

Honorable Mayor and City Council Members  
City of Pequot Lakes  
4638 County Road 11  
Pequot Lakes, MN 56472

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of City of Pequot Lakes (City) for the year ended December 31, 2012, and have issued our report thereon dated April 2, 2013. We have previously communicated to you information about our responsibilities under auditing standards generally accepted in the United States of America and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. Professional standards also require that we communicate to you the following information related to our audit.

### Significant audit findings

#### *Qualitative aspects of accounting practices*

##### Accounting policies

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by City of Pequot Lakes are described in Note 1 to the financial statements.

- *GASBS 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements, supersedes GASBS 20.* GASBS 20 gave governments the choice to elect to follow only GASB's authoritative literature, or to follow FASB and AICPA pronouncements that did not conflict with GASB pronouncements. Upon adoption of GASBS 62, all governmental accounting guidance is codified into the GASB literature.
- *GASBS 63, Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position,* provides guidance on deferred outflows and inflows of resources. It also renames the residual amounts from "net assets" to "net position". These financial statements include the statement of net position, which reports all assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position. Adoption of future GASB standards will include reporting of some items previously reported as assets and liabilities as deferred outflows and inflows of resources.

We noted no transactions entered into by the entity 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

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 financial statements was (were):

Accounting estimates (Continued)

- Management's estimate of the useful lives of depreciable assets is based on guidance issued by the Minnesota Office of the State Auditor and historical practice. We evaluated the key factors and assumptions used to develop the depreciation in determining that it is reasonable in relation to the financial statements taken as a whole.
- Management's estimate of accrued compensated absences is based on earned vacation, sick leave, and comp time. The current portion of the estimate is based on City policy and historical trends.
- Management's estimate of other postemployment benefits payable is based upon an actuarial calculation.

Financial statement disclosures

Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. There were no particularly sensitive financial statement disclosures.

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.

***Uncorrected misstatements***

Professional standards require us to accumulate all misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. Management did not identify and we did not notify them of any uncorrected financial statement misstatements.

Professional standards require us to accumulate all 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.

***Corrected misstatements***

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

- To adjust for receipts of payment on loan receivable.
- To adjust account payable for items not properly accrued.
- To record additional receivable not booked by the client.
- To adjust bond proceeds to account for client netting of issuance costs.

***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 auditors' report. No such disagreements arose during our audit.

***Management representations***

We have requested certain representations from management that are included in the management representation letter dated April 2, 2013.

***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 entity’s financial statements or a determination of the type of auditors’ 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.

***Significant issues discussed with management prior to engagement***

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

***Other audit findings or issues***

The following describes findings or issues arising from the audit that are, in our professional judgment, significant and relevant to your oversight of the financial reporting process:

- Limited Segregation of Duties – The City has limited employees with primary responsibility for all of the accounting and financial duties and receipting of utility billings. As a result, many of those aspects of internal accounting control which rely upon an adequate segregation of duties are, for all practical purposes, not available in this staffing scenario. We recognize that the City’s cost/benefit analysis has concluded the employment of additional persons for the purpose of segregating duties is not practicable from a financial standpoint, but we are required, under our professional responsibilities, to call the situation to your attention. The City should continue to utilize the City Council’s oversight of the budgeting, cash reconciling, and receipts and disbursements process to the maximum extent possible to mitigate the absence of segregation of duties. This condition increases the possibility that errors or irregularities may occur and not be detected on a timely basis
- Material Audit Adjustments – As part of the audit, we proposed audit entries, including cash to accrual basis entries, recording some capital assets, and reclassifying transactions to the proper accounts. The absence of a complete control procedure or process in this area is considered a material weakness because the potential exists that a material misstatement of the financial statements could occur and not be prevented or detected by the City’s internal control process. The design of the internal controls over recording cash to accrual entries and depreciation expense, could affect the organization’s ability to detect or prevent a misappropriation of assets or fraudulent activity.
- Oversight of the Financial Reporting Process – Management is responsible for establishing and maintaining internal controls for the fair presentation of the financial position, results of operations, cash flows, and disclosures in the financial statements, in conformity with U.S. generally accepted accounting principles (GAAP). The City does not have a system of internal controls that would enable management to conclude the financial statements and related disclosures are complete and presented in accordance with GAAP. As such, management requested us to prepare a draft of the financial statements, including the related footnote disclosures. The outsourcing of these services is not unusual in organization of your size and is a result of management’s cost/benefit decision to rely on our accounting expertise rather than incurring this internal resource cost. The design of internal controls over the financial reporting process affects the ability of the organization to report their financial data consistently with the assertions of management in the financial statements.

**Other audit findings or issues (continued)**

We understand this material weakness is already known to management and represents a conscious decision by management and the City Council as a result of cost or other considerations. We acknowledge management is responsible for making decisions concerning costs and the related benefits. We are responsible to communicate significant deficiencies and material weaknesses in accordance with professional standards regardless of management's decisions to ensure that the Board of directors is aware of this situation.

**Other information in documents containing audited financial statements**

With respect to the required supplementary information (RSI) accompanying the financial statements, we made certain inquiries of management about the methods of preparing the RSI, including whether the RSI has been measured and presented in accordance with prescribed guidelines, whether the methods of measurement and preparation have been changed from the prior period and the reasons for any such changes, and whether there were any significant assumptions or interpretations underlying the measurement or presentation of the RSI. We compared the RSI for consistency with management's responses to the foregoing inquiries, the basic financial statements, and other knowledge obtained during the audit of the basic financial statements. Because these limited procedures do not provide sufficient evidence, we did not express an opinion or provide any assurance on the RSI.

With respect to the Combining Balance Sheet – Nonmajor Governmental Funds and Combining Statement of Revenues, Expenditures, and Changes in Fund Balances – Nonmajor Governmental Funds (collectively, the supplementary information) accompanying the financial statements, on which we were engaged to report in relation to the financial statements as a whole, 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 or the reasons for such changes, 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. We have issued our report thereon dated April 2, 2013.

Our auditors' opinion, the audited financial statements, and the notes to financial statements should only be used in their entirety. Inclusion of the audited financial statements in a document you prepare, such as an annual report, should be done only with our prior approval and review of the document.

\* \* \*

The purpose of this communication is solely to provide you with information about findings or issues arising from the audit that are significant and relevant to your responsibility to oversee the financial reporting process and compliance. This communication is an integral part of an audit performed in accordance with *Government Auditing Standards*. This communication is not suitable for any other purpose.

  
CliftonLarsonAllen LLP

Brainerd, Minnesota  
April 2, 2013

**CITY OF PEQUOT LAKES, MINNESOTA**

**FINANCIAL STATEMENTS AND  
SUPPLEMENTARY INFORMATION**

**YEAR ENDED DECEMBER 31, 2012**





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## **INTRODUCTORY SECTION**



**CITY OF PEQUOT LAKES, MINNESOTA  
PRINCIPAL CITY OFFICIALS  
DECEMBER 31, 2012**

Position	Name	Term Expires
<u>Elected Officials</u>		
Mayor	Nancy Adams	December 31, 2012
Council Member	Jerry Akerson	December 31, 2014
Council Member	Scott Pederson	December 31, 2012
Council Member	Tom Ryan	December 31, 2012
Council Member	Dave Sjoblad	December 31, 2014
<u>Appointed</u>		
Clerk/Treasurer	Sandra Peine	
Attorney	Paul Sandelin	
Auditor	CliftonLarsonAllen LLP	

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## **FINANCIAL SECTION**

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## INDEPENDENT AUDITORS' REPORT

Honorable Mayor and  
Members of the City Council  
City of Pequot Lakes  
Pequot Lakes, Minnesota

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Pequot Lakes (City), Minnesota, as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

### ***Management's Responsibility for the Financial Statements***

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

### ***Auditors' 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 auditors' 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.

Honorable Mayor and  
Members of the City Council  
City of Pequot Lakes

***Opinions***

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Pequot Lakes, as of December 31, 2012, 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, budgetary comparison information, and schedules of funding progress on pages 5-16, 54-57, and 59-60, respectively, 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.

*Supplementary Information*

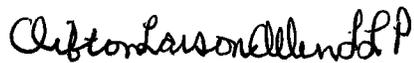
Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Pequot Lakes' basic financial statements. The combining nonmajor fund financial statements are presented for purposes of additional analysis and are not a required part of the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

The combining nonmajor 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 information is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Honorable Mayor and  
Members of the City Council  
City of Pequot Lakes

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated April 2, 2013, on our consideration of the City of Pequot Lakes' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City of Pequot Lakes' internal control over financial reporting and compliance.



**CliftonLarsonAllen LLP**

Brainerd, Minnesota  
April 2, 2013

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## **REQUIRED SUPPLEMENTARY INFORMATION**



**CITY OF PEQUOT LAKES, MINNESOTA  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
YEAR ENDED DECEMBER 31, 2012**

This section of the City of Pequot Lakes' (City) annual financial report presents our discussion and analysis of the City's financial performance during the fiscal year that ended on December 31, 2012. The Management's Discussion and Analysis (MD&A) is an element of Required Supplementary Information specified in the Governmental Accounting Standard Board's (GASB) Statement No. 34 – *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. Certain comparative information between the current year, 2012 and the prior year, 2011 is required to be presented in the MD&A.

### **FINANCIAL HIGHLIGHTS**

Key financial highlights for 2012 include the following:

- ◆ City-wide net position increased 16% over the prior year. The primary reason for the increase is due to additional grant money received.
- ◆ Overall, governmental fund-level revenues totaled \$2,249,916 and were \$103,616 more than expenditures. This excess of revenues over expenditures is due to an increase in tax revenues and gifts and contributions.
- ◆ The General Fund's fund balance decreased \$7,235 (-1%) from the prior year due mainly to an increase in capital outlay expenditures relating to highways and streets.
- ◆ The Fire Department Fund's fund balance decreased \$14,025 (-11%) from the prior year due mainly to the increase in public safety expenditures and debt principal payments.
- ◆ The Water Enterprise Fund net position increased \$13,243 (2%) from the prior year. Depreciation expense in this fund totaled \$63,275. Sewer Enterprise Fund net position increased \$97,299 (8%) from the prior year including the impact of the depreciation expense of \$21,187.

### **OVERVIEW OF THE FINANCIAL STATEMENTS**

The financial section of the annual report consists of four parts – Independent Auditors' Report, required supplementary information which includes the management's discussion and analysis (this section), the basic financial statements, and supplementary information. The basic financial statements include two kinds of statements that present different views of the City:

- ◆ The first two statements are City-wide financial statements which provide both short-term and long-term information about the City's overall financial status.
- ◆ The remaining statements are fund financial statements which focus on individual parts of the City, reporting the City's operations in more detail than the City-wide statements.
  - The governmental funds statements tell how basic services such as general government, public safety, and highways and streets were financed in the short term as well as what remains for future spending.

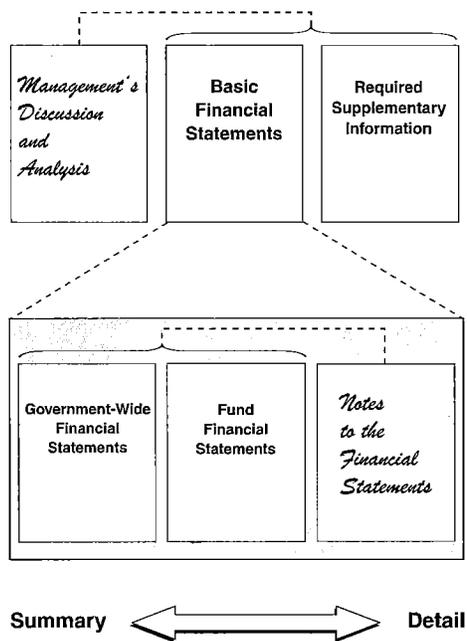
**CITY OF PEQUOT LAKES, MINNESOTA  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
YEAR ENDED DECEMBER 31, 2012**

**OVERVIEW OF THE FINANCIAL STATEMENTS (CONTINUED)**

The financial statements also include notes that explain some of the information in the statements and provide more detailed data.

Figure A-1 shows how the various parts of this annual report are arranged and related to one another.

**Figure A-1  
Annual Report Format**



**CITY OF PEQUOT LAKES, MINNESOTA  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
YEAR ENDED DECEMBER 31, 2012**

**OVERVIEW OF THE FINANCIAL STATEMENTS (CONTINUED)**

Figure A-2 summarizes the major features of the City's financial statements, including the portion of the City's activities they cover and the types of information they contain. The remainder of this overview section of management's discussion and analysis highlights the structure and contents of each of the statements.

**Figure A-2  
Major Features of the City's Financial Statements**

<b>Type of Statements</b>	<b>Government-Wide</b>	<b>Governmental Funds</b>	<b>Proprietary Funds</b>
<b>Scope</b>	Entire City's government (except fiduciary funds).	The activities of the City that are not proprietary or fiduciary.	The activities of the City that operate similar to private businesses: water and sewer.
<b>Required Financial Statements</b>	Statement of net position.	Balance sheet.	Statement of net position.
	Statement of activities.	Statement of revenues, expenditures and changes in fund balance.	Statement of revenues, expenses, and changes in net assets and statement of cash flows.
<b>Accounting Basis and Measurement Focus</b>	Accrual accounting and economic resources focus.	Modified accrual accounting and current financial resources focus.	Accrual accounting and economic resources focus.
<b>Type of Asset/Liability Information</b>	All assets and liabilities, both financial and capital, short-term and long-term.	Only assets expected to be used up and liabilities that come due during the year or soon thereafter, no capital assets included.	All assets and liabilities, both financial and capital, and short-term and long-term.
<b>Type of Inflow/Outflow Information</b>	All revenues and expenses during year, regardless of when cash is received or paid.	Revenues for which cash is received during or soon after the end of the year, expenditures when goods or services have been received and payment is due during the year or soon thereafter.	All revenues and expenses during the year, regardless of when cash is received or paid.

**City-Wide Statements**

The City-wide statements report information about the City as a whole using accounting methods similar to those used by private-sector companies. The statement of net position includes all of the City's assets and liabilities. All of the current year's revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two City-wide statements report the City's net position and how they have changed. Net position – the difference between the City's assets and liabilities – are one way to measure the City's financial health or position.

- ◆ Over time, increases or decreases in the City's net position are an indicator of whether its financial position is improving or deteriorating, respectively.
- ◆ To assess the overall health of the City, you need to consider additional non-financial factors such as changes in the City's property tax base and the condition of City buildings and other facilities.

**CITY OF PEQUOT LAKES, MINNESOTA  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
YEAR ENDED DECEMBER 31, 2012**

**OVERVIEW OF THE FINANCIAL STATEMENTS (CONTINUED)**

**City-Wide Statements (Continued)**

In the City-wide financial statements the City's activities are shown in two categories:

- ◆ Governmental activities – The City's basic services are included here. Property taxes, special assessments and state aids finance most of these activities.
- ◆ Business-type activities – The City's enterprise fund operations are included here. Charges for services finance most of these activities.

**Fund Financial Statements**

The fund financial statements provide more detailed information about the City's funds – focusing on its most significant or "major" funds – not the City as a whole. Funds are accounting devices the City uses to keep track of specific sources of funding and spending on particular programs:

- ◆ Some funds are required by state law and by bond covenants.
- ◆ The City establishes other funds to control and manage money for particular purposes (e.g., repaying its long-term debts) or to show that it is properly using certain revenues (e.g., federal grants).

The City has two kinds of funds:

- ◆ Governmental funds – The City's basic services are included in governmental funds, which generally focus on (1) how cash and other financial assets that can readily be converted to cash flow in and out and (2) the balances left at year-end that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that helps to determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs. Because this information does not encompass the additional long-term focus of the City-wide statements, we provide additional information after the governmental funds statements that explain the relationship (or differences) between them.
- ◆ Proprietary funds – The City reports two proprietary funds. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The City uses enterprise funds to account for its water and sewer utilities. Proprietary fund financial statements provide the same type of information as the government-wide financial statements, only in more detail.

**CITY OF PEQUOT LAKES, MINNESOTA  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
YEAR ENDED DECEMBER 31, 2012**

**FINANCIAL ANALYSIS OF THE CITY AS A WHOLE**

**Net Position**

The City's total net positions were \$10,250,006 on December 31, 2012 (see Table A-1).

**Table A-1  
The City's Net Position**

	Governmental Activities		Business-Type Activities		Total	
	2012	2011	2012	2011	2012	2011
Current and Other Assets	\$ 2,350,472	\$ 2,206,890	\$ 1,432,990	\$ 1,448,637	\$ 3,783,462	\$ 3,655,527
Capital and Noncurrent Assets	6,562,351	5,450,062	2,030,799	2,099,487	8,593,150	7,549,549
<b>Total Assets</b>	<b>8,912,823</b>	<b>7,656,952</b>	<b>3,463,789</b>	<b>3,548,124</b>	<b>12,376,612</b>	<b>11,205,076</b>
Current Liabilities	229,077	198,950	232,203	230,235	461,280	429,185
Long-Term Liabilities	448,152	496,440	1,217,174	1,414,019	1,665,326	1,910,459
<b>Total Liabilities</b>	<b>677,229</b>	<b>695,390</b>	<b>1,449,377</b>	<b>1,644,254</b>	<b>2,126,606</b>	<b>2,339,644</b>
<b>Net Position</b>						
Invested in Capital Assets,						
Net of Related Debt	6,186,400	4,966,411	758,441	671,289	6,944,841	5,637,700
Restricted	161,081	71,481	-	-	161,081	71,481
Unrestricted	1,888,113	1,923,670	1,255,971	1,232,581	3,144,084	3,156,251
<b>Total Net Position</b>	<b>\$ 8,235,594</b>	<b>\$ 6,961,562</b>	<b>\$ 2,014,412</b>	<b>\$ 1,903,870</b>	<b>\$ 10,250,006</b>	<b>\$ 8,865,432</b>

**CITY OF PEQUOT LAKES, MINNESOTA  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
YEAR ENDED DECEMBER 31, 2012**

**FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONTINUED)**

**Changes in Net Position**

The City-wide total revenues were \$3,715,153 the year ended December 31, 2012. Property taxes and intergovernmental revenues accounted for 77% of total revenue for the year (see Table A-2).

Table A-2  
Change in Net Position

	Governmental Activities			Business-Type Activities			Total		
	2012	2011	Total % Change	2012	2011	Total % Change	2012	2011	Total % Change
<b>REVENUES</b>									
<u>Program Revenues</u>									
Charges for Services	\$ 321,193	\$ 314,994	2.0 %	\$ 464,561	\$ 465,464	(0.2)%	\$ 785,754	\$ 780,458	0.7 %
Operating Grants and Contributions	191,662	183,378	4.5	-	-	-	191,662	183,378	4.5
Capital Grants and Contributions	999,069	75,372	1225.5	-	-	-	999,069	75,372	1225.5
<u>General Revenues</u>									
Property Taxes	1,572,603	1,512,450	4.0	-	-	-	1,572,603	1,512,450	4.0
Unrestricted State Aid	96,274	3,367	2759.3	-	-	-	96,274	3,367	2759.3
Investment Earnings	14,348	14,767	(2.8)	10,326	10,323	-	24,674	25,090	(1.7)
Other	40,117	71,771	(44.1)	5,000	3,800	31.6	45,117	75,571	(40.3)
Total Revenues	3,235,266	2,176,099	48.7	479,887	479,587	0.1	3,715,153	2,655,686	39.9
<b>EXPENSES</b>									
General Government	490,853	486,359	0.9	-	-	-	490,853	486,359	0.9
Public Safety	836,207	845,715	(1.1)	-	-	-	836,207	845,715	(1.1)
Highways and Streets	456,633	446,630	2.2	-	-	-	456,633	446,630	2.2
Sanitation	11,797	11,906	(0.9)	-	-	-	11,797	11,906	(0.9)
Water	-	-	-	229,691	233,980	(1.8)	229,691	233,980	(1.8)
Sewer	-	-	-	139,654	117,544	18.8	139,654	117,544	18.8
Culture and Recreation	50,899	53,486	(4.8)	-	-	-	50,899	53,486	(4.8)
Economic Development	96,581	69,347	39.3	-	-	-	96,581	69,347	39.3
Interest	18,264	21,597	(15.4)	-	-	-	18,264	21,597	(15.4)
Total Expenses	1,961,234	1,935,040	1.4	369,345	351,524	5.1	2,330,579	2,286,564	1.9
<b>TRANSFERS IN (OUT)</b>	-	5,191	(100.0)	-	(5,191)	100.0	-	-	-
<b>CHANGE IN NET POSITION</b>	1,274,032	246,250	417.4	110,542	122,872	(10.0)	1,384,574	369,122	275.1
Net Position - Beginning of Year	6,961,562	6,715,312	3.7	1,903,870	1,780,998	6.9	8,865,432	8,496,310	4.3
<b>NET POSITION - END OF YEAR</b>	<u>\$ 8,235,594</u>	<u>\$ 6,961,562</u>		<u>\$ 2,014,412</u>	<u>\$ 1,903,870</u>		<u>\$ 10,250,006</u>	<u>\$ 8,865,432</u>	

Total revenues surpassed expenses, increasing net position \$1,384,574 over last year.

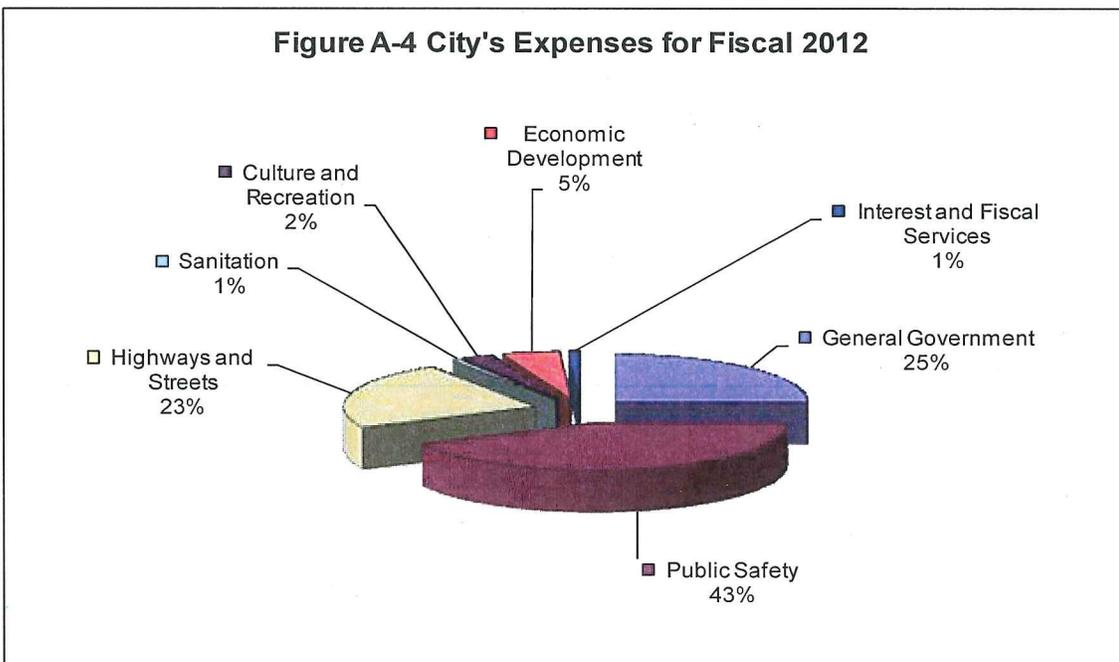
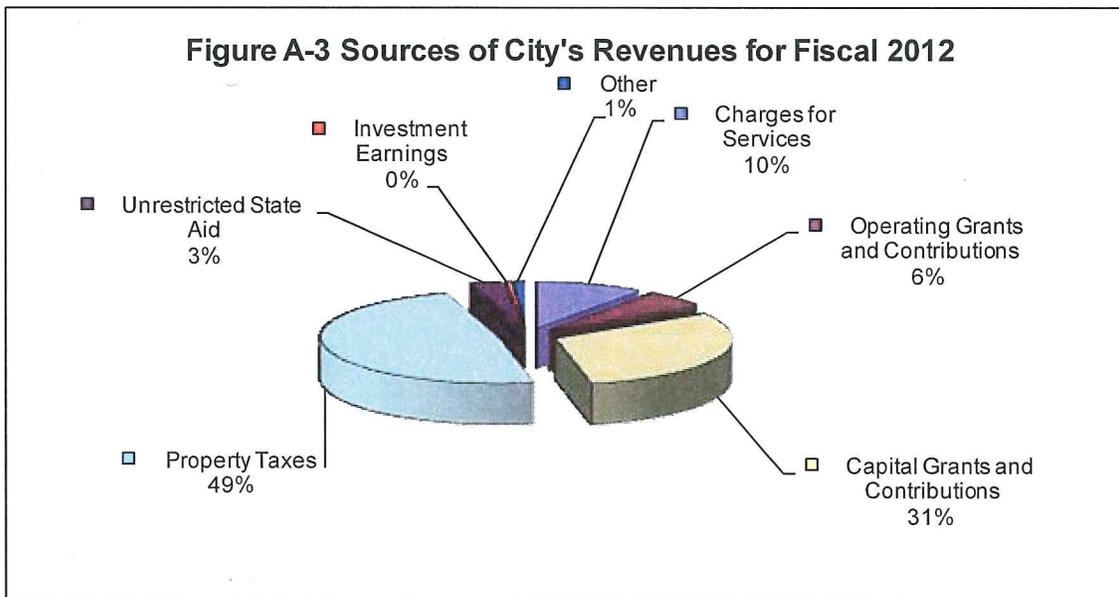
**CITY OF PEQUOT LAKES, MINNESOTA  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
YEAR ENDED DECEMBER 31, 2012**

**FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONTINUED)**

**Changes in Net Position (Continued)**

The City-wide cost of all governmental activities this year was \$1,961,234.

- ◆ Some of the cost was paid by the users of the City's programs \$321,193.
- ◆ The federal and state governments subsidized certain programs with grants and contributions \$1,190,731. Of this amount, \$984,800 was a contribution of land that was received in 2012.
- ◆ The remainder of the City's governmental activities costs of \$444,310, however, were paid for by City taxpayers, the taxpayers of our state, and other miscellaneous revenues.



**CITY OF PEQUOT LAKES, MINNESOTA  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
YEAR ENDED DECEMBER 31, 2012**

**FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONTINUED)**

**Changes in Net Position (Continued)**

**Table A-3  
Total and Net Cost of Services**

	Total Cost of Services		Percentage Change	Net (Revenue) Cost of Providing Services		Percentage Change
	2012	2011		2012	2011	
<b>GOVERNMENTAL ACTIVITIES</b>						
General Government	\$ 490,853	\$ 486,359	0.9 %	\$ 455,117	\$ 445,564	2.1 %
Public Safety	836,207	845,715	(1.1)	440,824	445,164	(1.0)
Highways and Streets	456,633	446,630	2.2	456,589	420,486	8.6
Sanitation	11,797	11,906	(0.9)	(6,661)	(11,543)	42.3
Culture and Recreation	50,899	53,486	(4.8)	(997,179)	(15,094)	(6506.5)
Economic Development	96,581	69,347	39.3	82,356	55,122	49.4
Interest	18,264	21,597	(15.4)	18,264	21,597	(15.4)
Total	<u>\$ 1,961,234</u>	<u>\$ 1,935,040</u>	1.4	<u>\$ 449,310</u>	<u>\$ 1,361,296</u>	(67.0)

**FINANCIAL ANALYSIS OF THE CITY AT THE FUND LEVEL**

The financial performance of the City is reflected in its governmental funds as well. As the City completed the year, its governmental funds reported a combined fund balance of \$2,018,754.

Revenues for the City's governmental funds were \$2,249,916, while total expenditures were \$2,146,300.

The General Fund's fund balance decreased \$7,235 from the prior year. This is due primarily to an increase in capital outlay expenditures relating to highways and streets.

The Fire Fund's fund balance decreased \$14,025 from the prior year, due to an increase in public safety expenditures.

The Business Park Fund's fund balance increased \$113,503 from the prior year, because there were minimal business park expenditures.

**CITY OF PEQUOT LAKES, MINNESOTA  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
YEAR ENDED DECEMBER 31, 2012**

**FINANCIAL ANALYSIS OF THE CITY AT THE FUND LEVEL (CONTINUED)**

The Water Enterprise Fund's net position increased \$13,243 from the prior year. This is due primarily to the decrease in expenses.

The Sewer Enterprise Fund's net position increased \$97,299. This increase is due to an increase in sewer sales revenue and department reorganization.

**GENERAL FUND**

The following schedule presents a summary of General Fund Revenues:

**Table A-4  
General Fund Revenues**

	Year Ended		Change	
	December 31,	December 31,	Increase	Percent
	2012	2011	(Decrease)	
Taxes and Specials	\$ 1,478,517	\$ 1,399,415	\$ 79,102	5.7 %
Intergovernmental	113,249	134,730	(21,481)	(15.9)
Charges for Services	117,537	93,798	23,739	25.3
Interest	9,401	9,773	(372)	(3.8)
Miscellaneous	105,330	143,123	(37,793)	(26.4)
<b>Total General Fund Revenue</b>	<b>\$ 1,824,034</b>	<b>\$ 1,780,839</b>	<b>\$ 43,195</b>	<b>2.4</b>

Total General Fund revenue increased by \$43,195, or (2.4%), from the previous year. This is due primarily to an increase in tax revenues and charges for services.

The following schedule presents a summary of General Fund Expenditures:

**Table A-5  
General Fund Expenditures**

	Year Ended		Change	
	December 31,	December 31,	Increase	Percent
	2012	2011	(Decrease)	
General Government	\$ 439,717	\$ 406,898	\$ 32,819	8.1 %
Public Safety	670,845	667,664	3,181	0.5
Highways and Streets	614,093	278,897	335,196	120.2
Sanitation	11,797	13,128	(1,331)	(10.1)
Culture and Recreation	29,473	35,472	(5,999)	(16.9)
Economic Development	32,908	3,475	29,433	847.0
Debt Service	32,436	98,680	(66,244)	(67.1)
<b>Total Expenditures</b>	<b>\$ 1,831,269</b>	<b>\$ 1,504,214</b>	<b>\$ 327,055</b>	<b>21.7</b>

**CITY OF PEQUOT LAKES, MINNESOTA  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
YEAR ENDED DECEMBER 31, 2012**

**GENERAL FUND (CONTINUED)**

**General Fund Budgetary Highlights**

Over the course of the year, the City did not revise the annual operating budget. Historically, the City has not made budget amendments during the year.

- ◆ Actual revenues were \$125,963 more than expected due to an increase in tax revenues received, intergovernmental revenue, gifts and contributions received to pay off debt, and miscellaneous revenue.
- ◆ The actual expenditures were \$126,498 more than budgeted due to capital outlays for the highways and streets being more than anticipated.

**CONSTRUCTION PROJECTS AND DEBT SERVICE**

Tax revenues and charges for utility services are used to fund the bond payments for all previous bond issues. The City completed two infrastructure projects in the amount of \$329,235.

**CAPITAL ASSETS**

By the end of 2012, the City had invested approximately \$14,800,000 in a broad range of capital assets, including buildings, computers, improvements, equipment, and infrastructure. (See Table A-6). (More detailed information about capital assets can be found in Note 3.A.2 to the financial statements.) Total depreciation expense for the year was \$409,270 (including the enterprise funds).

Table A-6  
The City's Capital Assets

	Governmental Activities		Percent Change	Business-Type Activities		Percent Change	Total		Percent Change
	2012	2011		2012	2011		2012	2011	
Land	\$ 1,520,693	\$ 535,893	183.8 %	\$ 178,167	\$ 178,167	- %	\$ 1,698,860	\$ 714,060	137.9 %
Construction-in-Progress	-	28,757	(100.0)	-	-	-	-	28,757	(100.0)
Infrastructure	5,254,405	4,925,170	6.7	393,117	393,117	-	5,647,522	5,318,287	6.2
Buildings	1,500,001	1,488,758	0.8	1,088,469	1,088,469	-	2,588,470	2,577,227	0.4
Machinery, Equipment, and Vehicles	1,848,649	1,715,073	7.8	3,063,236	3,411,893	(10.2)	4,911,885	5,126,966	(4.2)
Less: Accumulated Depreciation	<u>(3,561,397)</u>	<u>(3,243,589)</u>	9.8	<u>(2,692,190)</u>	<u>(2,972,159)</u>	(9.4)	<u>(6,253,587)</u>	<u>(6,215,748)</u>	0.6
Total	<u>\$ 6,562,351</u>	<u>\$ 5,450,062</u>	20.4	<u>\$ 2,030,799</u>	<u>\$ 2,099,487</u>	(3.3)	<u>\$ 8,593,150</u>	<u>\$ 7,549,549</u>	13.8

**CITY OF PEQUOT LAKES, MINNESOTA  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
YEAR ENDED DECEMBER 31, 2012**

**LONG-TERM LIABILITIES**

At year-end, the City had \$1,796,695 (net of related discounts and premiums) in long-term liabilities outstanding.

- ◆ The City's governmental activities total long-term debt decreased \$65,103 due primarily to payments on a capital lease and equipment certificates and paying off the American National Bank Loan for a fire truck. The City's business-type activities total long-term debt decreased \$151,072 due primarily to the repayment of general obligation bonds in 2012. Additional information on the City's long-term liabilities can be found in note 3 on pages 42-46.

**Table A-7  
The City's Long-Term Liabilities**

	2012	2011	Percentage Change
<b>GOVERNMENTAL ACTIVITIES</b>			
Equipment Certificates	\$ 78,000	\$ 102,000	(23.5)%
Capital Leases	297,951	317,276	(6.1)
Loans Payable	-	35,617	(100.0)
Compensated Absences Payable	33,057	36,091	(8.4)
Other Postemployment Benefit Payable	99,537	82,664	20.4
Total	<u>\$ 508,545</u>	<u>\$ 573,648</u>	(11.3)
<b>BUSINESS-TYPE ACTIVITIES</b>			
General Obligation Bonds	\$ 1,272,357	\$ 1,428,198	(10.9)%
Compensated Absences Payable	2,854	366	679.8
Other Postemployment Benefit Payable	12,939	10,638	21.6
Total	<u>\$ 1,288,150</u>	<u>\$ 1,439,202</u>	(10.5)

**FACTORS BEARING ON THE CITY'S FUTURE**

**Highway 371 Expansion**

The proposed Highway 371 project is expected to begin in 2018. Federal and State funding may have an influence on whether this project takes place in 2018 or perhaps beyond that date. MnDOT will begin right-of-way acquisition in 2015. The City has begun preparing for this project. Issues related to this highway project that will affect the City include roads that will possibly be turned back to the City, County Road 11 as the major corridor entrance to the City, and the City's spray irrigation field.

**CITY OF PEQUOT LAKES, MINNESOTA  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
YEAR ENDED DECEMBER 31, 2012**

**CONTACTING THE CITY'S FINANCIAL MANAGEMENT**

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of the City's finances and to demonstrate the City's accountability for the money it receives. If you have questions about this report or need additional financial information, contact Sandy Peine, City Clerk-Treasurer, Nancy Malecha, Finance Administrator, or Nancy Adams, Mayor at (218) 568-5222.

## **BASIC FINANCIAL STATEMENTS**



## **GOVERNMENT-WIDE FINANCIAL STATEMENTS**



**CITY OF PEQUOT LAKES, MINNESOTA**  
**STATEMENT OF NET POSITION**  
**DECEMBER 31, 2012**

	Governmental Activities	Business-Type Activities	Total
<b>ASSETS</b>			
Cash and Pooled Investments	\$ 2,066,709	\$ 1,207,410	\$ 3,274,119
Petty Cash and Change Funds	942	-	942
Taxes Receivable			
Unapportioned	51,530	-	51,530
Delinquent	121,385	-	121,385
Special Assessments Receivable			
Delinquent	1,844	-	1,844
Deferred	-	2,160	2,160
Accounts Receivable, Net of Allowance	24,512	174,435	198,947
Accrued Interest Receivable	354	-	354
Due from Other Governments	11,313	-	11,313
Loans Receivable	46,099	-	46,099
Deferred Debt Issue Costs	-	48,985	48,985
Land Held for Resale	25,784	-	25,784
Capital Assets not Being Depreciated			
Land	1,520,693	178,167	1,698,860
Capital Assets Being Depreciated			
Building (Net)	1,072,735	38,873	1,111,608
Machinery, Vehicles, Furniture and Equipment (Net)	558,418	1,483,069	2,041,487
Infrastructure (Net)	3,410,505	330,690	3,741,195
<b>Total Assets</b>	<b>8,912,823</b>	<b>3,463,789</b>	<b>12,376,612</b>
<b>LIABILITIES</b>			
Accounts Payable	130,714	141,246	271,960
Salaries Payable	14,274	1,040	15,314
Due to Other Governments	21,017	8,162	29,179
Accrued Interest Payable	2,680	10,779	13,459
Compensated Absences Payable - Due Within One Year	15,230	976	16,206
General Obligation Refunding Bonds Payable - Due Within One Year	-	70,000	70,000
Equipment Certificates - Due Within One Year	25,000	-	25,000
Capital Leases Payable - Due Within One Year	20,162	-	20,162
Compensated Absences Payable - Due in More than One Year	17,826	1,878	19,704
General Obligation Refunding Bonds Payable - Due in More than One Year	-	1,202,357	1,202,357
Equipment Certificates - Due in More than One Year	53,000	-	53,000
Capital Leases Payable - Due in More than One Year	277,789	-	277,789
Other Postemployment Benefits Payable - Due in More than One Year	99,537	12,939	112,476
<b>Total Liabilities</b>	<b>677,229</b>	<b>1,449,377</b>	<b>2,126,606</b>
<b>NET POSITION</b>			
Invested in Capital Assets, Net of Related Debt	6,186,400	758,441	6,944,841
Restricted for Library	24,164	-	24,164
Restricted for Forfeiture	42	-	42
Restricted for Park Dedication	42,662	-	42,662
Restricted for Loans Receivable	46,099	-	46,099
Restricted for Economic Development	17,516	-	17,516
Restricted for Debt Service	30,598	-	30,598
Unrestricted	1,888,113	1,255,971	3,144,084
<b>Total Net Position</b>	<b>\$ 8,235,594</b>	<b>\$ 2,014,412</b>	<b>\$ 10,250,006</b>

See accompanying Notes to Financial Statements.

**CITY OF PEQUOT LAKES, MINNESOTA  
STATEMENT OF ACTIVITIES  
YEAR ENDED DECEMBER 31, 2012**

Functions/Programs	Expenses	Program Revenues		
		Fees, Charges, Fines, and Other	Operating Grants and Contributions	Capital Grants and Contributions
Primary Government				
Governmental Activities				
General Government	\$ 490,853	\$ 30,503	\$ 5,233	\$ -
Public Safety	836,207	271,950	123,433	-
Highways and Streets	456,633	-	-	44
Sanitation	11,797	458	18,000	-
Culture and Recreation	50,899	18,282	44,996	984,800
Economic Development	96,581	-	-	14,225
Interest	18,264	-	-	-
Total Governmental Activities	1,961,234	321,193	191,662	999,069
Business-Type Activities				
Water	229,691	237,201	-	-
Sewer	139,654	227,360	-	-
Total Business-Type Activities	369,345	464,561	-	-
Total Primary Government	\$ 2,330,579	\$ 785,754	\$ 191,662	\$ 999,069

General Revenues

Property Taxes

Grants and Contributions not Restricted for a Particular Purpose

Investment Earnings

Miscellaneous

Gain on Sale of Capital Assets

Total General Revenues and Transfers

**CHANGE IN NET POSITION**

Net Position - Beginning of Year

**NET POSITION - END OF YEAR**

See accompanying Notes to Financial Statements.

Net (Expense) Revenue and  
Changes in Net Assets

Governmental Activities	Business-Type Activities	Total
\$ (455,117)	\$ -	\$ (455,117)
(440,824)	-	(440,824)
(456,589)	-	(456,589)
6,661	-	6,661
997,179	-	997,179
(82,356)	-	(82,356)
(18,264)	-	(18,264)
(449,310)	-	(449,310)
-	7,510	7,510
-	87,706	87,706
-	95,216	95,216
(449,310)	95,216	(354,094)
1,572,603	-	1,572,603
96,274	-	96,274
14,348	10,326	24,674
36,665	5,000	41,665
3,452	-	3,452
1,723,342	15,326	1,738,668
1,274,032	110,542	1,384,574
6,961,562	1,903,870	8,865,432
\$ 8,235,594	\$ 2,014,412	\$ 10,250,006

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## **FUND FINANCIAL STATEMENTS**

**CITY OF PEQUOT LAKES, MINNESOTA  
BALANCE SHEET  
GOVERNMENTAL FUNDS  
DECEMBER 31, 2012**

	Major Funds	
	General	Fire Department
<b>ASSETS</b>		
Cash and Pooled Investments	\$ 1,294,699	\$ 140,211
Petty Cash and Change Funds	942	-
Taxes Receivable		
Current	50,315	-
Delinquent	121,385	-
Special Assessments Receivable		
Delinquent	1,844	-
Accounts Receivable, Net of Allowance	7,057	1,605
Accrued Interest Receivable	354	-
Due from Other Governments	11,313	-
Interfund Receivable	48,919	-
Land Held for Resale	-	-
Loans Receivable	-	-
Total Assets	<u>\$ 1,536,828</u>	<u>\$ 141,816</u>
<b>LIABILITIES AND FUND BALANCES</b>		
<b>LIABILITIES</b>		
Accounts Payable	\$ 73,921	\$ 23,655
Due to Other Governments	21,017	-
Salaries Payable	14,274	-
Interfund Payable	-	-
Deferred Revenue - Unavailable	123,229	850
Total Liabilities	<u>232,441</u>	<u>24,505</u>
<b>FUND BALANCES (DEFICITS)</b>		
Restricted for Forfeiture	42	-
Restricted for Park Dedication	42,662	-
Restricted for Loans Receivable	-	-
Restricted for Other Governmental Funds	-	-
Restricted for Library	24,164	-
Committed for Library	78,629	-
Committed for Capital Outlay	235,255	64,917
Committed for Fire Protection Services	-	52,394
Committed for Business Park	-	-
Committed for Other Governmental Funds	-	-
Committed for Bobber Water Tower	11,245	-
Assigned for Capital Outlay	6,000	-
Unassigned	906,390	-
Total Fund Balances (Deficits)	<u>1,304,387</u>	<u>117,311</u>
Total Liabilities and Fund Balances	<u>\$ 1,536,828</u>	<u>\$ 141,816</u>

See accompanying Notes to Financial Statements.

Business Park	Other Governmental Funds	Total Governmental Funds
\$ 304,323	\$ 327,476	\$ 2,066,709
-	-	942
-	1,215	51,530
-	-	121,385
-	-	1,844
-	15,850	24,512
-	-	354
-	-	11,313
-	-	48,919
25,784	-	25,784
46,099	-	46,099
<u>\$ 376,206</u>	<u>\$ 344,541</u>	<u>\$ 2,399,391</u>

\$ -	\$ 33,138	\$ 130,714
-	-	21,017
-	-	14,274
-	48,919	48,919
25,784	15,850	165,713
<u>25,784</u>	<u>97,907</u>	<u>380,637</u>

-	-	42
-	-	42,662
46,099	-	46,099
-	49,739	49,739
-	-	24,164
-	-	78,629
-	-	300,172
-	-	52,394
304,323	-	304,323
-	257,533	257,533
-	-	11,245
-	-	6,000
-	(60,638)	845,752
<u>350,422</u>	<u>246,634</u>	<u>2,018,754</u>
<u>\$ 376,206</u>	<u>\$ 344,541</u>	<u>\$ 2,399,391</u>

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**CITY OF PEQUOT LAKES, MINNESOTA  
RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO THE  
GOVERNMENT-WIDE STATEMENT OF NET POSITION  
GOVERNMENTAL ACTIVITIES  
DECEMBER 31, 2012**

<b>FUND BALANCES - TOTAL GOVERNMENTAL FUNDS</b>		<b>\$ 2,018,754</b>
Amounts reported for governmental activities in the statement of net assets are different because:		
Capital assets, net of accumulated depreciation, used in governmental activities are not financial resources and, therefore, are not reported in the governmental funds.		6,562,351
Other long-term assets are not available to pay for current-period expenditures and, therefore, are deferred in the governmental funds.		165,713
Long-term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported in the governmental funds.		
Equipment Certificates	\$ (78,000)	
Capital Leases	(297,951)	
Compensated Absences	(33,056)	
Other Postemployment Benefits	(99,537)	
Accrued Interest Payable	(2,680)	
	<u>                    </u>	<u>(511,224)</u>
<b>NET POSITION OF GOVERNMENTAL ACTIVITIES</b>		<b><u><u>\$ 8,235,594</u></u></b>

**CITY OF PEQUOT LAKES, MINNESOTA**  
**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES**  
**GOVERNMENTAL FUNDS**  
**YEAR ENDED DECEMBER 31, 2012**

	Major Funds	
	General Fund	Fire Department
<b>REVENUES</b>		
Taxes	\$ 1,478,068	\$ -
Special Assessments	449	250
Licenses and Permits	15,893	-
Intergovernmental	113,249	36,552
Charges for Services	117,537	163,214
Fines and Forfeits	21,892	-
Gifts and Contributions	36,871	1,200
Interest on Investments	9,401	978
Miscellaneous	30,674	5,969
Total Revenues	1,824,034	208,163
<b>EXPENDITURES</b>		
<b>CURRENT</b>		
General Government	421,696	-
Public Safety	650,899	158,163
Highways and Streets	305,348	-
Sanitation	11,797	-
Culture and Recreation	29,473	-
Economic Development	32,908	-
<b>CAPITAL OUTLAY</b>		
General Government	18,021	-
Public Safety	19,946	27,157
Highways and Streets	308,745	-
<b>DEBT SERVICE</b>		
Principal	19,325	35,617
Interest	13,111	1,251
Total Expenditures	1,831,269	222,188
<b>EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES</b>	(7,235)	(14,025)
<b>OTHER FINANCING SOURCES (USES)</b>		
Proceeds from Sale of Assets	-	-
<b>NET CHANGE IN FUND BALANCES</b>	(7,235)	(14,025)
Fund Balance (Deficit) - Beginning of Year	1,311,622	131,336
<b>FUND BALANCE (DEFICIT) - END OF YEAR</b>	<u>\$ 1,304,387</u>	<u>\$ 117,311</u>

See accompanying Notes to Financial Statements.

Business Park	Other Governmental Funds	Total Governmental Funds
\$ -	\$ 105,562	\$ 1,583,630
14,225	-	14,924
-	-	15,893
-	-	149,801
-	-	280,751
-	-	21,892
93,941	-	132,012
1,946	2,023	14,348
-	22	36,665
110,112	107,607	2,249,916
-	465	422,161
-	-	809,062
-	-	305,348
-	-	11,797
-	-	29,473
61	63,817	96,786
-	-	18,021
-	-	47,103
-	-	308,745
-	24,000	78,942
-	4,500	18,862
61	92,782	2,146,300
110,051	14,825	103,616
3,452	-	3,452
113,503	14,825	107,068
236,919	231,809	1,911,686
\$ 350,422	\$ 246,634	\$ 2,018,754

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**CITY OF PEQUOT LAKES, MINNESOTA  
RECONCILIATION OF THE STATEMENTS OF REVENUES, EXPENDITURES,  
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO  
THE GOVERNMENT-WIDE STATEMENT OF ACTIVITIES  
GOVERNMENTAL ACTIVITIES  
YEAR ENDED DECEMBER 31, 2012**

**NET CHANGE IN FUND BALANCES - TOTAL GOVERNMENTAL FUNDS** \$ 107,068

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

Governmental funds report capital outlay 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.

Expenditures for General Capital Assets, Infrastructure, and Other Related Capital Assets Adjustments	\$ 1,437,097	
Current Year Depreciation	<u>(324,808)</u>	1,112,289

Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the governmental funds.		(11,027)
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Repayment of debt principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net position.

Principal Repayments		
Equipment Certificates	24,000	
Loans Payable	35,617	
Capital Leases	<u>19,325</u>	78,942

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.

Change in Accrued Interest Payable	598	
Change in Compensated Absences	3,035	
Change in Other Postemployment Benefits	<u>(16,873)</u>	<u>(13,240)</u>

<b>CHANGE IN NET POSITION OF GOVERNMENTAL ACTIVITIES</b>		<u><u>\$ 1,274,032</u></u>
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**CITY OF PEQUOT LAKES, MINNESOTA  
STATEMENT OF NET POSITION  
PROPRIETARY FUNDS  
DECEMBER 31, 2012**

	Water Fund	Sewer Fund	Total
<b>ASSETS</b>			
<b>CURRENT ASSETS</b>			
Cash and Pooled Investments	\$ 526,895	\$ 680,515	\$ 1,207,410
Special Assessments			
Deferred	1,039	1,121	2,160
Accounts Receivable (Net)	83,794	90,641	174,435
Total Current Assets	<u>611,728</u>	<u>772,277</u>	<u>1,384,005</u>
<b>NONCURRENT ASSETS</b>			
Deferred Debt Issue Costs	48,985	-	48,985
Capital Assets			
Land	21,198	156,969	178,167
Building (Net)	-	38,873	38,873
Machinery, Vehicles, Furniture and Equipment (Net)	1,352,510	130,559	1,483,069
Infrastructure (Net)	83,125	247,565	330,690
Total Noncurrent Assets	<u>1,505,818</u>	<u>573,966</u>	<u>2,079,784</u>
Total Assets	2,117,546	1,346,243	3,463,789
<b>LIABILITIES</b>			
<b>CURRENT LIABILITIES</b>			
Accounts Payable	73,540	67,706	141,246
Salaries Payable	520	520	1,040
Due to Other Governments	4,081	4,081	8,162
Accrued Interest Payable	10,779	-	10,779
Compensated Absences Payable	488	488	976
General Obligation Bonds Payable - Due Within One Year	70,000	-	70,000
Total Current Liabilities	<u>159,408</u>	<u>72,795</u>	<u>232,203</u>
<b>NONCURRENT LIABILITIES</b>			
General Obligation Bonds Payable - Due in More than One Year	1,202,357	-	1,202,357
Compensated Absences Payable - Due in More than One Year	939	939	1,878
Other Postemployment Benefits Payable - Due in More than One Year	6,470	6,469	12,939
Total Noncurrent Liabilities	<u>1,209,766</u>	<u>7,408</u>	<u>1,217,174</u>
Total Liabilities	<u>1,369,174</u>	<u>80,203</u>	<u>1,449,377</u>
<b>NET POSITION</b>			
Invested in Capital Assets, Net of Related Debt	184,475	573,966	758,441
Unrestricted	<u>563,897</u>	<u>692,074</u>	<u>1,255,971</u>
Total Net Position	<u>\$ 748,372</u>	<u>\$ 1,266,040</u>	<u>\$ 2,014,412</u>

See accompanying Notes to Financial Statements.

**CITY OF PEQUOT LAKES, MINNESOTA**  
**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION**  
**PROPRIETARY FUNDS**  
**YEAR ENDED DECEMBER 31, 2012**

	Water Fund	Sewer Fund	Total
<b>OPERATING REVENUES</b>			
Charges for Services	\$ 229,142	\$ 226,249	\$ 455,391
Miscellaneous Operating	7,981	1,051	9,032
Total Operating Revenues	237,123	227,300	464,423
<b>OPERATING EXPENSES</b>			
Personal Services	25,483	25,482	50,965
Professional Services	27,441	30,136	57,577
Other Services and Charges	7,318	3,275	10,593
Supplies	14,916	5,848	20,764
Repairs and Maintenance	9,417	32,630	42,047
Utilities	13,558	14,050	27,608
Insurance	3,708	4,326	8,034
Dues and Subscriptions	4,617	2,720	7,337
Depreciation	63,275	21,187	84,462
Total Operating Expenses	169,733	139,654	309,387
<b>OPERATING INCOME (LOSS)</b>	67,390	87,646	155,036
<b>NONOPERATING REVENUES (EXPENSES)</b>			
Intergovernmental	7	7	14
Special Assessment Charges	71	53	124
Interest Income	5,733	4,593	10,326
Rent	-	5,000	5,000
Interest Expense	(59,958)	-	(59,958)
Total Nonoperating Revenues (Expenses)	(54,147)	9,653	(44,494)
<b>CHANGE IN NET POSITION</b>	13,243	97,299	110,542
Net Position - Beginning of Year	735,129	1,168,741	1,903,870
<b>NET POSITION - END OF YEAR</b>	<u>\$ 748,372</u>	<u>\$ 1,266,040</u>	<u>\$ 2,014,412</u>

See accompanying Notes to Financial Statements.

**CITY OF PEQUOT LAKES, MINNESOTA  
STATEMENT OF CASH FLOWS  
PROPRIETARY FUNDS  
YEAR ENDED DECEMBER 31, 2012**

	Water Fund	Sewer Fund	Total
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Receipts from Customers and Users	\$ 237,802	\$ 221,404	\$ 459,206
Payments to Suppliers	(74,777)	(90,225)	(165,002)
Payments to Employees	(22,735)	(22,734)	(45,469)
Net Cash Provided (Used) by Operating Activities	140,290	108,445	248,735
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>			
Intergovernmental	7	7	14
Rent Deposits	-	5,000	5,000
Net Cash Provided (Used) by Noncapital Financing Activities	7	5,007	5,014
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>			
Principal Paid on Long-Term Debt	(1,425,841)	-	(1,425,841)
Interest Paid on Long-Term Debt	(113,448)	-	(113,448)
Special Assessments	(493)	(924)	(1,417)
Deferred Debt Issuance Costs	(48,985)	-	(48,985)
Proceeds from Issuance of Long-Term Debt	1,270,000	-	1,270,000
Purchases of Capital Assets	(3,220)	(12,554)	(15,774)
Net Cash Provided (Used) by Capital and Related Financing Activities	(321,987)	(13,478)	(335,465)
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Investment Earnings Received	5,733	4,593	10,326
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	(175,957)	104,567	(71,390)
Cash and Cash Equivalents - Beginning of Year	702,852	575,948	1,278,800
<b>CASH AND CASH EQUIVALENTS - END OF YEAR</b>	<b>\$ 526,895</b>	<b>\$ 680,515</b>	<b>\$ 1,207,410</b>
Reconciliation of Operating Income (Loss) to			
Net Cash Provided (Used) by Operating Activities			
Operating Income (Loss)	\$ 67,390	\$ 87,646	\$ 155,036
Adjustments to Reconcile Operating Income (Loss) to			
Net Cash Provided (Used) by Operating Activities			
Depreciation Expense	63,275	21,187	84,462
(Increase) Decrease in Accounts Receivable	679	(5,896)	(5,217)
Increase (Decrease) in Accounts Payable	2,142	(1,296)	846
Increase (Decrease) in Salaries Payable	353	353	706
Increase (Decrease) in Due to Other Governments	4,056	4,056	8,112
Increase (Decrease) in Compensated Absences Payable	1,244	1,244	2,488
Increase (Decrease) in Other Postemployment Benefits Payable	1,151	1,151	2,302
Total Adjustments	72,900	20,799	93,699
Net Cash Provided (Used) by Operating Activities	<b>\$ 140,290</b>	<b>\$ 108,445</b>	<b>\$ 248,735</b>

See accompanying Notes to Financial Statements.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The City of Pequot Lakes' (City) financial statements are prepared in accordance with generally accepted accounting principles (GAAP). The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (statements and interpretations). The more significant accounting policies established in GAAP and used by the City are discussed below.

**A. Financial Reporting Entity**

The City of Pequot Lakes was formed and operates pursuant to applicable Minnesota laws. The City operates under a Mayor-Council form of government with a full-time City Clerk-Treasurer and provides the following services: public safety (police and fire), public works, culture-recreation, public improvements, planning and zoning, and general administrative services. The City also operates public water and sewer utilities.

As required by generally accepted accounting principles, these financial statements present City of Pequot Lakes (primary government) and its component units for which the City is financially accountable. There is financial accountability if the Primary Government appoints a voting majority of an organization's governing body and has the ability to impose its will on that governing body; or there is the potential for the organization to provide specific financial benefits or to impose specific financial burden on the Primary Government. Based on the criteria for determining component units, the City is not required to include any component units.

**B. Government-Wide and Fund Financial Statements**

The government-wide financial statements (i.e., the statement of net position and the statement of activities) report information about the Primary Government. These statements include the financial activities of the overall City government. Eliminations have been made to minimize the double-counting of internal activities. 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 to external parties for support.

The statement of activities demonstrates the degree to which the direct expenses of each function of the City's governmental activities and different business-type activity are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or activity. Program revenues include: (1) fees, fines, and charges paid by the recipients of goods, services, or privileges provided by a given function or activity; and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or activity. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**B. Government-Wide and Fund Financial Statements (Continued)**

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.

The City reports the following major governmental funds:

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

Fire Department Fund – The Fire Fund, a special revenue fund, is used to account for charges for services, grants, and contributions that are restricted and committed for the operation and maintenance of the fire service to the City and surrounding areas.

Business Park Fund – The Business Park Fund, a special revenue fund, is used to account for special assessments and other revenue committed to the fund.

The City reports the following major proprietary funds:

Water Fund – The Water Fund accounts for the activities of the City's water wells' operations.

Sewer Fund – The Sewer Fund accounts for the activities of the City's sewer system.

**C. Measurement Focus and Basis of Accounting**

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

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. The City considers all revenues to be available if they are collected within 60 days after the end of the current period. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, and compensated absences, which are recognized as expenditures to the extent that they have matured. Proceeds of general long-term debt and acquisitions under capital leases are reported as other financing sources.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

**C. Measurement Focus and Basis of Accounting (Continued)**

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

When both restricted and unrestricted resources are available for use, it is the City's policy to use restricted resources first, then unrestricted resources as they are needed.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenue of the City's enterprise funds are charges to customers for sales of goods and services. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

**D. Assets, Liabilities, and Net Position or Equity**

**1. Cash and Investments (Including Cash Equivalents)**

Cash balances are invested to the extent available in various securities as authorized by *Minnesota Statutes*. Investment earnings are recorded in the individual fund carrying the investment. Investments are stated at fair value.

Cash equivalents are considered to be short-term, highly liquid investments that are readily convertible to cash and have original maturities of three months or less.

For the purposes of the statement of cash flows of the proprietary fund types, the City considers all cash and investments under the classifications current assets to be cash and cash equivalents, except those held with fiscal agent. Cash and cash equivalents consist of checking and saving certificate accounts, cash on hand, and money market savings accounts.

**2. Short-Term Interfund Receivables/Payables**

During the course of operations, numerous transactions occur between individual funds for goods provided or services rendered. These receivables and payables are classified as "due from other funds" or "due to other funds" on the fund financial statements. Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as internal balances.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

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

**3. Accounts Receivable**

The City has provided an allowance for uncollectable accounts receivable based on specific identification method. An allowance is estimated for these loans based on the historical experience of the City and knowledge of TIF District 1-13's operations. At December 31, 2012, the allowance for uncollectable accounts receivable in the TIF 1-13 fund is \$47,550.

**4. Special Assessments**

Special assessments are levied against the benefited properties for the assessable costs of improvement projects in accordance with *Minnesota Statutes*. Assessments are collectible over a term of years at an interest rate established by the City Council upon adoption of each assessment roll. Any annual installments remaining unpaid as of November 30th of each year are certified to the County for collection with property taxes during the following year.

Special assessments receivable represents the past six years of uncollected special assessments. Property owners are allowed to prepay future installments without interest or prepayment penalties.

In the governmental fund financial statements, special assessment levies are recorded as a receivable and as deferred revenue at the time of the levy. Deferred revenue is recognized as current revenue as the annual assessment installments become measurable and available. Interest on special assessments is also recognized when it becomes measurable and available.

**5. Capital Assets**

Capital assets, which include property, plant, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items) are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. In the case of the initial capitalization of infrastructure, the City retroactively implemented the reporting of this item when GASB #34 was implemented. Capital assets are defined by the government as assets with an initial, individual cost of more than \$2,500 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets of business-type activities, when applicable, is included as part of the capitalized value of the assets constructed.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

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

**5. Capital Assets (Continued)**

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

Assets	Years
Buildings	25-75
Infrastructure	15-75
Machinery, Furniture, and Equipment	3-15

**6. Compensated Absences**

Compensated absences include accumulated vacation, compensatory time, and sick leave. All full time employees of the City are entitled to annual vacation and sick leave with pay. Employees are allowed to accumulate 120 hours of vacation time to carry over to the following year. Employees earn vacation from 40 to 160 hours per year, depending on length of service. Sick leave of one day per month is earned with a 960 hour maximum. Upon retirement the employee is paid for all accumulated, unused vacation and a portion of the unused sick leave. Unused sick leave is paid out at termination for full-time employees as follows: 10% of total unused sick leave if five to nine years of service and 25% of unused sick leave if more than ten years of service with the City.

Compensated absences (including sick leave payments) are accrued when incurred in the government-wide financial statements. A liability and related expenditure for these amounts is reported in the governmental funds only if they have matured, for example, as a result of known employee resignations and retirements.

In the City's proprietary funds, amounts earned but unused for vacation leave and that portion of earned but unused sick leave estimated to be payable upon retirement are reflected under the accrual basis of accounting.

**7. Other Postemployment Benefits**

In the government-wide financial statements, and proprietary fund types in the fund financial statements, other postemployment benefit obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type statement of net assets. These other postemployment benefit liabilities are an estimate based on an actuarial valuation.

**8. Long-Term Obligations**

In the government-wide financial statements, and proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type statement of net position. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds or loans payable using the straight-line method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

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

**8. Long-Term Obligations (Continued)**

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

**9. Fund Balance/Net Position**

In the fund financial statements, governmental funds report components of fund balance to provide information about fund balance availability for appropriation. Nonspendable fund balance represents amounts that are inherently nonspendable or assets that will never be converted to cash or will be converted to cash soon enough to affect the current period. Restricted fund balance represents amounts available for appropriation but intended for a specific use and is legally restricted by outside parties. Committed fund balance represents constraints on spending that the government imposes upon itself by high-level formal action prior to the close of the fiscal period. Assigned fund balance represents resources intended for spending for a purpose set by the government body itself or by some person or body delegated to exercise such authority in accordance with policy established by the board. Unassigned fund balance is the residual classification for the City's general fund and includes all spendable amounts not contained in the other classifications. It is the City's policy that at the end of each fiscal, the City will set aside fund balance in the general fund up to 50% of the following year's general fund budgeted expenditures for cash flow purposes.

When an expenditure is incurred for purposes for which both restricted and unrestricted fund balance is available, it is the City's policy to use restricted first, then unrestricted fund balance. When an expenditure is incurred for purposes for which committed, assigned, and unassigned amounts are available, it is the City's policy to use committed first, then assigned, and finally unassigned amounts.

Net position represents the difference between assets and liabilities in the government-wide financial statements. Net investment in capital assets, net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any long-term debt used to build or acquire capital assets.

Net position is reported as restricted in government-wide financial statements when there are limitations on its use through external restrictions imposed by creditors, grantors, or laws or regulations of other governments.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

E. Revenues, Expenditures, and Expenses

**1. Revenues**

In the fund financial statements, property taxes are recognized to the extent they are collected and received in the current period or within 60 days after year-end. Portions paid by the State in the form of market value credit aid, and other state tax credits are included in intergovernmental revenues. Delinquent property taxes receivable which have not been recognized as revenue are equally offset in the financial statements by deferred revenues.

Licenses and permits, charges for services, fines, forfeits, and miscellaneous revenues are recorded as revenues when measurable and available.

Special assessments principal and interest earnings are recorded as revenues in the same manner as property taxes.

Property Tax Collection Calendar

The City levies its property taxes for the subsequent year during the month of December. In Minnesota, the lien date and assessment date is January 2. The property tax is recorded as revenue when it becomes available. Crow Wing County is the collecting agency for the levy and then remits the collection to the City. All taxes not collected as of December 31 are shown as delinquent taxes receivable.

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

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

Property owners are required to pay one-half of their real estate taxes by May 15 and the balances by October 15.

Within 30 days after the May settlement, the County Treasurer is required to pay 70 percent of the estimated collections of taxes and special assessments to the City Treasurer. The County Treasurer must pay the balance to the City Treasurer within 60 days after the settlement, provided that after 45 days interest begins to accrue.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

E. Revenues, Expenditures, and Expenses (Continued)

**1. Revenues (Continued)**

Property Tax Collection Calendar (Continued)

Current year property tax revenues represent the tax levy certified to the County Auditor in December of 2011 which was collected during the year ended December 31, 2012. Any adjustments or abatements to either the current, or any prior year, levy are adjusted through the current year general property tax revenues. Property taxes not collected by the County and remitted to the City within 60 days of year end are classified as delinquent and not considered measurable and available and are fully offset by deferred revenue in the governmental fund financial statements. Delinquent taxes receivable represent the past six years of uncollected tax years. No allowance for uncollectible taxes has been provided because such amounts are not expected to be material.

Within ten business days after November 15, the County Treasurer shall pay to each taxing district, except any school district, 100 percent of the estimated collections arising from taxes levied by and belonging to each taxing district from May 20 to November 20.

**2. Expenditures**

Expenditure recognition for governmental fund types includes only amounts represented by current liabilities. Since noncurrent liabilities do not affect net current assets, they are not recognized as governmental fund expenditures or liabilities. They are reported as liabilities on the statement of net position.

**3. Expenses**

Proprietary funds recognize expenses, including compensated absences, when they are incurred.

**NOTE 2 STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY**

Deficit Fund Balance

The TIF 1-13 Lonesome Cottage Special Revenue Fund has a deficit fund balance as of December 31, 2012. The amount of the deficit is \$60,638 and is due to timing of when the expenditures occurred for this project and when the revenues will be received in the future. This deficit will be corrected through normal government operations as taxes are collected in the future and transfers, as needed.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 3 DETAILED NOTES ON ALL FUNDS**

A. Assets

**1. Deposits and Investments**

The cash balances of substantially all funds are pooled by the City Clerk-Treasurer for the purpose of increasing earning through investment activities. Pooled and fund investments are reported at their fair value at December 31, 2012, based on market prices. Investment earnings on cash and pooled investments are credited to the general fund. In addition other funds received investment earnings based on other state statutes, grant agreements, contracts, and bond covenants.

In accordance with applicable Minnesota State Statutes, the City maintains deposits at financial institutions authorized by the City Council. All such deposits are members of the Federal Reserve System. *Minnesota Statutes* require that all deposits be protected by insurance, surety bond, or collateral. The market value of collateral pledged must equal 110% of the deposits not covered by insurance or corporate surety bonds.

**Custodial Credit Risk – Deposits –** In the case of deposits, custodial credit risk is the risk that in the event of bank failure, the City's deposits may not be returned to it. The City's deposit policy does not provide additional restrictions beyond Minnesota State Statutes to the type of risk.

Authorized collateral includes: U.S. government treasury bills, notes, and or bonds; issued of the U.S. government agency; general obligation of local government related "A" or better; revenue obligations of a state or local government rated "AA" or better; irrevocable standby letters of credit issued by a Federal Home Loan Bank; and time deposits insured by a federal agency. *Minnesota Statutes* required securities pledged as collateral be held in safekeeping in a restricted account at the Federal Reserve Bank or at an account at a trust department of a commercial bank or other financial institution not owned or controlled by the depository. As of December 31, 2012, no City deposits were subject to custodial credit risk.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 3 DETAILED NOTES ON ALL FUNDS (CONTINUED)**

A. Assets (Continued)

**1. Deposits and Investments (Continued)**

*Minnesota Statutes* §§ 118A.04 and 118A.05 generally authorize the following types of investments as available to the City:

- a) securities which are direct obligations or are guaranteed or insured issues of the United States, its agencies, its instrumentalities, or organizations created by an act of Congress, except mortgage-backed securities defined as "high risk" by *Minnesota Statutes* §118A.04, subd. 6;
- b) mutual funds through shares of registered investment companies provided the mutual fund receives certain ratings depending on its investments;
- c) general obligations of the state of Minnesota and its municipalities, and in certain state agency and local obligations of Minnesota and other states provided such obligations have certain specified bond ratings by a national bond rating service;
- d) bankers' acceptances of United States banks;
- e) commercial paper issued by United States corporations or their Canadian subsidiaries that is rated in the highest quality category by two nationally recognized rating agencies and matures in 270 days or less; and
- f) with certain restrictions, in repurchase agreements, securities lending agreements, joint powers investment trusts, and guaranteed investment contracts.

At December 31, 2012, the City did not have any investments.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 3 DETAILED NOTES ON ALL FUNDS (CONTINUED)**

A. Assets (Continued)

**2. Capital Assets**

Capital asset activity for the governmental activities of the City for the year ended December 31, 2012, is as follows:

	Beginning Balance	Additions	Deletions	Ending Balance
Capital Assets, not Being Depreciated				
Land and Right of Way	\$ 535,893	\$ 984,800	\$ -	\$ 1,520,693
Construction in Progress	28,757	275,295	304,052	-
Total Capital Assets not Being Depreciated	564,650	1,260,095	304,052	1,520,693
Capital Assets Being Depreciated				
Buildings	1,488,758	11,243	-	1,500,001
Machinery, Furniture, and Equipment	1,715,073	140,576	7,000	1,848,649
Infrastructure	4,925,170	329,235	-	5,254,405
Total Capital Assets Being Depreciated	8,129,001	481,054	7,000	8,603,055
Less: Accumulated Depreciation for				
Buildings	374,101	53,165	-	427,266
Machinery, Furniture, and Equipment	1,196,723	100,508	7,000	1,290,231
Infrastructure	1,672,765	171,135	-	1,843,900
Total Accumulated Depreciation	3,243,589	324,808	7,000	3,561,397
Total Capital Assets, Depreciated, Net	4,885,412	156,246	-	5,041,658
Governmental Activities Capital Assets, Net	\$ 5,450,062	\$ 1,416,341	\$ 304,052	\$ 6,562,351

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 3 DETAILED NOTES ON ALL FUNDS (CONTINUED)**

A. Assets (Continued)

**2. Capital Assets (Continued)**

The following is a summary of the proprietary fund capital assets for the year ended December 31, 2012:

	Beginning Balance	Additions	Deletions	Ending Balance
Capital Assets, not Being Depreciated				
Land	\$ 178,167	\$ -	\$ -	\$ 178,167
Capital Assets Being Depreciated				
Buildings	1,088,469	-	-	1,088,469
Machinery and Vehicles	3,411,893	15,774	364,431	3,063,236
Infrastructure	393,117	-	-	393,117
Total Capital Assets Being Depreciated	4,893,479	15,774	364,431	4,544,822
Less: Accumulated Depreciation for:				
Buildings	1,047,006	2,592	-	1,049,598
Machinery and Vehicles	1,875,417	69,179	364,431	1,580,165
Infrastructure	49,736	12,691	-	62,427
Total Accumulated Depreciation	2,972,159	84,462	364,431	2,692,190
Total Capital Assets, Depreciated, Net	1,921,320	(68,688)	-	1,852,632
Business-Type Activities Capital Assets, Net	\$ 2,099,487	\$ (68,688)	\$ -	\$ 2,030,799

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 3 DETAILED NOTES ON ALL FUNDS (CONTINUED)**

A. Assets (Continued)

**2. Capital Assets (Continued)**

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

Governmental Activities		
General Government	\$	62,655
Public Safety		49,229
Highways and Streets, Including Depreciation of Infrastructure Assets		190,377
Culture and Recreation		22,547
Total Depreciation Expense - Governmental Activities	<u>\$</u>	<u>324,808</u>
Business-Type Activity		
Water Fund	\$	63,275
Sewer Fund		21,187
Total Depreciation Expense - Business-Type Activities	<u>\$</u>	<u>84,462</u>

B. Interfund Receivables and Payables

Receivable Fund	Payable Fund	Amount
Major Funds		
General	TIF 1-13 Lonesome Cottage	<u>\$ 48,919</u>

The above payable relates to a negative pooled cash balance.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 3 DETAILED NOTES ON ALL FUNDS (CONTINUED)**

C. Liabilities

**1. Long-Term Debt**

General Obligation Bonds

The City issues general obligation bonds to provide funds for the acquisition and construction of major capital facilities including infrastructure. General obligation bonds have been issued for both general government and proprietary activities. Bonds issued to provide funds for proprietary activities are reported in proprietary funds if they are expected to be repaid from proprietary revenues.

General obligation bonds are direct obligations and pledge the full faith and credit of the City. Assets of the general fund and the enterprise funds, together with scheduled future ad valorem tax levies, tax increments and special assessments, are dedicated for the retirement of these bonds.

General Obligation Refunding Bonds

On August 9, 2012, the City issued \$1,270,000 in General Obligation Utility Refunding Bonds Series 2012A to currently refund \$1,428,198 on the General Obligation Bond, Series 2000A and 2000B. The refunding was undertaken to reduce future interest costs and resulting in savings of \$761,150 and an economic gain of \$432,623

Equipment Certificates

The City issued \$115,000 of equipment certificates on May 12, 2010 to provide funds for the acquisition of four police cars. Repayment of the principal will be five annual installments, plus a fixed interest rate of 5%, commencing February 1, 2011.

Capital Lease Obligations

The City issued a capital lease for the City Hall building. Certain assets of the general fund, together with scheduled future ad valorem levies are dedicated for the retirement of this obligations.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 3 DETAILED NOTES ON ALL FUNDS (CONTINUED)**

C. Liabilities (Continued)

**2. Components of Long-Term Debt**

Types of Indebtedness	Final Maturity	Installment Amounts	Interest Rates (%)	Original Issued Amount	Outstanding Balance December 31, 2012	Due Within One Year
<b>Business-Type Activities</b>						
<b>Water Fund</b>						
General Obligation Utility Refunding Bonds of 2012	2031	\$55,000 - \$85,000	0.6 - 3.1%	\$ 1,270,000	\$ 1,270,000	\$ 70,000
Plus: Unamortized Premium					2,357	-
Total Water Fund, Net					<u>\$ 1,272,357</u>	<u>\$ 70,000</u>
<b>Governmental Activities</b>						
<b>General Obligation Bonds</b>						
Equipment Certificates, Series 2010	2015	\$13,000- \$27,000	5.0%	\$ 115,000	\$ 78,000	\$ 25,000
<b>Capital Leases</b>						
City Hall Building	2024	\$34,583	4.25%	1,097,442	297,951	20,162
Total Governmental Activities Long-Term Debt				<u>1,212,442</u>	<u>375,951</u>	<u>45,162</u>
Total Long-Term Debt				<u>\$ 2,482,442</u>	<u>\$ 1,648,308</u>	<u>\$ 115,162</u>

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 3 DETAILED NOTES ON ALL FUNDS (CONTINUED)**

C. Liabilities (Continued)

**3. Changes in Long-Term Liabilities**

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Governmental Activities:					
Equipment Certificates	\$ 102,000	\$ -	\$ 24,000	\$ 78,000	\$ 25,000
Capital Leases	317,276	-	19,325	297,951	20,162
Loans Payable	35,617	-	35,617	-	-
Compensated Absences	36,091	80,271	83,305	33,057	15,230
Other Postemployment Benefits	82,664	16,873	-	99,537	-
Governmental Activities Long-Term Debt	<u>\$ 573,648</u>	<u>\$ 97,144</u>	<u>\$ 162,247</u>	<u>\$ 508,545</u>	<u>\$ 60,392</u>
Business-Type Activities:					
General Obligation Bonds	\$ 1,428,198	\$ -	\$ 1,428,198	\$ -	\$ -
General Obligation Refunding Bonds	-	1,270,000	-	1,270,000	70,000
Bond Premium	-	2,482	125	2,357	-
Compensated Absences	366	6,436	3,948	2,854	976
Other Postemployment Benefits	10,638	2,301	-	12,939	-
Business-Type Activities Long-Term Debt	<u>\$ 1,439,202</u>	<u>\$ 1,281,219</u>	<u>\$ 1,432,271</u>	<u>\$ 1,288,150</u>	<u>\$ 70,976</u>

**4. Refunding Debt Issued**

During 2012, the City issued General Obligation Utility Refunding Bonds, Series 2012A in the amount of \$1,270,000 with interest rates from 0.6 percent to 3.1 percent, along with \$150,000 of City funds to provide for the current refunding of the General Obligation Bonds Series 2000A and 2000B on October 1, 2012.

As a result of this refunding, the City will decrease its debt service requirements \$611,725, resulting in an economic gain (difference between the present value of the debt service payments on the old and new debt service) of \$283,198.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 3 DETAILED NOTES ON ALL FUNDS (CONTINUED)**

C. Liabilities (Continued)

**5. Minimum Debt Payments**

The annual requirements to amortize general obligation debt outstanding are as follows:

Year Ending December 31,	Business-Type Activities		
	General Obligation		
	Principal	Interest	Total
2013	\$ 70,000	\$ 25,660	\$ 95,660
2014	55,000	25,285	80,285
2015	55,000	24,955	79,955
2016	60,000	24,520	84,520
2017	60,000	23,980	83,980
2018-2022	305,000	107,580	412,580
2023-2027	345,000	74,265	419,265
2028-2031	320,000	20,305	340,305
Total	<u>\$1,270,000</u>	<u>\$ 326,550</u>	<u>\$ 1,596,550</u>

Year Ending December 31,	Governmental Activities		
	Capital Leases		
	Principal	Interest	Total
2013	\$ 20,162	\$ 12,273	\$ 32,435
2014	21,036	11,399	32,435
2015	21,948	10,488	32,436
2016	22,899	9,537	32,436
2017	23,891	8,544	32,435
2018-2022	135,915	26,263	162,178
2023-2027	52,100	1,960	54,060
Total	<u>\$ 297,951</u>	<u>\$ 80,464</u>	<u>\$ 378,415</u>

Year Ending December 31,	Governmental Activities		
	Equipment Certificates		
	Principal	Interest	Total
2013	\$ 25,000	\$ 3,275	\$ 28,275
2014	26,000	2,000	28,000
2015	27,000	675	27,675
2016	-	-	-
2017	-	-	-
2018-2022	-	-	-
2023-2027	-	-	-
Total	<u>\$ 78,000</u>	<u>\$ 5,950</u>	<u>\$ 83,950</u>

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 3 DETAILED NOTES ON ALL FUNDS (CONTINUED)**

C. Liabilities (Continued)

**5. Minimum Debt Payments (Continued)**

At year-end, included in capital assets related to these capital leases are assets recorded at \$1,056,200 for the City Hall building. There was accumulated depreciation of \$320,632 for the City Hall.

**6. Operating Leases**

The City leases a copier and a postage machine under operating leases. Total costs for these leases were \$6,184 for the year ended December 31, 2012. The future minimum lease obligations as of December 31, 2012, were as follows:

Year Ended	Amount
2013	\$ 3,045
2014	1,923
2015	1,602
Total	<u>\$ 6,570</u>

**NOTE 4 RISK MANAGEMENT**

The City is exposed to various risks of loss related to: torts, theft of, damage to, or destruction of assets; errors or omissions; injuries to employees; or natural disasters. The City has entered into a joint powers agreement with the League of Minnesota Cities Insurance Trust (LMCIT). The LMCIT is a public entity risk pool currently operating as common risk management and insurance program for Minnesota cities. The agreement for formation of the LMCIT provides that the pool will be self-sustaining through member assessments and will reinsure through commercial companies for claims in excess of reserved amounts for each insured event. The pool can make additional assessments to make the pool self-sustaining. The City has determined that it is not possible to estimate the amount of such additional assessments; however, they are not expected to be material to the financial statements.

The City also carries commercial insurance for certain other risks of loss, including employee health insurance. There were no significant reductions in insurance coverage from the previous year or settlements in excess of insurance coverage for any of the past three fiscal years.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 5 PENSION PLANS**

A. Public Employees Retirement Association

Plan Description

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

GERF members belong to either the Coordinated Plan or the Basic Plan. Coordinated Plan members are covered by Social Security and Basic Plan members are not. All new members must participate in the Coordinated Plan. All police officers, fire-fighters and peace officers who qualify for membership by statute are covered by the PEPFF.

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

Two methods are used to compute benefits for PERA's Coordinated and Basic Plan members. The retiring member receives the higher of a step-rate benefit accrual formula (Method 1) or a level accrual formula (Method 2). Under Method 1, the annuity accrual rate for a Basic Plan member is 2.2 percent of average salary for each of the first ten years of service and 2.7 percent for each remaining year. The annuity accrual rate for a Coordinated Plan member is 1.2 percent of average salary for each of the first ten years and 1.7 percent for each remaining year. Under Method 2, the annuity accrual rate is 2.7 percent of average salary for Basic Plan members and 1.7 percent for Coordinated Plan members for each year of service. For PEPFF members, the annuity accrual rate is 3.0 percent for each year of service. For all PEPFF members and GERF members hired prior to July 1, 1989 whose annuity is calculated using Method 1, a full annuity is available when age plus years of service equal 90. Normal retirement age is 55 for PEPFF and 65 for Basic and Coordinated members hired prior to July 1, 1989. Normal retirement age is the age for unreduced Social Security benefits capped at 66 for Coordinated members hired on or after July 1, 1989. A reduced retirement annuity is also available to eligible members seeking early retirement.

There are different types of annuities available to members upon retirement. A single-life annuity is a lifetime annuity that ceases upon the death of the retiree--no survivor annuity is payable. There are also various types of joint and survivor annuity options available which will be payable over joint lives. Members may also leave their contributions in the fund upon termination of public service in order to qualify for a deferred annuity at retirement age. Refunds of contributions are available at any time to members who leave public service, but before retirement benefits begin.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 6 PENSION PLANS (CONTINUED)**

A. Public Employees Retirement Association (Continued)

Plan Description (Continued)

The benefit provisions stated in the previous paragraphs of this section are current provisions and apply to active plan participants. Vested, terminated employees who are entitled to benefits but are not receiving them yet are bound by the provisions in effect at the time they last terminated their public service.

PERA issues a publicly available financial report that includes financial statements and required supplementary information for GERF and PEPFF. That report may be obtained on the Internet at [www.mnpera.org](http://www.mnpera.org), by writing to PERA at 60 Empire Drive #200, St. Paul, Minnesota, 55103-2088 or by calling (651) 296-7460 or 1-800-652-9026.

Funding Policy

*Minnesota Statutes*, Chapter 353 sets the rates for employer and employee contributions. These statutes are established and amended by the state legislature. The City makes annual contributions to the pension plans equal to the amount required by state statutes. GERF Basic Plan members and Coordinated Plan members were required to contribute 9.10% and 6.25%, respectively, of their annual covered salary in 2012. PEPFF members are required to contribute 9.6% of their annual covered salary in 2012. The City of Pequot Lakes is required to contribute the following percentages of annual covered payroll: 11.78% for Basic Plan GERF members, 7.25% for Coordinated Plan GERF members and 14.4% for PEPFF members. The City's contributions to the General Employees Retirement Fund and the Public Employees Police and Fire Fund for the years ending December 31, 2012, 2011, and 2010 were:

	General Employees Retirement Fund	Public Employees Police and Fire Fund
2012	\$ 21,921	\$ 44,149
2011	22,625	39,359
2010	25,800	41,908

These contribution amounts are equal to the contractually required contributions for each year as set by state statute.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 6 PENSION PLANS (CONTINUED)**

**B. Defined Contribution Plan**

Three elected officials of the City are covered by the Public Employees Defined Contribution Plan (PEDCP), a multiple-employer deferred compensation plan administered by the Public Employees Retirement Association of Minnesota (PERA). The PEDCP is a tax qualified plan under Section 401(a) of the Internal Revenue Code and all contributions by or on behalf of employees are tax deferred until time of withdrawal.

Plan benefits depend solely on amounts contributed to the plan plus investment earnings, less administrative expenses. *Minnesota Statutes*, Chapter 353D.03, specifies the employee and employer contribution rates for those qualified personnel who elect to participate. An eligible elected official who decides to participate contributes 5% of salary which is matched by the elected official's employer. Employees who are paid for their services may elect to make member contributions in an amount not to exceed the employer share. Employer and employee contributions are combined and used to purchase shares in one or more of the seven accounts of the Minnesota Supplemental Investment Fund. For administering the plan, PERA receives 2% of employer contributions and twenty-five hundredths of one percent of the assets in each member's account annually.

The employer's contribution amounts for the years ending December 31, 2012, 2011, and 2010 were \$449, \$474, and \$894, respectively, equal to the contractually required contributions for each year as set by state statute.

**C. Pequot Lakes Fire Department Relief Association**

Plan Description

The Public Employee Retirement System (PERS) Plan is a single-employer defined benefit pension plan administered by the Pequot Lakes Fire Department Relief Association. The Plan provides retirement, disability, and death benefits to plan members and beneficiaries. Benefits are established by state statute. The Pequot Lakes Fire Department issues a publicly available financial report that includes financial statements and required supplementary information for the plan. That report may be obtained by contacting the City's Fire Department.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 6 PENSION PLANS (CONTINUED)**

C. Pequot Lakes Fire Department Relief Association (Continued)

Funding Policy

*Minnesota Statutes* specify minimum contributions that may be required from the City on an annual basis. These minimum contributions are determined based on the amount required to meet the normal cost plus amortizing any prior year's service cost over a ten year period. A contribution was not required from the City for the year ended December 31, 2012. The Pequot Lakes Fire Department Relief Association also receives funding from the State of Minnesota as a two percent fire premium tax. The City receives the contributions and is required by statute to pass this through as payment to the Fire Relief Association. Investment earnings also add to the resources available for benefits.

Annual Pension Cost and Net Pension Obligation

The City's annual pension cost and net pension obligation to PERS for the current year were as follows:

Annual Required Contribution	\$ -
Interest on Net Pension Obligation	-
Adjustment to Annual Required Contribution	35,012
Annual Pension Cost	<u>35,012</u>
Less Contribution Made	<u>(35,012)</u>
Increase (Decrease) in Net Pension Obligation	-
Net Pension Obligation - Beginning of Year	-
Net Pension Obligation - End of Year	<u><u>\$ -</u></u>

The annual required contribution for the current year was determined as part of December 31, 2011, actuarial valuation using the entry age actuarial cost method. The actuarial assumptions included (a) 5% investment rate of return and (b) age and service retirement was assumed to occur at age 50. Pension benefit obligations on an actuarial basis are not calculated for individual volunteer fire relief associations since state statutes permit alternate calculation of required reserves based on overall actuarial assumptions.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 6 PENSION PLANS (CONTINUED)**

C. Pequot Lakes Fire Department Relief Association (Continued)

The City's net pension obligation for the Fire Relief Association (Association) for the years ended December 31, 2012, 2011, and 2010 are as follows:

<u>December 31,</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
2012	\$ 35,012	100.0 %	N/A
2011	35,500	100.0	N/A
2010	53,671	100.0	N/A

Contributions Required and Made

The City makes contributions to the Association annually in an amount equal to the fire aid received from the State of Minnesota as required by state statutes. The City is required to make additional contributions to the Association in the following year if the following years anticipated administrative expenses plus the anticipated increase in the required reserves plus amortization of the original unfunded accrued liability exceeds the anticipated revenues. The City was required to make a contribution in excess of fire aid for 2010 in the amount of \$14,384, of which was paid for through contracts from the surrounding areas for fire protection, and none for 2012 or 2011.

Funding Progress

As of December 31, 2011 (the most recent available information), the plan was overfunded by \$149,992. Additional information on the funding progress is included in the required supplementary information section of this report.

Related-Party Investments

As of December 31, 2011 (the most recent information available) and for the year then ended, the Association held no securities issued by the City or other related-parties.

D. OPEB Disclosure

The City provides health insurance benefits for certain retired employees under a single-employer fully-insured plan. The City provides benefits for retirees as required by *Minnesota Statutes* §471.61 subdivision 2b. Active employees who retire from the City when eligible to receive a retirement benefit from the Public Employees Retirement Association (PERA) of Minnesota (or similar plan) and do not participate in any other health benefits program providing coverage similar to that herein described, will be eligible to continue coverage with respect to both themselves and their eligible dependent(s) under the City's health benefits program. Pursuant to the provisions of the plan, retirees are required to pay varying percentages of the total premium cost. As of January 1, 2012, no retirees were receiving health benefits from the City's health plan.

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 6 PENSION PLANS (CONTINUED)**

D. OPEB Disclosure

**1. Annual OPEB Cost and Net OPEB Obligation**

The City's annual other post employment benefit (OPEB) cost is calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of fund 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 30 years. The following table shows the components of the City's annual OPEB cost for 2012, the amount actually contributed to the plan, and changes in the City's net OPEB obligation:

Annual Required Contribution	\$ 20,673
Interest on Net OPEB Obligation	4,199
Adjustment to ARC	<u>(5,698)</u>
Annual OPEB Cost	19,174
Contributions During the Year	<u>-</u>
Increase in Net OPEB Obligation	19,174
Net OPEB - Beginning of Year	<u>93,302</u>
Net OPEB - End of Year	<u><u>\$ 112,476</u></u>
Governmental Activities	\$ 99,537
Business-Type Activities	<u>12,939</u>
Total OPEB Payable	<u><u>\$ 112,476</u></u>

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 6 PENSION PLANS (CONTINUED)**

**D. OPEB Disclosure (Continued)**

**1. Annual OPEB Cost and Net OPEB Obligation (Continued)**

The City's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan and the net OPEB obligation for December 31, 2012 and 2011 were as follows:

Year Ended	Annual OPEB Cost	Employer Contribution	Percentage Contributed	Net OPEB Obligation
December 31, 2012	\$ 19,174	\$ 157	0.82 %	\$ 112,476
December 31, 2011	30,465	457	1.48	93,302
December 31, 2010	31,099	321	1.02	62,837

**2. Funding Status and Funding Progress**

The City currently has no assets that have been deposited into an irrevocable trust for future health benefits. Therefore, the actuarial value of assets is zero. No separate stand-alone financial report is issued for this plan.

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (b)	Unfunded Actuarial Accrued Liability (b-a)	Funded Ratio - (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
1/1/2012	\$ -	\$ 105,338	\$ 105,338	- %	\$ 580,558	18.1 %

The schedule of funding progress, presented as required supplementary information following the notes to the basic financial statements presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

**3. Actuarial Methods and Assumptions**

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of the occurrence of events far into the future. Examples include assumptions about future employment, mortality, and healthcare cost trends. 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.

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

**CITY OF PEQUOT LAKES, MINNESOTA  
NOTES TO THE FINANCIAL STATEMENTS  
DECEMBER 31, 2012**

**NOTE 6 PENSION PLANS (CONTINUED)**

D. OPEB Disclosure (Continued)

**3. Actuarial Methods and Assumptions (Continued)**

In the January 1, 2012 actuarial valuation, the entry age normal actuarial cost method was used. The actuarial assumptions included a 4.50% discount rate, which is based on the estimated long-term investment yield on the general assets of the City using an underlying long-term inflation assumption of 2.50%. The annual healthcare cost trend rate is 8.00% initially, reduced incrementally to an ultimate rate of 5.00% after six years. The unfunded actuarial accrued liability is being amortized as a level dollar amount over a closed 30-year period.

**NOTE 6 RELATED-ORGANIZATION**

The Pequot Lakes Fire Relief Association (Association) is excluded from the financial reporting entity because the City's financial accountability does not extend beyond making appointments. The purpose of the Association is to provide lump-sum retirement benefits for City firefighters. The City has no significant influence over the management, budget, or policies of the association. Audited financial statements are available from the Association.

**REQUIRED SUPPLEMENTARY INFORMATION OTHER THAN MD&A**

**CITY OF PEQUOT LAKES, MINNESOTA  
BUDGETARY COMPARISON SCHEDULE  
GENERAL FUND  
YEAR ENDED DECEMBER 31, 2012**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
<b>REVENUES</b>				
Taxes	\$ 1,450,551	\$ 1,450,551	\$ 1,478,068	\$ 27,517
Special Assessments	200	200	449	249
Licenses and Permits	13,350	13,350	15,893	2,543
Intergovernmental	58,750	58,750	113,249	54,499
Charges for Services	120,020	120,020	117,537	(2,483)
Fines and Forfeits	29,000	29,000	21,892	(7,108)
Gifts and Contributions	11,400	11,400	36,871	25,471
Investment Earnings	12,000	12,000	9,401	(2,599)
Miscellaneous	2,800	2,800	30,674	27,874
Total Revenues	1,698,071	1,698,071	1,824,034	125,963
<b>EXPENDITURES</b>				
<b>CURRENT</b>				
<b>GENERAL GOVERNMENT</b>				
Council	31,630	31,630	29,364	2,266
Clerk	198,580	198,580	190,591	7,989
Planning and Zoning	90,780	90,780	83,084	7,696
Buildings and Plant	33,250	33,250	36,285	(3,035)
Other General Government	67,930	67,930	82,372	(14,442)
Total General Government	422,170	422,170	421,696	474
<b>PUBLIC SAFETY</b>				
Police	551,400	551,400	579,177	(27,777)
Fire	77,400	77,400	71,290	6,110
Civil Defense	1,180	1,180	432	748
Total Public Safety	629,980	629,980	650,899	(20,919)
<b>HIGHWAYS AND STREETS</b>				
Public Works	242,395	242,395	284,973	(42,578)
Street Lighting	14,400	14,400	14,613	(213)
Traffic Signs and Signals	6,050	6,050	5,762	288
Total Highways and Streets	262,845	262,845	305,348	(42,503)
<b>SANITATION</b>				
Recycling	18,000	18,000	11,797	6,203
<b>CULTURE AND RECREATION</b>				
Parks	19,300	19,300	18,565	735
Regional Library	8,900	8,900	10,908	(2,008)
Total Culture and Recreation	28,200	28,200	29,473	(1,273)

The Notes to the Required Supplementary Information are an Integral Part of this Schedule.

**CITY OF PEQUOT LAKES, MINNESOTA  
BUDGETARY COMPARISON SCHEDULE  
GENERAL FUND (CONTINUED)  
YEAR ENDED DECEMBER 31, 2012**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
<b>EXPENDITURES (CONTINUED)</b>				
<b>CURRENT (CONTINUED)</b>				
<b>ECONOMIC DEVELOPMENT</b>				
Housing and Redevelopment Authority	\$ 32,126	\$ 32,126	\$ 32,908	\$ (782)
<b>CAPITAL OUTLAY</b>				
General Government	-	-	18,021	(18,021)
Public Safety	25,000	25,000	19,946	5,054
Highways and Streets	247,000	247,000	308,745	(61,745)
Culture and Recreation	1,000	1,000	-	1,000
Total Capital Outlay	273,000	273,000	346,712	(73,712)
<b>DEBT SERVICE</b>				
Principal Retirement	25,330	25,330	19,325	6,005
Interest	13,120	13,120	13,111	9
Total Debt Service	38,450	38,450	32,436	6,014
Total Expenditures	1,704,771	1,704,771	1,831,269	(126,498)
<b>NET CHANGE IN FUND BALANCE</b>	<b>\$ (6,700)</b>	<b>\$ (6,700)</b>	<b>(7,235)</b>	<b>\$ (535)</b>
Fund Balance - Beginning of Year			1,311,622	
<b>FUND BALANCE - END OF YEAR</b>			<b>\$ 1,304,387</b>	

The Notes to the Required Supplementary Information are an Integral Part of this Schedule.

**CITY OF PEQUOT LAKES, MINNESOTA  
BUDGETARY COMPARISON SCHEDULE  
FIRE DEPARTMENT SPECIAL REVENUE FUND  
YEAR ENDED DECEMBER 31, 2012**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
<b>REVENUES</b>				
Licenses and Permits	\$ -	\$ -	\$ 250	\$ 250
Intergovernmental	-	-	36,552	36,552
Charges for Services	175,500	175,500	163,214	(12,286)
Gifts and Contributions	-	-	1,200	1,200
Investments Earnings	1,400	1,400	978	(422)
Miscellaneous	5,800	5,800	5,969	169
Total Revenues	<u>182,700</u>	<u>182,700</u>	<u>208,163</u>	<u>25,463</u>
<b>EXPENDITURES</b>				
<b>CURRENT</b>				
Public Safety				
Fire	131,130	131,130	158,163	(27,033)
<b>CAPITAL OUTLAY</b>				
Public Safety	28,000	28,000	27,157	843
<b>DEBT SERVICE</b>				
Principal Retirement	17,440	17,440	35,617	(18,177)
Interest	1,330	1,330	1,251	79
Total Debt Service	<u>18,770</u>	<u>18,770</u>	<u>36,868</u>	<u>(18,098)</u>
Total Expenditures	<u>177,900</u>	<u>177,900</u>	<u>222,188</u>	<u>(44,288)</u>
<b>NET CHANGE IN FUND BALANCE</b>	<u>\$ 4,800</u>	<u>\$ 4,800</u>	<u>(14,025)</u>	<u>\$ (18,825)</u>
Fund Balance - Beginning of Year			<u>131,336</u>	
<b>FUND BALANCE - END OF YEAR</b>			<u>\$ 117,311</u>	

The Notes to the Required Supplementary Information are an Integral Part of this Schedule.

**CITY OF PEQUOT LAKES, MINNESOTA**  
**NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION**  
**DECEMBER 31, 2012**

**I. BUDGETARY INFORMATION**

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

- a. Prior to September 1, the City Clerk-Treasurer submits to the City Council a proposed operating budget for the fiscal year commencing the following January 1. The operating budget includes proposed expenditures and the means of financing them. The City Council adopts the proposed budget as amended and adjusted by the Council and certifies the proposed property tax levy to the County Auditor according to *Minnesota Statutes*.
- b. Public hearings are conducted in the Council's chambers.
- c. On or before December 28, the final budget is legally enacted by Council resolution and the final property tax levy certified to the County Auditor.
- d. Management is authorized to transfer budgeted amounts between departments within any fund; however, any revisions that alter the total expenditures of any fund must be approved by the City Council. Reported budget amounts are as originally adopted or amended by the City Council.
- e. The City has legally adopted budgets for the general fund, and the fire fund special revenue funds. Expenditures may not legally exceed budgeted appropriations at the total fund level. Monitoring of budgets is maintained at the expenditure category level (i.e., personal services, supplies, charges for services, and capital outlay) within each program. All amounts over budget have been approved by the City Council through the disbursement process.
- f. Budgets for the general, and certain special revenue funds are adopted on a basis consistent with generally accepted accounting principles (GAAP). Budgeted amounts are as originally adopted, or as amended by the city council. All annual appropriations lapse at fiscal year-end.

**II. EXPENDITURES IN EXCESS OF BUDGET**

The General Fund expenditures exceeded appropriations by \$126,498. However, total revenues also exceeded budgeted amounts by \$125,963. The overage was mainly caused from an increase in capital outlay expenditures related to highways and streets.

The Fire Department special revenue fund expenditures exceeded appropriations by \$44,288. However total revenues also exceeded budgeted amounts by \$25,463. The overage was mainly caused from the receipt and payment of fire state aid which is not budgeted.

**CITY OF PEQUOT LAKES, MINNESOTA  
SCHEDULE OF FUNDING PROGRESS  
PEQUOT LAKES FIREMAN'S RELIEF ASSOCIATION  
DECEMBER 31, 2012**

Fiscal Year Ending	Value of Assets (a)	Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Benefit Per Year of Service
12/31/2011	\$ 1,030,654	\$ 880,662	\$ (149,992)	117.0 %	\$ 2,900
12/31/2010	949,834	817,762	(132,072)	116.2	2,900
12/31/2009	831,439	773,518	(57,921)	107.5	2,900
12/31/2008	734,308	725,088	(9,220)	101.3	2,900
12/31/2007	747,773	661,774	(85,999)	113.0	2,500

Additional information relating to the pension plan is provided in Note 6C.

The December 31, 2012 report is not yet available.

**CITY OF PEQUOT LAKES, MINNESOTA  
 SCHEDULE OF FUNDING PROGRESS  
 OTHER POSTEMPLOYMENT HEALTH CARE BENEFITS  
 DECEMBER 31, 2012**

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (b)	Unfunded Actuarial Accrued Liability (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
1/1/2012	\$ -	\$ 105,338	\$ 105,338	- %	\$ 580,558	18.1 %
1/1/2009	-	118,698	118,698	-	616,864	19.2

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## **SUPPLEMENTARY INFORMATION**

**CITY OF PEQUOT LAKES, MINNESOTA  
 COMBINING BALANCE SHEET  
 NONMAJOR GOVERNMENTAL FUNDS  
 DECEMBER 31, 2012**

	Cemetery Perpetual Care	TIF 1-7 Babinsky	TIF 1-9 Lime Greenery
<b>ASSETS</b>			
Cash and Pooled Investments	\$ 27,335	\$ 31,306	\$ 7,629
Accounts Receivable	-	-	-
Taxes Receivable			
Current	-	-	-
Total Assets	\$ 27,335	\$ 31,306	\$ 7,629
 <b>LIABILITIES AND FUND BALANCES</b>			
<b>LIABILITIES</b>			
Accounts Payable	\$ -	\$ 15,310	\$ 6,109
Interfund Payable	-	-	-
Deferred Revenue - Unavailable	-	-	-
Total Liabilities	-	15,310	6,109
 <b>FUND BALANCES</b>			
Restricted for Economic Development	-	15,996	1,520
Restricted for Debt Repayment	-	-	-
Committed for Cemetery Perpetual Care	27,335	-	-
Committed for Highway 371 Project	-	-	-
Unassigned	-	-	-
Total Fund Balances (Deficits)	27,335	15,996	1,520
 Total Liabilities and Fund Balances	 \$ 27,335	 \$ 31,306	 \$ 7,629

TIF 1-13 Lonesome Cottage	Highway 371 Project	Total Nonmajor Special Revenue Funds	2010 Equipment Certificates	Total Nonmajor Governmental Funds
\$ - 15,850	\$ 229,988 -	\$ 296,258 15,850	\$ 31,218 -	\$ 327,476 15,850
-	210	210	1,005	1,215
<u>\$ 15,850</u>	<u>\$ 230,198</u>	<u>\$ 312,318</u>	<u>\$ 32,223</u>	<u>\$ 344,541</u>
\$ 11,719 48,919 15,850 76,488	\$ - - - -	\$ 33,138 48,919 15,850 97,907	\$ - - - -	\$ 33,138 48,919 15,850 97,907
- - - -	- - - 230,198	17,516 - 27,335 230,198	- 32,223 - -	17,516 32,223 27,335 230,198
(60,638) (60,638)	- 230,198	(60,638) 214,411	- 32,223	(60,638) 246,634
<u>\$ 15,850</u>	<u>\$ 230,198</u>	<u>\$ 312,318</u>	<u>\$ 32,223</u>	<u>\$ 344,541</u>

**CITY OF PEQUOT LAKES, MINNESOTA  
 COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES  
 NONMAJOR GOVERNMENTAL FUNDS  
 YEAR ENDED DECEMBER 31, 2012**

	Cemetery Perpetual Care	TIF 1-7 Babinsky	TIF 1-9 Lime Greenery
<b>REVENUES</b>			
Taxes	\$ -	\$ 33,187	\$ 6,787
Interest on Investments	197	126	20
Miscellaneous	11	-	-
Total Revenues	208	33,313	6,807
<b>EXPENDITURES</b>			
<b>CURRENT</b>			
General Government	465	-	-
Economic Development	-	32,346	7,401
<b>DEBT SERVICE</b>			
Principal	-	-	-
Interest	-	-	-
Total Expenditures	465	32,346	7,401
<b>NET CHANGE IN FUND BALANCES</b>	(257)	967	(594)
Fund Balance - Beginning of Year	27,592	15,029	2,114
<b>FUND BALANCE - END OF YEAR</b>	<u>\$ 27,335</u>	<u>\$ 15,996</u>	<u>\$ 1,520</u>

TIF 1-13 Lonesome Cottage	Highway 371 Project	Total Nonmajor Special Revenue Funds	2010 Equipment Certificates	Total Nonmajor Governmental Funds
\$ 26,052	\$ 10,630	\$ 76,656	\$ 28,906	\$ 105,562
-	1,589	1,932	91	2,023
-	-	11	11	22
26,052	12,219	78,599	29,008	107,607
-	-	465	-	465
24,070	-	63,817	-	63,817
-	-	-	24,000	24,000
-	-	-	4,500	4,500
24,070	-	64,282	28,500	92,782
1,982	12,219	14,317	508	14,825
(62,620)	217,979	200,094	31,715	231,809
\$ (60,638)	\$ 230,198	\$ 214,411	\$ 32,223	\$ 246,634

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**REPORTS RELATED TO *GOVERNMENT AUDITING STANDARDS***



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**INDEPENDENT AUDITORS' 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 Mayor and  
Members of the City Council  
City of Pequot Lakes  
Pequot Lakes, Minnesota

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Pequot Lakes (City), Minnesota as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the City of Pequot Lakes' basic financial statements and have issued our report thereon dated April 2, 2013.

**Internal Control Over Financial Reporting**

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying Schedule of Findings and Recommendations, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider deficiencies 2006-01 and 2006-02 described in the accompanying Schedule of Findings and Recommendations to be material weaknesses.

A *significant deficiency* is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider deficiency 2006-03 as described in the accompanying Schedule of Findings and Recommendations to be a significant deficiency.

Honorable Mayor and  
Members of the City Council  
City of Pequot Lakes

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and 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 test disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

### **City of Pequot Lakes' Response to Findings**

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

### **Purpose of this Report**

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



**CliftonLarsonAllen LLP**

Brainerd, Minnesota  
April 2, 2013

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**CITY OF PEQUOT LAKES, MINNESOTA  
SCHEDULE OF FINDINGS AND RECOMMENDATIONS  
YEAR ENDED DECEMBER 31, 2012**

**MATERIAL WEAKNESSES (FINANCIAL REPORTING)**

**2006-01 FINANCIAL STATEMENT PRESENTATION**

**Criteria:** The City of Pequot Lakes' (the City) management is responsible for establishing and maintaining internal controls, including monitoring, and for the fair presentation in the financial statements in accordance with Governmental Accounting Standards Board Statement No. 34.

**Condition:** As part of the audit, management requested us to prepare a draft of your financial statements, including the related notes to the financial statements.

**Cause:** The City has a limited number of personnel with financial reporting experience.

**Effect:** The design of the controls over the financial reporting process would affect the ability of the City to report its financial data consistently with the assertions of the management in the financial statements.

**Recommendation:** We recommend that the City be aware of the requirements for fair presentation of the financial statements in accordance with the Governmental Accounting Standards Board Statement No. 34. Should the City elect, based upon an analysis of costs and benefits, to establish the full oversight of the financial statement preparation of an appropriate level, we suggest management establish effective review policies and procedures including but not limited to the following functions: reconciling general ledger amounts to the draft financial statements; review of all supporting documentation and explanations for journal entries proposed by us; complete the disclosure checklist; review and approval of schedules and calculations supporting the amounts included in the notes to the financial statements; apply analytic procedures to the draft financial statements; and perform other procedures considered necessary by management.

**CLIENT'S RESPONSE:**

*The City understands that this is required communications for the preparation of the financial statements.*

**CITY OF PEQUOT LAKES, MINNESOTA  
SCHEDULE OF FINDINGS AND RECOMMENDATIONS (CONTINUED)  
YEAR ENDED DECEMBER 31, 2012**

**MATERIAL WEAKNESSES (FINANCIAL REPORTING) (CONTINUED)**

**2006-02 AUDIT ADJUSTMENTS**

**Criteria:** The City of Pequot Lakes' management is responsible for establishing and maintaining internal controls for the proper recording of all the City's accounting transactions, including account coding, reporting of accruals and net assets, and cash flows.

**Condition:** As part of the audit, we proposed material adjustments for recording of receivables, recording of some capital assets, reclassifying transactions to the proper accounts and preparing note disclosures.

**Cause:** The City has a limited number of personnel with financial reporting experience.

**Effect:** The design of the internal controls over recording transactions and year-end accruals limits the ability of the City to provide accurate accrual basis financial information.

**Recommendation:** We recommend City management be constantly aware of all procedures and processes involved in recording transactions, accruals, and reclassifications and develop internal control policies to ensure proper recording of these items.

**CLIENT'S RESPONSE:**

*The City will continue to work at eliminating the need for audit adjustments.*

**SIGNIFICANT DEFICIENCY**

**2006-03 SEGREGATION OF DUTIES**

**Criteria:** City management should constantly be aware of the need to have adequate segregation of duties regarding the processing of transactions for the City. In addition, City management should be aware that the concentration of duties and responsibilities in one or a very few individuals is not desirable from an internal control perspective.

**Condition:** Adequate segregation of the accounting functions necessary to ensure adequate internal accounting control, is not in place. The City has reassigned a number of the previously identified responsibilities, however due to the number of employees available to assign responsibilities, some weaknesses still exist.

**Cause:** The City has a limited number of personnel.

**Effect:** The design of the internal controls over financial reporting could affect the ability of the City to record, process, summarize and report financial data consistently with the assertions of management in the financial statements. In addition, this lack of segregation of duties may result in the City's inability to prevent/detect misappropriation of assets.

**Recommendation:** We recommend City management be aware of the lack of segregation of duties within the accounting functions and provide oversight to ensure the internal control policies and procedures are being implemented by City staff.

**CLIENT'S RESPONSE:**

*The City will review the accounting functions and segregate them if it is possible with limited staff.*

**CITY OF PEQUOT LAKES, MINNESOTA  
SCHEDULE OF FINDINGS AND RECOMMENDATIONS (CONTINUED)  
YEAR ENDED DECEMBER 31, 2012**

**OTHER ITEM FOR CONSIDERATION – MINNESOTA LEGAL COMPLIANCE**

None Noted.

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## INDEPENDENT AUDITORS' REPORT ON MINNESOTA LEGAL COMPLIANCE

Honorable Mayor and  
Members of the City Council  
City of Pequot Lakes  
Pequot Lakes, Minnesota

We have audited, in accordance with auditing standards generally accepted in the United States of America, the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Pequot Lakes (the City), Minnesota, as of December 31, 2012, and the related notes to the financial statements, which collectively comprise the entity's basic financial statements as listed in the table of contents and have issued our report thereon dated April 2, 2013.

The *Minnesota Legal Compliance Audit Guide for Political Subdivisions* covers seven categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, miscellaneous provisions, and tax increment financing.

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

The purpose of this report is solely to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on compliance. Accordingly, this communication is not suitable for any other purpose.

*CliftonLarsonAllen LLP*

**CliftonLarsonAllen LLP**

Brainerd, Minnesota  
April 2, 2013



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