-line method which approximates the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are recognized as an expense in the period that the bond was issued.

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

Village of Kalkaska

Notes to the Financial Statements

issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Net Position Flow Assumption

Sometimes the government will fund outlays for a particular purpose from both restricted (e.g., restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted – net position and unrestricted – net position in the government-wide and proprietary fund financial statements, a flow assumption must be made about the order in which the resources are considered to be applied.

It is the government's policy to consider restricted – net position to have been depleted before unrestricted – net position is applied.

Fund Balance Flow Assumptions

Sometimes the government will fund outlays for a particular purpose from both restricted and unrestricted resources (the total of committed, assigned, and unassigned fund balance). In order to calculate the amounts to report as restricted, committed, assigned, and unassigned fund balance in the governmental fund financial statements a flow assumption must be made about the order in which the resources are considered to be applied. It is the government's policy to consider restricted fund balance to have been depleted before using any of the components of unrestricted fund balance. Further, when the components of unrestricted fund balance can be used for the same purpose, committed fund balance is depleted first, followed by assigned fund balance. Unassigned fund balance is applied last.

Fund Balance Policies

Fund balance of governmental funds is reported in various categories based on the nature of any limitations requiring the use of resources for specific purposes. Governmental funds report nonspendable fund balance for amounts that cannot be spent because they are either (a) not in spendable form or (b) legally or contractually required to be maintained intact. Restricted fund balance is reported when externally imposed constraints are placed on the use of resources by grantors, contributors, or laws or regulations of other governments. The government itself can establish limitations on the use of resources through either a commitment (committed fund balance) or an assignment (assigned fund balance).

The committed fund balance classification includes amounts that can be used only for the specific purposes determined by a formal action of the government's highest level of decision-making authority. The Village Council is the highest level of decision-making authority for the government that can, by adoption of a resolution prior to the end of the fiscal year, commit fund balance. Once adopted, the limitation imposed by the resolution remains in place until a similar action is taken (the adoption of another resolution) to remove or revise the limitation.

Village of Kalkaska

Notes to the Financial Statements

Amounts in the assigned fund balance classification are intended to be used by the government for specific purposes but do not meet the criteria to be classified as committed. The Village Council has authorized the Village Manager, or the Village Manager's designee, to assign fund balance. The Village Council may also assign fund balance as it does when appropriating fund balance to cover a gap between estimated revenue and appropriations in the subsequent year's appropriated budget. Unlike commitments, assignments generally only exist temporarily. In other words, an additional action does not normally have to be taken for the removal of an assignment. Conversely, as discussed above, an additional action is essential to either remove or revise a commitment.

Unassigned fund balance is the residual classification for the Village's general fund and includes all spendable amounts not contained in the other classifications and is therefore available to be spent as determined by the Village Council.

Property Tax Revenue Recognition

The Village property tax is levied each July 1 on the taxable valuation of property located in the Village as of the preceding December 31, the lien date. Collections are made July 1 through September 14. Taxable values are established annually by the County and are equalized by the State at an estimated 50% of current market value.

Interfund Transactions

During the course of normal operations, the Village has numerous transactions between funds, including expenditures and transfers of resources to provide services, construct assets, and service debt. The accompanying financial statements generally reflect such transactions as transfers. Operating subsidies are also recorded as transfers. The amounts recorded as subsidies or advances are determined by the Village.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

Budgetary and Budgetary Accounting

Budgets presented in the financial statements were prepared on the same basis as the accounting basis used to reflect actual results. The general fund and special revenue funds are subject to legal budgetary accounting controls and all are budgeted annually.

Village of Kalkaska

Notes to the Financial Statements

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

1. The Village Manager submits to the Village Council a proposed operating budget for the fiscal year commencing the following March 1.
2. A public hearing is conducted to obtain taxpayer comments.
3. Prior to the first day of the following fiscal year, the budget is legally enacted through passage of a resolution.
4. The legal level of budgetary control is at the activity level.
5. The Village Manager is authorized to transfer budget amounts between line items within the department. Supplemental appropriations that amend total expenditures for any department require Village Council resolution.
6. Budget appropriations lapse at year-end.
7. Adoption and amendments of all budgets used by the Village are governed by Public Act 621, which was followed for the year ended February 28, 2014. Expenditures may not exceed appropriations.

Note 2 – Excess of Expenditures over Budget

P.A. 621 of 1978, as amended, provides that a local unit shall not incur expenditures in excess of the amount budgeted. Budgetary control is exercised at the activity level in the general fund and the function level in other funds.

During the year ended February 28, 2014, the Village had no expenditures in budgetary funds which were in excess of the amounts budgeted.

Note 3 – Cash and Investments

The captions on the government-wide and fund statements relating to cash and investments are as follows:

	Governmental Activities	Business-type Activities	Primary Government	Component Unit
Statement of Net Position				
Cash & Cash Equivalents	\$ 1,415,033	\$ 1,474,510	\$ 2,889,543	\$ 997,632
Restricted Cash	-	854,087	854,087	-
Total Cash & Cash Equivalents	\$ 1,415,033	\$ 2,328,597	\$ 3,743,630	\$ 997,632

Village of Kalkaska

Notes to the Financial Statements

These deposits are held in three (3) financial institutions located in Michigan in varying amounts. State policy limits the Treasurer's investing options as described in detail below. All accounts are in the name of the Village and a specific fund or common account. Deposits and investments are recorded in Village records at fair value. Interest is recorded when earned.

Deposits & Investments	
Checking & Savings Accounts	\$ 4,078,222
Certificates of Deposit	662,625
Cash on hand	415
Total Cash & Cash Equivalents	<u>\$ 4,741,262</u>

Custodial Credit Risk - Deposits. Custodial credit risk is the risk that, in the event of a bank failure, the Village's deposits might not be returned. State law does not require, and the Village does not have, a policy for deposit custodial credit risk. As of year-end, \$3,954,806 of the Villages bank balance of \$4,740,732 was exposed to custodial credit risk because it was uninsured and uncollateralized. Due to the dollar amounts of cash deposits and the limits of FDIC insurance, the Village believes it is impractical to insure all bank deposits. As a result, the Village evaluates each financial institution with which it deposits Village funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

Statutory Authority

State statutes authorize the Village to invest in:

- a. Bonds, securities, other obligations and repurchase agreements of the United States of America, or an agency or instrumentality of the United States of America.
- b. Certificates of deposit, savings accounts, deposit accounts or depository receipts of a qualified financial institution.
- c. Commercial paper rated at the time of purchase within the two highest classifications established by not less than two standard rating services and that matures not more than 270 days after the date of purchase.
- d. Bankers' acceptances of United States banks.
- e. Obligations of the State of Michigan and its political subdivisions that, at the time of purchase are rated as investment grade by at least one standard rating service.

Village of Kalkaska

Notes to the Financial Statements

- f. Mutual funds registered under the Investment Company Act of 1940 with the authority to purchase only investment vehicles that are legal for direct investment by a public corporation.
- g. External investment pools as authorized by Public Act 20 as amended through December 31, 1997.

Note 4 - Capital Assets

Capital asset activities for governmental activities for the year ended February 28, 2014 are as follows:

Governmental Activities	<u>Beginning of Year</u>	<u>Additions</u>	<u>Disposals</u>	<u>End of Year</u>
Capital Assets not being Depreciated				
Land	\$ 168,421	\$ 77,950	\$ -	\$ 246,371
Capital Assets being Depreciated				
Buildings	674,099	-	-	674,099
Land Improvements	991,358	-	-	991,358
Equipment & Vehicles	869,906	9,122	-	879,028
Infrastructure	552,389	-	-	552,389
Total Capital Assets being Depreciated	3,087,752	9,122	-	3,096,874
Less Accumulated Depreciation				
Buildings	169,211	13,656	-	182,867
Land Improvements	573,040	33,045	-	606,085
Equipment & Vehicles	830,503	19,098	-	849,601
Infrastructure	112,744	13,810	-	126,554
Total Accumulated Depreciation	1,685,498	79,609	-	1,765,107
Net Capital Assets being Depreciated	1,402,254	(70,487)	-	1,331,767
Net Capital Assets, Governmental	\$ 1,570,675	\$ 7,463	\$ -	\$ 1,578,138

Village of Kalkaska

Notes to the Financial Statements

Capital asset activities for business-type activities for the year ended February 28, 2014 are as follows:

Business-type Activities	Beginning of Year	Additions	Disposals	End of Year
Capital Assets not being Depreciated				
Land	\$ 87,934	\$ -	\$ -	\$ 87,934
Capital Assets being Depreciated				
Buildings	38,943	-	-	38,943
Land Improvements	539,391	-	-	539,391
Equipment & Vehicles	187,773	39,459	-	227,232
Water & Sewer System	12,444,783	-	-	12,444,783
Total Capital Assets being Depreciated	13,210,890	39,459	-	13,250,349
Less Accumulated Depreciation				
Buildings	23,677	865	-	24,542
Land Improvements	161,817	17,980	-	179,797
Equipment & Vehicles	167,997	9,263	-	177,260
Water & Sewer System	4,401,276	255,628	-	4,656,904
Total Accumulated Depreciation	4,754,767	283,736	-	5,038,503
Net Capital Assets being Depreciated	8,456,123	(244,277)	-	8,211,846
Net Capital Assets, Governmental	\$ 8,544,057	\$ (244,277)	\$ -	\$ 8,299,780

Depreciation expense was charged to governmental functions of the Village as follows:

Governmental Activities	
General Government	\$ 14,023
Public Safety	445
Public Works	48,960
Recreation & Culture	748
Depreciation Charged to the Internal Service Fund	15,433
Total Governmental Activities	\$ 79,609
Business-type Activities	
Water Fund	\$ 100,851
Sewer Fund	182,885
Total Business-type Activities	\$ 283,736

Village of Kalkaska

Notes to the Financial Statements

Note 5 – Interfund Transactions

For the year ending February 28, 2014, there was interfund transfer of \$20,000 from the general fund to the motor pool fund. This transfer was used to allocate unrestricted revenues of the general fund to finance various programs accounted for in other funds in accordance with budgetary authorizations.

There were no interfund balances as of February 28, 2014.

Note 6 – Long-Term Debt

Long-term debt activity for the year ended February 28, 2014 is as follows:

	Beginning of Year	Additions	Reductions	End of Year	Due Within One Year
Governmental Activities:					
Compensated Absences	\$ 35,299	\$ -	\$ 2,979	\$ 32,320	\$ 32,320
OPEB Obligation	649,579	15,005	-	664,584	-
Total Governmental Activities	684,878	15,005	2,979	696,904	32,320
Business-type Activities:					
1996 Water Supply and Disposal System Revenue Bonds, payable in semi-annual installments of \$50,000 - \$65,000 plus interest at 5.35 - 7.20%, through January 2016.	180,000	-	55,000	125,000	60,000
1996 Water and Sewage Disposal System Revenue Bonds, payable in semi-annual installments of \$65,000 - \$75,000 plus interest at 5.0%, through February 2015.	145,000	-	70,000	75,000	75,000
2002 Sewage System Bonds, payable in semi- annual installments of \$30,000 - \$145,000, plus interest at 4.5%, through January 1, 2042.	4,839,000	-	40,000	4,799,000	44,000
Unamortized Bond Discount	(2,700)		(1,350)	(1,350)	(1,350)
OPEB Obligation	278,927	6,443	-	285,370	-
Compensated Absences	8,927	-	751	8,176	8,176
Total Business-type Activities	5,449,154	6,443	164,401	5,291,196	185,826
Total Primary Government Long-term Debt	\$ 6,134,032	\$ 21,448	\$ 167,380	\$ 5,988,100	\$ 218,146

Village of Kalkaska

Notes to the Financial Statements

The annual requirements, excluding accrued employee benefits and unamortized discounts, to maturity on the total long-term debt obligations outstanding at February 28, 2014 are as follows:

Year Ending February 28,	Business-type Activities		
	Principal	Interest	Total
2015	\$ 179,000	\$ 227,506	\$ 406,506
2016	160,000	218,100	378,100
2017	120,000	209,926	329,926
2018	125,000	204,526	329,526
2019	130,000	198,900	328,900
2020-2024	725,000	902,252	1,627,252
2025-2029	850,000	727,878	1,577,878
2030-2034	975,000	525,378	1,500,378
2035-2039	1,070,000	296,326	1,366,326
2040-2042	665,000	60,526	725,526
Totals:	\$ 4,999,000	\$ 3,571,318	\$ 8,570,318

The compensated absence and OPEB obligation attributable to the governmental activities will generally be liquidated by the general fund, major streets fund, or local streets fund.

Note 7 – Risk Management

The Village is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees (workers' compensation); and natural disasters. During the year ended February 28, 2014, the Village carried commercial insurance to cover all risks of loss. The Village has had no settled claims resulting from these risks that exceeded their commercial coverage in any of the past three fiscal years. There was no significant change in coverage during the year.

Note 8 – Defined Benefit Pension Plan

Municipal Employees Retirement System of Michigan

Plan Description. The Village participates in the Municipal Employees Retirement System of Michigan (MERS), an agent multiple-employer defined benefit pension plan providing retirement, death and disability benefits covering full-time Village employees. The System is administered by the MERS retirement board. The MERS Retirement Board establishes and amends the benefit provisions of the participants in MERS. A publicly available financial report that includes financial statements and required supplementary information for MERS may be obtained by writing to the Municipal Employees Retirement System of Michigan, 447 North Canal Road, Lansing, Michigan 48917 or by calling (800) 767-6377.

Village of Kalkaska

Notes to the Financial Statements

Funding Policy. The Village is required to contribute at an actuarially determined rate; the current rate varies by employment group from 19.95% to 37.87% percent of annual covered payroll. Participating employees are required to contribute at a rate of zero percent for all employment groups. The contribution requirements of the Village are established and may be amended by the MERS Retirement Board. The contribution requirements of plan members are established and may be amended by the Village depending on the MERS contribution program adoption by the Village.

Plan Contributions. For the year ended February 28, 2014, the Village's annual pension cost for MERS of \$156,192 was equal to the Village's required and actual contributions. The required contribution was determined as part of the December 31, 2011 actuarial valuation using the entry age actuarial cost method. The actuarial assumptions included: (a) a rate of return on the investment of present and future assets of 8.0%; (b) projected salary increases of 4.5% per year compounded annually, attributable to inflation; and (c) additional projected salary increases of 0.0% to 13% per year, depending on age, attributable to seniority/merit. The actuarial value of MERS assets was determined on the basis of a valuation method that assumes the fund earns the expected rate of return, and includes an adjustment of 20% of the difference between assumed earnings and market value (5 year seniority) to reflect fair value. The Village's unfunded actuarial accrued liability is being amortized as a level percentage of projected payrolls on an open basis.

The remaining amortization period at December 31, 2012, the date of the latest actuarial valuation, was 26 years.

Three-year Trend Information			
Fiscal Year Ended	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
2012	\$ 110,093	100%	\$ -
2013	\$ 146,199	100%	\$ -
2014	\$ 156,192	100%	\$ -

Funded Status and Funding Progress. As of December 31, 2012, the most recent actuarial valuation date, the Plan was 61 percent funded. The actuarial accrued liability for benefits was \$4,731,154, and the actuarial value of assets was \$2,872,233, resulting in an unfunded actuarial accrued liability (UAAL) of \$1,858,921. The covered payroll (annual payroll of active employees covered by the Plan) was \$362,832, and the ratio of the UAAL to the covered payroll was 519 percent.

The schedule of funding progress, presented as RSI 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 liability for benefits.

Village of Kalkaska

Notes to the Financial Statements

Note 9 - Other Postemployment Benefits

Plan Description. The Village of Kalkaska administers a single-employer defined benefit healthcare plan (the “Plan”). In addition to the retirement benefits described in Note 8, the Plan provides health insurance benefits to certain retirees and their beneficiaries, which are advance-funded on a discretionary basis. In accordance with Village policy, certain individuals and their beneficiaries receive medical, dental, prescription, and eyeglass coverage for varying periods of timing, depending on bargaining unit and years of service. As of February 29, 2012, the date of the last plan valuation, the Plan covered 14 members (6 active plan members and 8 retirees receiving benefits).

Funding policy. The contribution requirements of Plan members and the Village are established and may be amended by the Council. The required contribution is based on projected pay-as-you-go financing requirements, with an additional amount to prefund benefits as determined annually by the Village Council. For the year ended February 28, 2014, the Village contributed \$178,561 to the Plan. In accordance with Village policy, retirees were not required to make any contributions to the Plan.

Annual OPEB Cost and Net OPEB Obligation. The Village’s annual other postemployment benefit (OPEB) cost (expense) is calculated based on the *annual required contribution of the employer (ARC)*. The Village has elected to calculate the ARC and related information using the alternative measurement method permitted by GASB Statement No. 45 for employers in plans with fewer than one hundred total plan members. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. The following table shows the components of the Village’s annual OPEB cost for the year, the amount actually contributed to the Plan, and changes in the Village’s net OPEB obligation:

Annual Required Contribution	\$ 217,299
Interest on Net OPEB Obligation	11,607
Adjustment to Annual Required Contribution	<u>(28,897)</u>
Annual OPEB Cost (Expense)	200,009
Less: Contributions Made	<u>(178,561)</u>
<i>Increase in OPEB Obligation</i>	21,448
<i>Net OPEB Obligation - Beginning of Year</i>	<u>928,506</u>
<i>Net OPEB Obligation - End of Year</i>	<u>\$ 949,954</u>

Village of Kalkaska

Notes to the Financial Statements

The Village's annual OPEB cost, the percentage of annual OPEB cost contributed to the Plan, and the net OPEB obligation for fiscal year 2014 and the previous years were as follows:

	<u>2/29/2012</u>	<u>2/28/2013</u>	<u>2/28/2014</u>
Annual OPEB Cost (Expense)	\$ 224,799	\$ 182,798	\$ 200,009
Percentage of OPEB Cost Contributed	32%	137%	89%
Net OPEB Obligation	\$ 995,960	\$ 928,506	\$ 949,954

Funded Status and Funding Progress. As of February 29, 2012, the most recent actuarial valuation date, the actuarial accrued liability for benefits was \$5,630,933, all of which was unfunded. The covered payroll (annual payroll of the active employees covered by the Plan) was \$208,428 and the ratio of the UAAL to the covered payroll was 2,702 percent.

The projection of future benefit payments for an ongoing plan involves 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 calculations.

Methods and Assumptions. Projections of benefits for financial reporting purposes are based on the substantive plan (the Plan as understood by the employer and 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 members to that point. The 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.

The following simplifying assumptions were made:

Retirement age for active employees - Based on the historical average retirement age for the covered group, active plan members were assumed to retire at age 55.

Marital status - Marital status of members at the calculation date was assumed to continue throughout retirement.

Mortality - Life expectancies were based on mortality tables from the National Center for Health Statistics. The 2006 United States Life Tables for Males and for Females were used.

Village of Kalkaska

Notes to the Financial Statements

Turnover - Non-group-specific age-based turnover data from GASB Statement 45 were used as the basis for assigning active members a probability of remaining employed until the assumed retirement age and for developing an expected future working lifetime assumption for purposes of allocating to periods the present value of total benefits to be paid.

Healthcare cost trend rate - The expected rate of increase in healthcare insurance premiums was based on projections by the Village's management. A rate of 5 percent to 8 percent was used.

Health insurance premiums - 2012 health insurance premiums for retirees were used as the basis for calculation of the present value of total benefits to be paid.

Inflation rate - The expected long-term inflation assumption of 3.3 percent was based on projected changes in the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) in *The 2006 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds* for an intermediate growth scenario.

Payroll growth rate - The expected long-term payroll growth rate was assumed to equal the rate of inflation.

Based on the historical and expected returns of the Village's short-term investment portfolio, a discount rate of 1.25 percent was used. In addition, a simplified version of the entry age actuarial cost method was used. The unfunded actuarial accrued liability is being amortized as a level percentage of projected payrolls on an open basis. The remaining amortization period at February 28, 2014, was 30 years.

Note 10 – Fund Balances – Governmental Funds

The Village reports fund balance in governmental funds based on the provisions of GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*. GASB 54 establishes fund balance classifications that comprise a hierarchy based primarily on the extent to which a government is bound to observe constraints imposed upon the use of the resources reported in governmental funds.

Village of Kalkaska

Notes to the Financial Statements

Detailed information on fund balances of governmental funds is as follows:

	<u>General Fund</u>	<u>Major Streets</u>	<u>Nonmajor Funds</u>	<u>Total</u>
Nonspendable:				
Inventories	\$ -	\$ 422	\$ 818	\$ 1,240
Prepaid Items	22,633	918	918	24,469
Total Nonspendable	<u>22,633</u>	<u>1,340</u>	<u>1,736</u>	<u>25,709</u>
Restricted for:				
Major & Local Streets	-	579,536	286,157	865,693
Public Safety Programs	-	-	3,891	3,891
Total Restricted	<u>-</u>	<u>579,536</u>	<u>290,048</u>	<u>869,584</u>
Unassigned	<u>1,002,732</u>	<u>-</u>	<u>-</u>	<u>1,002,732</u>
Total Fund Balances - Governmental Funds	<u>\$ 1,025,365</u>	<u>\$ 580,876</u>	<u>\$ 291,784</u>	<u>\$ 1,898,025</u>

Note 11 – Subsequent Events

The Village expects to begin a series of sewer improvement project in 2015 at an estimated cost of \$1,675,000 to be financed with Village funds of \$197,000 and a USDA low-interest 40 year loan in the amount of \$1,478,000. The project includes the replacement of three sewer pump stations, replacement of pump station discharge force main, installation of storm sewers and sewer main, an extension of sewer lines to donated property, and an infiltration and inflow study.

In March of 2014 the Village was awarded a Downtown Improvement Grant in the amount of \$750,000 to finance its streetscape project. The project is expected to be complete in 2014.

The Village passed a resolution on May 19, 2014 that discontinued the retirees' health insurance benefits with an effective date of August 19, 2014 in an effort to restore the declining financial position of the governmental activities of the Village into a surplus, rather than its current \$114,579 deficit balance.

Management is not aware of any other subsequent events that would have a significant impact on the financial condition of the Village as of August 20, 2014.

REQUIRED SUPPLEMENTARY INFORMATION

Village of Kalkaska
Required Supplementary Information
MERS Agent Multiple-Employer Defined Benefit Pension Plan
Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	(Overfunded) Unfunded AAL (UAAL) (b-a)	Funded Ratio Total	Covered Payroll (c)	UAL as a Percentage of Covered Payroll ((b-a)/c)
12/31/2010	\$ 2,868,125	\$ 4,418,476	\$ 1,550,351	65%	\$ 335,147	463%
12/31/2011	2,889,526	4,674,434	1,784,908	62%	343,912	519%
12/31/2012	2,872,233	4,731,154	1,858,921	61%	362,832	512%

Schedule of Employer Contributions

Fiscal Year Ending	Annual Pension Cost	Percentage of APC Contributed
2012	\$ 110,093	100%
2013	146,199	100%
2014	156,192	100%

Village of Kalkaska
Required Supplementary Information
Other Postemployment Benefits Plan
Schedule of Funding Progress

* Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	(Overfunded) Unfunded AAL (UAAL) (b-a)	Funded Ratio Total	Covered Payroll (c)	UAL as a Percentage of Covered Payroll ((b-a)/c)
2/28/2009	\$ -	\$ 6,356,264	\$ 6,356,264	0%	\$ 476,986	1333%
2/28/2012	-	5,630,933	5,630,933	0%	208,428	2702%

Schedule of Employer Contributions

Fiscal Year Ending	Annual Pension Cost	Percentage of APC Contributed
2/28/2012	\$ 224,799	32%
2/28/2013	199,245	126%
2/28/2014	200,009	89%

* A plan of this size is not required to be valued each year. Additional years of data will be included in future years as revised valuations are necessary.

Village of Kalkaska
Statement of Revenues, Expenditures, and Changes in Fund Balance-Budget and Actual
General Fund
For the Year Ended February 28, 2014

	Budgeted Amounts		Actual	Variance
	Original	Final		Favorable (Unfavorable) Final to Actual
Revenues				
Property Taxes	\$ 533,306	\$ 533,306	\$ 532,946	\$ (360)
Licenses & Permits	2,000	2,000	1,785	(215)
Intergovernmental	156,540	156,540	178,696	22,156
Charges for Services	13,400	13,400	17,729	4,329
Fines & Forfeitures	7,000	7,000	2,912	(4,088)
Interest	1,000	1,000	142	(858)
Rentals	59,842	59,842	69,353	9,511
Other Revenue	35,117	32,117	602	(31,515)
Total Revenues	808,205	805,205	804,165	(1,040)
Other Financing Sources				
Total Revenues and Other Financing Sources	808,205	805,205	804,165	(1,040)
Expenditures				
Legislative - Village Council	28,578	28,578	27,569	1,009
General Government				
Manager	36,071	36,071	31,500	4,571
Clerk	13,565	16,265	14,683	1,582
Audit	4,650	4,650	4,641	9
Administrative	42,288	34,288	19,709	14,579
Treasurer	15,380	16,680	12,507	4,173
Municipal Building	46,802	51,802	44,046	7,756
Total General Government	158,756	159,756	127,086	32,670
Public Safety				
Police Department	214,339	226,339	211,575	14,764
Fire Department	200	200	130	70
Total Public Safety	214,539	226,539	211,705	14,834

Village of Kalkaska
Statement of Revenues, Expenditures, and Changes in Fund Balance-Budget and Actual
General Fund - Continued
For the Year Ended February 28, 2014

	Budgeted Amounts			Variance Favorable (Unfavorable) Final to Actual
	Original	Final	Actual	
Expenditures				
Public Works				
Department of Public Works	56,441	62,841	45,822	17,019
Airport	23,937	33,437	22,311	11,126
Parking Lots	12,786	12,786	535	12,251
Total Public Works	93,164	109,064	68,668	40,396
Community & Economic Development				
Planning Commission	15,199	10,199	7,232	2,967
Economic Development	15,000	15,000	14,655	345
Total Community & Economic Development	30,199	25,199	21,887	3,312
Recreation & Culture - Parks	19,743	19,743	9,674	10,069
Other Functions				
Property & Liability Insurance	58,241	38,241	20,472	17,769
Employee Insurance	273,792	293,792	286,335	7,457
Employer's Additional MERS	--	8,000	8,404	(404)
Total Other Functions	332,033	340,033	315,211	24,822
Total Expenditures	877,012	908,912	781,800	127,112
Other Financing Uses				
Transfers Out	20,000	20,000	20,000	--
Total Expenditures and Other Financing Uses	897,012	928,912	801,800	127,112
Excess (Deficiency) of Revenues and Other Sources Over Expenditures and Other Uses	(88,807)	(123,707)	2,365	126,072
Net Change in Fund Balance	(88,807)	(123,707)	2,365	126,072
Fund Balance at Beginning of Period	303,482	303,482	303,482	--
Fund Balance at End of Period	\$ 214,675	\$ 179,775	\$ 305,847	\$ 126,072

Village of Kalkaska
Statement of Revenues, Expenditures, and Changes in Fund Balance-Budget and Actual
Major Streets
For the Year Ended February 28, 2014

	Budgeted Amounts		Actual	Variance Favorable (Unfavorable) Final to Actual
	Original	Final		
Revenues				
Property Taxes	\$ 21,113	\$ 21,113	\$ 21,009	\$ (104)
Intergovernmental	130,000	130,000	161,741	31,741
Other Revenue	160,230	230	118	(112)
Interest	200	200	132	(68)
Total Revenues	311,543	151,543	183,000	31,457
Other Financing Sources				
Total Revenues and Other Financing Sources	311,543	151,543	183,000	31,457
Expenditures				
Administrative	14,089	14,089	19,627	(5,538)
Routine Maintenance	32,541	32,541	24,362	8,179
Preventative Maintenance	266,250	66,250	25,236	41,014
Traffic Service	13,482	13,482	2,557	10,925
Winter Maintenance	53,702	61,702	49,410	12,292
Roadside Parks	3,453	3,453	176	3,277
Insurance & Fringe Benefits	12,500	22,000	20,983	1,017
Total Expenditures	396,017	213,517	142,351	71,166
Other Financing Uses				
Total Expenditures and Other Financing Uses	396,017	213,517	142,351	71,166
Excess (Deficiency) of Revenues and Other Sources Over Expenditures and Other Uses	(84,474)	(61,974)	40,649	102,623
Net Change in Fund Balance	(84,474)	(61,974)	40,649	102,623
Fund Balance at Beginning of Period	540,227	540,227	540,227	--
Fund Balance at End of Period	\$ 455,753	\$ 478,253	\$ 580,876	\$ 102,623

COMBINING AND INDIVIDUAL FUND STATEMENTS

NONMAJOR GOVERNMENTAL FUNDS

**Village of Kalkaska
Combining Balance Sheet
Nonmajor Governmental Funds
February 28, 2014**

	Special Revenue			Total Nonmajor Governmental Funds
	Local Streets	Drug Enforcement	Justice Training	
ASSETS				
Cash & Cash Equivalents	\$ 281,316	\$ 892	\$ 2,999	\$ 285,207
Due from Other Governments	14,812	--	--	14,812
Inventories	818	--	--	818
Prepaid Items	918	--	--	918
Total Assets	\$ 297,864	\$ 892	\$ 2,999	\$ 301,755
LIABILITIES				
Accounts Payable	\$ 9,263	\$ --	\$ --	\$ 9,263
Accrued Payroll Liabilities	708	--	--	708
Total Liabilities	9,971	--	--	9,971
FUND BALANCE				
Nonspendable	1,736	--	--	1,736
Restricted	286,157	892	2,999	290,048
Unassigned	--	--	--	--
Total Fund Balance	287,893	892	2,999	291,784
Total Liabilities and Fund Balance	\$ 297,864	\$ 892	\$ 2,999	\$ 301,755

Village of Kalkaska
Combining Statement of Revenues, Expenditures, and Changes in Fund Balance
Nonmajor Governmental Funds
For the Year Ended February 28, 2014

	<u>Special Revenue</u>			Total Nonmajor Governmental Funds
	<u>Local Streets</u>	<u>Drug Enforcement</u>	<u>Justice Training</u>	
Revenues				
Property Taxes	\$ 73,534	\$ --	\$ --	\$ 73,534
Intergovernmental	54,692	--	500	55,192
Interest Income	82	--	--	82
<i>Total Revenues</i>	<u>128,308</u>	<u>--</u>	<u>500</u>	<u>128,808</u>
Expenditures				
Public Safety	--	--	250	250
Public Works	98,001	--	--	98,001
<i>Total Expenditures</i>	<u>98,001</u>	<u>--</u>	<u>250</u>	<u>98,251</u>
<i>Excess of Revenues Over (Under) Expenditures</i>	<u>30,307</u>	<u>--</u>	<u>250</u>	<u>30,557</u>
<i>Net Change in Fund Balance</i>	<u>30,307</u>	<u>--</u>	<u>250</u>	<u>30,557</u>
<i>Fund Balance at Beginning of Period</i>	257,586	892	2,749	261,227
<i>Fund Balance at End of Period</i>	<u>\$ 287,893</u>	<u>\$ 892</u>	<u>\$ 2,999</u>	<u>\$ 291,784</u>

INTERNAL SERVICE FUNDS

Village of Kalkaska
Combining Statement of Net Position
Internal Service Funds
February 28, 2014

	Internal Service		
	Motor Pool	Retiree Healthcare	Total Internal Service Funds
ASSETS			
<i>Current Assets</i>			
Cash & Cash Equivalents	\$ 81,917	\$ 200,727	\$ 282,644
Prepaid Items	5,551	13,419	18,970
<i>Total Current Assets</i>	87,468	214,146	301,614
<i>Noncurrent Assets</i>			
Capital Assets being Depreciated, net	25,303	--	25,303
<i>Total Assets</i>	112,771	214,146	326,917
LIABILITIES			
<i>Current Liabilities</i>			
Accounts Payable	11,387	16,419	27,806
Accrued Payroll Liabilities	406	--	406
<i>Total Current Liabilities</i>	11,793	16,419	28,212
<i>Noncurrent Liabilities</i>			
Compensated Absences	778	--	778
<i>Total Liabilities</i>	12,571	16,419	28,990
NET POSITION			
Net Investment In Capital Assets	25,303	--	25,303
<i>Unrestricted</i>	74,897	197,727	272,624
<i>Total Net Position</i>	\$ 100,200	\$ 197,727	\$ 297,927

Village of Kalkaska
Combining Statement of Revenues, Expenses, and Changes in Net Position
Internal Service Funds
For the Year Ended February 28, 2014

	Internal Service		
	Motor Pool	Retiree Healthcare	Total Internal Service Funds
Operating Revenues			
Charges for Services	\$ 96,289	\$ 178,561	\$ 274,850
Other Revenue	477	--	477
Total Operating Revenues	96,766	178,561	275,327
Operating Expenses			
Personnel Services	37,443	156,457	193,900
Contractual Services	898	3,300	4,198
Supplies	22,552	--	22,552
Repair & Maintenance	25,418	--	25,418
Depreciation	15,433	--	15,433
Total Operating Expenses	101,744	159,757	261,501
Operating Income (Loss)	(4,978)	18,804	13,826
Non-Operating Revenues (Expenses)			
Interest Income	27	175	202
Net Non-Operating Revenues (Expenses)	27	175	202
Transfers	(4,951)	18,979	14,028
Transfers In	20,000	--	20,000
Transfers Out	--	--	--
Change In Net Position	15,049	18,979	34,028
<i>Net Position at Beginning of Period</i>	85,151	178,748	263,899
Net Position at End of Period	\$ 100,200	\$ 197,727	\$ 297,927

Village of Kalkaska
Combining Statement of Cash Flows
Internal Service Funds
For the Year Ended February 28, 2014

	Internal Service		Total
	Motor Pool	Retiree Healthcare	Internal Service Funds
Cash Flows from Operating Activities			
Cash Received from Interfund Services Provided	\$ 96,766	\$ 178,579	\$ 275,345
Cash Payments to Employees for Services and Fringe Benefits	(37,986)	(142,447)	(180,433)
Cash Payments to Suppliers for Good and Services	(43,709)	(3,300)	(47,009)
Total Cash Flows from Operating Activities	15,071	32,832	47,903
Cash Flows from Non-capital Financing Activities			
Operating Transfers In (Out)	20,000	-	20,000
Total Cash Flows from Non-capital Financing Activities	20,000	-	20,000
Cash Flows from Capital and Related Financing Activities			
Purchases of Capital Assets	(9,122)	-	(9,122)
Total Cash Flows from Capital and Related Financing Activities	(9,122)	-	(9,122)
Cash Flows from Investing Activities			
Collection of Interfund Balances	16,643	-	16,643
Interest Income	27	175	202
Total Cash Flows from Investing Activities	16,670	175	16,845
Net Increase (Decrease) in Cash and Cash Equivalents	42,619	33,007	75,626
<i>Cash and Cash Equivalents - Beginning of Year</i>	<i>39,298</i>	<i>167,720</i>	<i>207,018</i>
Cash and Cash Equivalents - End of Year	\$ 81,917	\$ 200,727	\$ 282,644
Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities			
Operating Income	\$ (4,978)	\$ 18,804	\$ 13,826
Adjustments to Reconcile Operating Income to Net Cash			
Provided (Used) by Operating Activities			
Depreciation Expense	15,433	-	15,433
Changes in Assets & Liabilities			
Accounts Receivable	-	18	18
Prepaid Items	(75)	(2,409)	(2,484)
Accounts Payable	5,234	16,419	21,653
Accrued Payroll Liabilities	(543)	-	(543)
Net Cash Provided by Operating Activities	\$ 15,071	\$ 32,832	\$ 47,903

COMPONENT UNIT

Village of Kalkaska
Component Unit - Downtown Development Authority
Statement of Net Position and DDA Fund Balance Sheet
February 28, 2014

	<u>DDA Fund</u>	<u>Adjustments</u>	<u>Statement of Net Position</u>
ASSETS			
<i>Assets</i>			
Cash & Cash Equivalents	\$ 997,632	\$ -	\$ 997,632
Prepaid Items	55	-	55
<i>Total Assets</i>	<u>997,687</u>	<u>-</u>	<u>997,687</u>
LIABILITIES			
<i>Liabilities</i>			
Accounts Payable	11,783	-	11,783
<i>Total Liabilities</i>	<u>11,783</u>	<u>-</u>	<u>11,783</u>
FUND BALANCE			
Unassigned	985,904	(985,904)	-
<i>Total Fund Balance</i>	<u>985,904</u>	<u>(985,904)</u>	<u>-</u>
<i>Total Liabilities & Fund Balance</i>	<u>\$ 997,687</u>		
 NET POSITION			
Unrestricted		<u>\$ 985,904</u>	<u>\$ 985,904</u>

Village of Kalkaska
Component Unit - Downtown Development Authority
Statement of Activities and DDA Fund Revenue,
Expenditures and Changes in Fund Balance
For the Year Ended February 28, 2014

	<u>DDA Fund</u>	<u>Adjustments</u>	<u>Statement of Activities</u>
Expenditures / Expenses			
Community & Economic Development	\$ 206,866	\$ -	\$ 206,866
<i>Total Expenditures / Expenses</i>	<u>206,866.00</u>	<u>-</u>	<u>206,866</u>
General Revenue			
Property Taxes	136,609	-	136,609
Other Income	2,402	-	2,402
Interest Income	2,194	-	2,194
<i>Total General Revenue</i>	<u>141,205</u>	<u>-</u>	<u>141,205</u>
 <i>Net Change in Fund Balance / Net Position</i>	 (65,661)	 -	 (65,661)
Beginning of Year Fund Balance / Net Position	<u>1,051,565</u>		<u>1,051,565</u>
<i>End of Year Fund Balance / Net Position</i>	<u>\$ 985,904</u>		<u>\$ 985,904</u>

August 20, 2014

Honorable Village President
and Members of the Village Council
Village of Kalkaska
Kalkaska, Michigan

We have audited the financial statements of the governmental activities, the business-type activities, the discretely presented component unit each major fund, and the aggregate remaining fund information of the Village of Kalkaska (the "Village") for the year ended February 28, 2014. 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. We have communicated such information in our letter to you dated April 14, 2014. Professional standards also require that we communicate to you the following information related to our audit.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the Village are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the fiscal year 2014. We noted no transactions entered into by the Village 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 estimate(s) affecting the Village's financial statements was:

- Management's estimate of the useful lives of depreciable capital assets is based on the length of time it is believed that those assets will provide some economic benefit in the future.
- Management's estimate of the accrued compensated absences is based on current hourly rates and policies regarding payment of sick and vacation banks.

- The assumptions used in the valuations of the pension and other postemployment benefits plans are based on historical trends and industry standards.

We evaluated the key factors and assumptions used to develop these estimates in determining that they are reasonable in relation to the financial statements as a whole.

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. The following material misstatements detected as a result of audit procedures were corrected by management:

- General fund taxes receivable were increased by \$43,953 to eliminate a credit balance in the taxes receivable account.
- Due to other funds was credited in the general fund by \$79,690 to properly allocate tax revenues to the other funds, including the component unit.
- Interfund advances were credited in the general fund by \$14,178 to reconcile the year-end balances across all funds.
- Due from other funds was debited \$10,346 in the major streets fund to reconcile interfund activity as of year-end.
- Depreciation expense of \$15,433, \$182,885, and \$100,851 was charged to the motor pool fund, sewer fund, and water fund, respectively, to record the current year's share of depreciation expense.
- Capital assets were debited \$9,122 and \$39,459 in the motor pool fund and sewer fund, respectively, to record capital assets that were originally posted to expense accounts.
- Long-term bonds payable were debited \$40,000 in the sewer fund to properly classify a principal payment that was originally posted to interest expense.
- Accounts receivable were credited by \$35,273 and \$17,903 in the sewer and water funds, respectively, to reconcile the accounts receivable aging report to the year-end financial statements.

Disagreements 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 August 20, 2014.

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 Village's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the Village's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Other Matters

We applied certain limited procedures to management's discussion and analysis, the schedules of funding progress and employer contributions for the pension and other postemployment benefit plans, and the budgetary comparison schedules, which are required supplementary information (RSI) that supplements the basic financial statements. Our procedures consisted of inquiries of management regarding 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 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 and individual fund financial statements, which accompany the financial statements but are not RSI. With respect to this supplementary information, we made certain inquiries 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 supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

Restriction on Use

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

Very truly yours,

A handwritten signature in dark ink that reads "Gabridge & Company". The script is cursive and fluid, with the ampersand being particularly stylized.

Gabridge & Company, PLC
Grand Rapids, MI

**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***

Honorable Village President
and Members of the Village Council
Village of Kalkaska
Kalkaska, 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, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the Village of Kalkaska, Michigan (the "Village"), as of and for the year ended February 28, 2014, and the related notes to the financial statements, which collectively comprise the Village's basic financial statements and have issued our report thereon dated August 20, 2014.

Internal Control over Financial Reporting

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

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the

accompanying schedule of findings and responses to be a material weakness (2014-1 and 2014-2).

Compliance and Other Matters

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

The Village's Response to Findings

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

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results 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.



Gabridge & Company, PLC
Grand Rapids, Michigan
August 20, 2014

Village of Kalkaska

Schedule of Findings and Responses

Material Weaknesses

2014-1 – Preparation of Governmental Financial Statements

Criteria:	All Michigan governments are required to prepare financial statements in accordance with generally accepted accounting principles (GAAP). This is a responsibility of the government's management. The preparation of financial statements in accordance with GAAP requires internal controls over both 1) recording, processing and summarizing accounting data (i.e., maintaining internal books and records), and 2) reporting government-wide and fund financial statements, including the related footnotes (i.e., external financial reporting.)
Condition/Finding:	As is the case with many smaller and medium sized entities, the Village has historically relied on its independent external auditors to assist in the preparation of the government-wide financial statements and footnotes as part of its external financial reporting process. Accordingly, the Village's ability to prepare financial statements in accordance with GAAP is based, at least in part, on its reliance on its external auditors, who cannot by definition be considered a part of the Village's internal controls. In addition, we proposed, and management approved, material journal entries to properly record debt service, accounts receivable, interfund balances, and capital asset transactions in the proprietary and governmental funds.
Cause:	This condition was caused by the Village's decision that it is more cost effective to outsource the preparation of its annual financial statements to the auditors than to incur the time and expense of obtaining the necessary training and expertise required for the Village to perform this task internally.
Effect:	As a result of this condition, the Village lacks complete internal controls over the preparation of financial statements in accordance with GAAP, and instead relies, at least in part, on its external auditors for assistance with this task. In addition, the Village's records were initially misstated by an amount material to the financial statements. Finally, management of the Village is not able to review and inquire of the financial condition of the Village on a timely basis.
View of Responsible Officials:	The Village Council has evaluated the cost versus benefit of establishing internal controls over the recording, processing, summarizing accounting data and preparing financial statements, and determined that it is in the best interests of the Village to outsource this task to its external auditors and to carefully review, approve, and accept responsibility for all nonattest work performed by the external auditors.

Village of Kalkaska

Schedule of Findings and Responses

2014-2 – Segregation of Incompatible Duties

Criteria:	Management is responsible for establishing and maintaining internal controls in order to safeguard the assets of the Village. A key element of internal control is the segregation of incompatible duties within the accounting function.
Condition/Finding:	The Village has accounting functions which are performed by the same individual and are not subject to a documented independent review and approval. These areas include payroll, adjusting journal entry, and cash reconciliation transactions.
Cause:	This condition is a result of the limited size of the Village's accounting staff.
Effect:	As a result of this condition, the Village is exposed to an increased risk that misstatements (whether caused by error or fraud) may occur and not be prevented or detected and corrected by management on a timely basis.
Recommendation:	While there are, of course, no easy answers to the challenge of balancing the costs and benefits of internal controls and the segregation of incompatible duties, we would nevertheless encourage management to actively seek ways to further strengthen its internal control structure by requiring as much independent review, reconciliation, and approval of accounting functions by qualified members of management as possible.
View of Responsible Officials:	As a result of limited staffing, we cannot accomplish the desired segregation of duties. Management staff will provide increased oversight and review of operations to help deter inappropriate actions and potential fraud.