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Certified Public Accountants & Consultants

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Herman A Bertuleit, CPA

CITY OF HARRISVILLE  
WATER AND SEWER FUNDS  
ALCONA COUNTY, MICHIGAN

AUDITORS' REPORT  
YEAR ENDED DECEMBER 31, 2007

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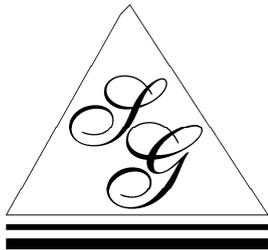
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February 21, 2008

Independent Auditors' Report

Members of the City Council  
City of Harrisville  
Alcona County, Michigan

We have audited the accompanying financial statements of the business -type activities of the Water and Sewer Funds of the City of Harrisville, Alcona County, Michigan, as of and for the year ended December 31, 2007, which collectively comprise the City of Harrisville Water and Sewer Funds' basic financial statements, as listed in the index. These financial statements are the responsibility of the City's management. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 1, the financial statements present only the City of Harrisville Water and Sewer Funds and do not purport to, and do not present fairly the financial position of the City of Harrisville, Alcona County, Michigan, as of December 31, 2007, and the changes in its financial position and cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the business -type activities of the City of Harrisville Water and Sewer Funds, Alcona County, Michigan, as of December 31, 2007, and the respective changes in financial position and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 21, 2008, on our consideration of the City of Harrisville Water and Sewer Funds' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis information is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

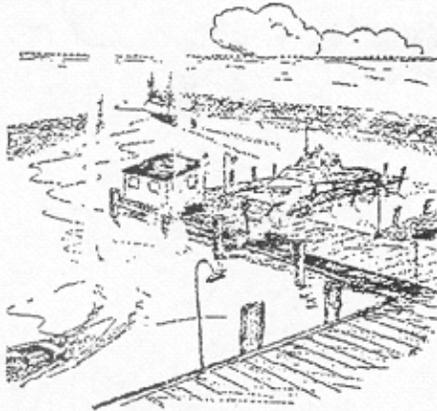
Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Harrisville Water and Sewer Funds' basic financial statements. The supplemental information for Farmers Home Administration is presented for purposes of additional analysis and is not a required part of the basic financial statements. The supplemental information for Farmers Home Administration has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

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Harbor of Refuge - Dedicated August 6, 1961

**City of Harrisville**  
**Office of the Clerk**  
P.O. Box 278  
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**MANAGEMENT'S DISCUSSION AND ANALYSIS**

As management of the Water and Sewer Funds of the City of Harrisville (the Water and Sewer Funds), we offer readers of the Water and Sewer Funds' financial statements this narrative overview and analysis of the financial activities of the Water and Sewer Funds for the fiscal year ended December 31, 2007.

**Financial Highlights**

- The Water and Sewer Funds' assets exceeded its liabilities by \$1,373,971 (*net assets*) for the fiscal year reported. Of this amount, \$736,192 (*unrestricted net assets*) represents the portion available for spending.
- The Water and Sewer Funds' total net assets increased by \$56,752 or 4.3% over the course of the year's operations.

**Overview of the Financial Statements**

This annual report includes this management's discussion and analysis report, the independent auditors' report and the basic financial statements of the Water and Sewer Funds. The basic financial statements include notes that explain, in more detail, some of the information in the financial statements.

**Required Financial Statements**

The financial statements of the Water and Sewer Funds report information using accounting methods similar to those used by private sector companies. These statements offer short and long-term financial information about its activities. The Statement of Net Assets includes all of the Water and Sewer Funds' assets and liabilities and provides information about the nature and amounts of investments in resources (assets) and the obligations to City creditors (liabilities). The Statement of Net Assets also provides the basis for evaluating the capital structure and assessing the liquidity and financial flexibility of these funds.

All of the current year's revenues and expenses are accounted for in the Statement of Revenue, Expenses and Changes in Net Assets. This statement measures the success of the Water and Sewer Funds' operations over the past year and can be used to determine whether the Water and Sewer Funds have successfully recovered all its costs through its user fees and other charges, profitability and credit worthiness.

The final required financial statement is the Statement of Cash Flows. This statement reports cash receipts, cash payments, and net changes in cash resulting from operating, financing and investing activities. It provides answers to such questions as where did cash come from, what was cash used for, and what was the change in the cash balance during the reporting period.

## Notes to Financial Statements

The accompanying notes to financial statements provide information essential to a full understanding of the financial statements. The notes to financial statements are presented in Exhibit D of this report.

### Analysis of Financial Position:

One of the most important questions asked about the Water and Sewer Funds' finances is "Are the Water and Sewer Funds as a whole better off or worse off as a result of this year's activities?" The Statement of Net Assets and the Statement of Revenue, Expenses, and Changes in Net Assets report information about the Water and Sewer Funds' activities in a way that will help answer this question. These two statements report the net assets of the Water and Sewer Funds and the changes in them. One can think of the Water and Sewer Funds' net assets (the difference between assets and liabilities) as one way to measure financial health or financial position. Over time, increases or decreases in the Water and Sewer Funds' net assets are one indicator of whether its financial health is improving or deteriorating. However, one will need to consider other non-financial factors such as changes in economic conditions and new or changed government legislation.

### Summary of Net Assets:

The following summarizes the net assets of the Water and Sewer Funds of the City of Harrisville at December 31, 2007 and 2006:

	Net Assets Summary			
	<u>Water Fund</u>	<u>Sewer Fund</u>	<u>December 31, 2007</u>	<u>December 31, 2006</u>
Current Assets	\$ 535,664	\$ 200,690	\$ 736,354	\$ 653,421
Restricted Assets	0	30,000	30,000	30,000
Capital Assets - net	<u>864,534</u>	<u>389,195</u>	<u>1,253,729</u>	<u>1,316,755</u>
Total Assets	<u>1,400,198</u>	<u>619,885</u>	<u>2,020,083</u>	<u>2,000,176</u>
Current Liabilities	23,950	162	24,112	28,957
Long-Term Liabilities	<u>466,000</u>	<u>156,000</u>	<u>622,000</u>	<u>654,000</u>
Total Liabilities	<u>489,950</u>	<u>156,162</u>	<u>646,112</u>	<u>682,957</u>
Net Assets				
Investment in Capital Assets, Net of Related Debt	374,584	233,195	607,779	638,505
Restricted for Debt Service	0	30,000	30,000	30,000
Unrestricted	<u>535,664</u>	<u>200,528</u>	<u>736,192</u>	<u>648,714</u>
Total Net Assets	<u>\$ 910,248</u>	<u>\$ 463,723</u>	<u>\$ 1,373,971</u>	<u>\$ 1,317,219</u>

### Capital Asset and Debt Administration

#### Capital Assets

The Water and Sewer Funds' investment in capital assets as of December 31, 2007, amounted to \$1,253,729 (net of accumulated depreciation). This investment in capital assets includes land, distribution and collection systems, and machinery and equipment. Capital assets for the Water and Sewer Funds decreased by \$63,026 as a result of current year depreciation and the addition of a new well pump. Accumulated depreciation as of December 31, 2007 was \$1,545,415.

**Capital Assets Summary**  
(Net of depreciation)

	<u>December 31, 2007</u>	<u>December 31, 2006</u>
Land	\$ 18,000	\$ 18,000
Distribution and collection systems	2,716,812	2,716,812
Machinery and equipment	64,332	59,161
Subtotal	2,799,144	2,793,973
Less accumulated depreciation	1,545,415	1,477,218
 Capital Assets - Net	 \$ 1,253,729	 \$ 1,316,755

Additional information on capital assets can be found in Note 3 of the audit, notes to financial statements .

**Long-Term Debt**

At year end, long-term debt (due in more than one year) amounted to \$622,000. Such debt includes *Bonds and Contracts Payable*.

**Summary of Revenues and Expenses:**

The following summarizes the revenues and expenses of the Water and Sewer Funds of the City of Harrisville at December 31, 2007 and 2006:

	<u>Water Fund</u>	<u>Sewer Fund</u>	<u>December 31, 2007</u>	<u>December 31, 2005</u>
Operating revenue	\$ 77,553	\$ 98,821	\$ 176,374	\$ 182,480
Non operating revenue	64,215	6,491	70,706	60,821
Total revenues	141,768	105,312	247,080	243,301
 Depreciation expense	34,298	33,899	68,197	67,421
Other operating expense	49,480	39,651	89,131	104,636
Nonoperating expense	24,200	8,800	33,000	34,525
Total expenses	107,978	82,350	190,328	206,582
 Change in Net Assets	33,790	22,962	56,752	36,719
 Beginning Net Assets	876,458	440,761	1,317,219	1,280,500
 Ending Net Assets	\$ 910,248	\$ 463,723	\$ 1,373,971	\$ 1,317,219

**Economic Factors and Next Year's Budget and Rates**

The management of the Water and Sewer Funds considered many factors in setting the fiscal year 2008 budget, user fees and charges. As always, the overriding factor was to keep expenses at or below the amount of revenue. The majority of revenue generated by the Water and Sewer Funds are derived from charges for water and sewer services. Water and sewer rates did not change in 2007.

The most significant expenses remain employee related costs, operating supplies and system repairs and depreciation .

### **Requests for Information**

**This financial report is designed to provide a general overview of the Water and Sewer Funds of the City of Harrisville for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the City Mayor, P.O. Box 278, Harrisville, Michigan 48740.**

CITY OF HARRISVILLE  
 WATER AND SEWER FUNDS  
Alcona County, Michigan

STATEMENT OF NET ASSETS  
 PROPRIETARY FUNDS  
December 31, 2007

	Business-Type Activities Enterprise Funds		
	Water Fund	Sewer Fund	Total
<u>Assets</u>			
Current assets:			
Cash and cash equivalents (Note 2)	\$ 313,324	\$ 174,021	\$ 487,345
Investments (Note 2)	201,765	0	201,765
Accounts receivable	20,413	26,669	47,082
Due from other funds	162	0	162
Total current assets	<u>535,664</u>	<u>200,690</u>	<u>736,354</u>
Restricted assets:			
Investments (Note 2)	<u>0</u>	<u>30,000</u>	<u>30,000</u>
Noncurrent assets:			
Capital assets, net (Note 3)	<u>864,534</u>	<u>389,195</u>	<u>1,253,729</u>
Total Assets	<u>1,400,198</u>	<u>619,885</u>	<u>2,020,083</u>
<u>Liabilities</u>			
Current liabilities:			
Accrued interest	11,950	0	11,950
Due to other funds	0	162	162
Bond payable (Note 4)	12,000	0	12,000
Total current liabilities	<u>23,950</u>	<u>162</u>	<u>24,112</u>
Long-term liabilities:			
Bond payable (Note 4)	466,000	0	466,000
Contract payable (Note 4)	0	156,000	156,000
Total long-term liabilities	<u>466,000</u>	<u>156,000</u>	<u>622,000</u>
Total Liabilities	<u>489,950</u>	<u>156,162</u>	<u>646,112</u>
<u>Net Assets</u>			
Investment in capital assets, net of related debt	374,584	233,195	607,779
Restricted for Debt Service	0	30,000	30,000
Unrestricted	<u>535,664</u>	<u>200,528</u>	<u>736,192</u>
Total Net Assets	<u>\$ 910,248</u>	<u>\$ 463,723</u>	<u>\$ 1,373,971</u>

The accompanying notes to financial statements are an integral part of this statement.

CITY OF HARRISVILLE  
WATER AND SEWER FUNDS  
Alcona County, Michigan

STATEMENT OF REVENUE, EXPENSES AND CHANGES IN NET ASSETS  
PROPRIETARY FUNDS  
For the Year Ended December 31, 2007

	Business-Type Activities Enterprise Funds		
	Water Fund	Sewer Fund	Total
<u>Operating Revenue</u>			
Charges for services	\$ 76,915	\$ 98,790	\$ 175,705
Service connection charges	560	0	560
Refunds	78	31	109
Total operating revenue	<u>77,553</u>	<u>98,821</u>	<u>176,374</u>
<u>Operating Expenses</u>			
Salaries and wages	13,482	13,482	26,964
Employee benefits	6,493	6,493	12,986
Office supplies	276	441	717
Operating supplies	4,833	4,054	8,887
Telephone	1,095	797	1,892
Insurance	2,119	611	2,730
Utilities	2,438	3,478	5,916
Repairs	1,173	2,504	3,677
Equipment rentals	3,681	4,090	7,771
Contracted services	11,283	3,151	14,434
State fees	1,056	0	1,056
Miscellaneous	1,551	550	2,101
Depreciation	34,298	33,899	68,197
Total operating expenses	<u>83,778</u>	<u>73,550</u>	<u>157,328</u>
Operating income (loss)	<u>(6,225)</u>	<u>25,271</u>	<u>19,046</u>
<u>Non-Operating Revenue (Expenses)</u>			
Property taxes	47,446	0	47,446
Interest on investments	16,769	6,491	23,260
Interest expense	(24,200)	(8,800)	(33,000)
Total non-operating revenue (expenses)	<u>40,015</u>	<u>(2,309)</u>	<u>37,706</u>
Change in net assets	33,790	22,962	56,752
Net assets - beginning of year	<u>876,458</u>	<u>440,761</u>	<u>1,317,219</u>
Net assets - end of year	<u>\$ 910,248</u>	<u>\$ 463,723</u>	<u>\$ 1,373,971</u>

The accompanying notes to financial statements are an integral part of this statement.

CITY OF HARRISVILLE  
WATER AND SEWER FUNDS  
Alcona County, Michigan

STATEMENT OF CASH FLOWS  
PROPRIETARY FUNDS  
For the Year Ended December 31, 2007

	Business-Type Activities Enterprise Funds		
	<u>Water Fund</u>	<u>Sewer Fund</u>	<u>Total</u>
<u>Cash Flows from Operating Activities</u>			
Cash received from customers	\$ 75,899	\$ 97,805	\$ 173,704
Cash paid to suppliers for goods and services	(34,050)	(19,676)	(53,726)
Cash paid to employees for services	(19,975)	(19,975)	(39,950)
Refunds received	78	31	109
Net cash provided by operating activities (Note 7)	<u>21,952</u>	<u>58,185</u>	<u>80,137</u>
<u>Cash Flows From Noncapital Financing Activities</u>			
Property taxes received	<u>47,446</u>	<u>0</u>	<u>47,446</u>
<u>Cash Flows From Capital and Related Financing Activities</u>			
Acquisition and construction of capital assets	(5,171)	0	(5,171)
Principal paid on contract payable	0	(20,000)	(20,000)
Principal paid on bond payable	(12,000)	0	(12,000)
Interest paid on contract and bond payable	(24,500)	(8,800)	(33,300)
Net cash used by capital and related financing activities	<u>(41,671)</u>	<u>(28,800)</u>	<u>(70,471)</u>
<u>Cash Flows From Investing Activities</u>			
Purchase of investments	(3,478)	(60,000)	(63,478)
Proceeds from matured investments	0	60,000	60,000
Interest on investments	7,500	6,491	13,991
Net cash provided by investing activities	<u>4,022</u>	<u>6,491</u>	<u>10,513</u>
Net increase in cash and cash equivalents (Note 1)	31,749	35,876	67,625
Cash and cash equivalents at beginning of year (Note 1)	<u>281,575</u>	<u>138,145</u>	<u>419,720</u>
Cash and cash equivalents at end of year (Note 1)	<u>\$ 313,324</u>	<u>\$ 174,021</u>	<u>\$ 487,345</u>

The accompanying notes to financial statements are an integral part of this statement.

CITY OF HARRISVILLE  
WATER AND SEWER FUNDS  
Alcona County, Michigan

NOTES TO FINANCIAL STATEMENTS  
For the Year Ended December 31, 2007

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the City of Harrisville Water and Sewer Funds conform to accounting principles generally accepted in the United States of America (GAAP) applicable to governmental units. The following is a summary of the significant accounting policies.

A. Description of City Operations and Fund Type

The City of Harrisville Water and Sewer Funds operate as enterprise funds and are governed by an elected council with a City Manager overseeing daily operations. The basic financial statements of the City of Harrisville Water and Sewer Funds have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental units. The Water and Sewer Funds apply all relevant Governmental Accounting Standards Board (GASB) and Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions, that apply to all proprietary fund type activities, issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements, in which case GASB prevails. All activities over which the Water and Sewer Funds exercise oversight responsibility have been included in the reporting entity.

Oversight responsibility is determined by factors such as financial interdependency, selection of governing authority, designation of management, ability to significantly influence operations, and accountability for fiscal matters of the entity.

B. Fund Accounting

The Water and Sewer Funds use funds to maintain their financial records during the year. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts.

**Proprietary Fund**

Proprietary fund reporting focuses on the determination of operating income, changes in net assets, financial position, and cash flows.

The City of Harrisville's Enterprise Funds, which consist of the Water and Sewer Funds, report operations that provide services which are financed primarily by user charges, or activities where periodic measurement of net income is appropriate for capital maintenance, public policy, management control or other purposes. The Water and Sewer Funds are both considered to be major funds.

C. Basis of Presentation

The Water and Sewer Funds' basic financial statements consist of a statement of net assets, a statement of revenue, expenses and changes in net assets, and a statement of cash flows. Government wide financial statements report information about the City of Harrisville Water and Sewer Funds as a whole. The Water and Sewer Funds have only one fund type which is business-type in nature, so the financial statements present one set of statements that meets both the government-wide and fund requirements.

A statement of net assets provides information about the assets, liabilities, and net assets of the Water and Sewer Funds at the end of the year. Assets and liabilities are classified as either current or noncurrent. Net assets are classified according to external donor restrictions or availability of assets to satisfy Water

CITY OF HARRISVILLE  
WATER AND SEWER FUNDS  
Alcona County, Michigan

NOTES TO FINANCIAL STATEMENTS  
For the Year Ended December 31, 2007

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Basis of Presentation (Continued)

and Sewer Fund obligations. Invested in capital assets represents the value of capital assets, net of accumulated depreciation. Unrestricted net assets include all other net assets, including those that have been designated by management to be used for other than general operation purposes.

A statement of revenue, expenses and changes in net assets provides information about the Water and Sewer Funds' financial activities during the year ended December 31, 2007. Revenue and expenses are classified as either operating or nonoperating, and all changes in net assets are reported, including capital contributions. Operating revenues and expenses generally result from providing water and sewer services. Other revenues, such as property taxes, are not generated from operations and are considered to be nonoperating revenues. Operating expenses include the cost of providing the services and depreciation on capital assets.

A statement of cash flows provides information about the Water and Sewer Funds' sources and uses of cash and cash equivalents during the year ended December 31, 2007. Increases and decreases in cash and cash equivalents are classified as either operating, noncapital financing, capital financing, or investing.

D. Measurement Focus and Basis of Accounting

The term measurement focus is used to denote what is being measured and reported in the Water and Sewer Funds' operating statements. The Water and Sewer Funds are accounted for on the flow of economic resources measurement focus. The fundamental objective of this focus is to measure whether the Water and Sewer Funds are better or worse off economically as a result of events and transactions of the period.

The term basis of accounting is used to determine when a transaction or event is recognized on the Water and Sewer Funds' operating statements. The Water and Sewer Funds use the full accrual basis of accounting. Under this basis, revenues are recorded when earned and expenses are recorded when incurred, even though actual payment or receipt may not occur until after the period ends.

E. Cash and Cash Equivalents

For presentation on the financial statements, investments in cash management pools and investments with an original maturity of three months or less at the time they are purchased by the Water and Sewer Funds are considered to be cash equivalents. Investments with an initial maturity of more than three months are reported as investments.

F. Receivables

Receivables at December 31, 2007, consist of accounts (fees). All receivables are net of estimated uncollectible accounts. Receivables are recognized to the extent the amounts are determined material and substantiated, not only by supporting documentation but also by a reasonable systematic method of determining their existence, completeness, valuation, and collectibility .

The balances consist primarily of charges for water and sewer services due from various customers .

CITY OF HARRISVILLE  
WATER AND SEWER FUNDS  
Alcona County, Michigan

NOTES TO FINANCIAL STATEMENTS  
For the Year Ended December 31, 2007

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

G. Capital Assets

Capital assets are defined by the City as assets with an initial cost of more than \$5,000 and an estimated useful life in excess of five years. 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. Provision for depreciation is provided with respect to plant and equipment of the Water and Sewer Funds. Depreciation is calculated using the straight line basis at rates ranging from 2% to 20% per year. The estimated useful lives are as follows:

Buildings and plant	30 - 50 years
Equipment	5 - 10 years

Expenditures for maintenance, repairs and renewals are charged to operations as incurred and betterments are capitalized. The Water and Sewer Funds eliminate the cost and related allowances from the accounts for assets sold or retired and resulting gains or losses therefrom are included in operations concurrently. Donated fixed assets are recorded at their fair market values as of the date received.

H. Use of Estimates

The process of preparing financial statements in conformity with accounting principles generally accepted in the United States of America requires the use of estimates and assumptions regarding certain types of assets, liabilities, revenues and expenses. Such estimates primarily relate to unsettled transactions and events as of the date of the financial statements. Accordingly, upon settlement, actual results may differ from estimated amounts.

I. Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowings used for the acquisition, construction or improvement of those assets. Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the Water and Sewer Funds or through external restrictions imposed by creditors, grantors or laws or regulations of other governments. The Water and Sewer Funds' policy is to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

J. Operating Revenues and Expenses

Operating revenues are those revenues that are generated directly from the primary activities of the enterprise funds. For the Water and Sewer Funds, these revenues are charges for services for water and sewer services. Operating expenses are the necessary costs incurred to provide the service that is the primary activity of the funds. Revenues and expenses not meeting these definitions are reported as nonoperating.

CITY OF HARRISVILLE  
WATER AND SEWER FUNDS  
Alcona County, Michigan

NOTES TO FINANCIAL STATEMENTS  
For the Year Ended December 31, 2007

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

K. Extraordinary and Special Items

Extraordinary items are transactions or events that are both unusual in nature and infrequent in occurrence. Special items are transactions or events that are within the control of the Council and that are either unusual in nature or infrequent in occurrence. Neither type of transaction occurred during the current year.

NOTE 2 - DEPOSITS AND INVESTMENTS

At year-end, the City of Harrisville Water and Sewer Funds' deposits and investments were reported in the basic financial statements in the following categories:

<u>Current Assets</u>	
Cash and Cash Equivalents	\$ 487,345
Investments	<u>201,765</u>
Total Current Assets	689,110
 <u>Restricted Assets</u>	
Investments	<u>30,000</u>
	<u>\$ 719,110</u>

The breakdown between deposits and investments is as follows:

Bank Deposits (checking and savings accounts, certificates of deposit)	\$ 232,173
Investment in financial institution pooled funds	<u>486,937</u>
Total	<u>\$ 719,110</u>

As of December 31, 2007, the City of Harrisville Water and Sewer Funds had the following investments.

<u>Investment Type</u>	<u>Fair Value</u>	<u>Specific Identification Maturities</u>
Investment pools	<u>\$ 486,937</u>	Daily

Credit Risk

State law authorizes investments in investment pools as authorized by the Surplus Funds Investment Pool Act, Act No. 367 of the Public Acts of 1982, being sections 129.111 to 129.118 of the Michigan Compiled Laws, composed entirely of instruments that are legal for direct investment by a local governmental unit in Michigan. The Water and Sewer Fund's investment pools are unrated.

CITY OF HARRISVILLE  
WATER AND SEWER FUNDS  
Alcona County, Michigan

NOTES TO FINANCIAL STATEMENTS  
For the Year Ended December 31, 2007

NOTE 2 - DEPOSITS AND INVESTMENTS (CONTINUED)

Custodial Credit Risk – Deposits

In the case of deposits, this is the risk that in the event of a bank failure, the Water and Sewer Funds' deposits may not be returned to it. As of December 31, 2007, \$16,711 of the Water and Sewer Funds' bank balance of \$232,173 was exposed to custodial credit risk because it was uninsured and uncollateralized.

Custodial Credit Risk – Investments

For an investment, this is the risk that, in the event of the failure of the counterparty, the Water and Sewer Funds will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The Water and Sewer Funds will minimize custodial credit risk, which is the risk of loss due to the failure of the security issuer or backer, by; limiting investments to the types of securities approved in the Water and Sewer Funds' investment policy which is in accordance with State law.

Concentration of Credit Risk, Interest Rate Risk and Foreign Currency Risk

The Water and Sewer Funds' investment policy does not address concentration of credit risk, interest rate risk or foreign currency risk.

Investments:

The City Council has adopted an investment policy in accordance with Act 196, PA 1997 which authorizes the Water and Sewer Funds to deposit and invest in the following:

- \* Accounts of federally insured banks, credit unions and savings and loan associations
- \* Bonds and other direct obligations of the United States or an agency or instrumentality of the United States
- \* United States government or federal agency obligation repurchase agreements
- \* Banker's acceptances of United States banks
- \* Commercial paper rated within the two highest classifications by not less than two standard rating services which mature not more than 270 days after the date of purchase
- \* Mutual funds registered under the Investment Company Act of 1940, Title I of Chapter 686, 54 Stat. 789 15 U.S.C. 80a-1 to 80a-3 and 80a-4 to 80a-64 with the authority to purchase only investment vehicles that are legal for direct investment by a public corporation

Michigan law requires that public funds may not be deposited in financial institutions that do not maintain an office in Michigan. The Water and Sewer Funds' deposits and investments are in accordance with statutory authority.

CITY OF HARRISVILLE  
WATER AND SEWER FUNDS  
Alcona County, Michigan

NOTES TO FINANCIAL STATEMENTS  
For the Year Ended December 31, 2007

NOTE 3 - CAPITAL ASSETS

Capital asset activity for the fiscal year ended December 31, 2007, was as follows:

	<u>Balance</u> <u>January 1, 2007</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance</u> <u>December 31, 2007</u>
Capital Assets Not Being Depreciated:				
Land	\$ 18,000	\$ 0	\$ 0	\$ 18,000
Capital Assets Being Depreciated:				
Distribution and Collection Systems	2,716,812	0	0	2,716,812
Machinery and equipment	<u>59,161</u>	<u>5,171</u>	<u>0</u>	<u>64,332</u>
	<u>2,775,973</u>	<u>5,171</u>	<u>0</u>	<u>2,781,144</u>
Less accumulated depreciation	<u>(1,477,218)</u>	<u>(68,197)</u>	<u>0</u>	<u>(1,545,415)</u>
Net capital assets	<u>\$ 1,316,755</u>	<u>\$ (63,026)</u>	<u>\$ 0</u>	<u>\$ 1,253,729</u>

NOTE 4 - LONG TERM LIABILITIES

\$615,000 General Obligation Water Supply System Bond Dated September 14, 1989

Said bonds are issued pursuant to the resolutions adopted by the City Council of the City of Harrisville for the purpose of the construction of a water supply system and improvements.

These bonds constitute a valid and legally binding obligation of the City of Harrisville, payable from ad valorem taxes assessed in the City, and payable from net revenues of said water supply system collected from the users of such system through use charges pursuant to the ordinances of the City of Harrisville.

The bonds, which bear interest at 5%, are due serially through 2029, payable on July 1, with interest due semi-annually on January 1 and July 1 of each year.

Annual Principal and Interest Requirements

<u>Fiscal</u> <u>Year</u>	<u>January 1</u> <u>Interest</u>	<u>July 1</u> <u>Principal</u>	<u>July 1</u> <u>Interest</u>	<u>Total</u> <u>Future Annual</u> <u>Requirements</u>
2008	\$ 11,950	\$ 12,000	\$ 11,950	\$ 35,900
2009	11,650	13,000	11,650	36,300
2010	11,325	14,000	11,325	36,650
2011	10,975	14,000	10,975	35,950
2012	10,625	15,000	10,625	36,250
2013	10,250	16,000	10,250	36,500
2014	9,850	17,000	9,850	36,700
2015	9,425	17,000	9,425	35,850
2016	9,000	18,000	9,000	36,000
2017	8,550	19,000	8,550	36,100
2018	8,075	20,000	8,075	36,150

CITY OF HARRISVILLE  
WATER AND SEWER FUNDS  
Alcona County, Michigan

NOTES TO FINANCIAL STATEMENTS  
For the Year Ended December 31, 2007

NOTE 4 - LONG TERM LIABILITIES (CONTINUED)

Annual Principal and Interest Requirements

<u>Fiscal Year</u>	<u>January 1 Interest</u>	<u>July 1 Principal</u>	<u>July 1 Interest</u>	<u>Total Future Annual Requirements</u>
2019	\$ 7,575	\$ 21,000	\$ 7,575	\$ 36,150
2020	7,050	22,000	7,050	36,100
2021	6,500	23,000	6,500	36,000
2022	5,925	25,000	5,925	36,850
2023	5,300	26,000	5,300	36,600
2024	4,650	27,000	4,650	36,300
2025	3,975	29,000	3,975	36,950
2026	3,250	30,000	3,250	36,500
2027	2,500	32,000	2,500	37,000
2028	1,700	33,000	1,700	36,400
2029	875	35,000	875	36,750
	<u>\$ 160,975</u>	<u>\$ 478,000</u>	<u>\$ 160,975</u>	<u>\$ 799,950</u>

\$462,000 Contract Payable - County, Dated March 5, 1976

The City of Harrisville entered into a contract with the County of Alcona, through its Board of Public Works, to finance a portion of the costs for sewage collection and treatment facilities. The City also enacted Ordinance No. 75-1 authorizing the sale of revenue bonds by the County.

Pursuant to Act no. 185, Public Acts of Michigan, 1957, the City has irrevocably pledged its full faith and credit for the payment of this issue. If revenues are insufficient to cover annual obligations, the City shall levy an ad valorem tax to pay these obligations.

Ordinance No. 75-1 requires the establishment of certain funds and accounts. A Receiving Fund is to be used for all incoming revenue. This account has been established. A Bond Reserve Account is to be opened whereby at least \$250 per quarter is to be deposited until there is accumulated the sum of \$30,000. All bonds carry interest at 5%. This requirement has been met.

Annual Principal and Interest Requirements

<u>Year</u>	<u>January 1 Principal</u>	<u>January 1 Interest</u>	<u>July 1 Interest</u>	<u>Total Future Annual Requirements</u>
2008	\$ 0	\$ 0	\$ 3,900	\$ 3,900
2009	21,000	3,900	3,375	28,275
2010	22,000	3,375	2,825	28,200
2011	22,000	2,825	2,275	27,100
2012	22,000	2,275	1,725	26,000
2013	22,000	1,725	1,175	24,900
2014	22,000	1,175	625	23,800
2015	25,000	625	0	25,625
	<u>\$ 156,000</u>	<u>\$ 15,900</u>	<u>\$ 15,900</u>	<u>\$ 187,800</u>

CITY OF HARRISVILLE  
WATER AND SEWER FUNDS  
Alcona County, Michigan

NOTES TO FINANCIAL STATEMENTS  
For the Year Ended December 31, 2007

NOTE 4 - LONG TERM LIABILITIES (CONTINUED)

Changes in Long-Term Liabilities

	<u>Balance</u> <u>January 1, 2007</u>	<u>Issues or</u> <u>Additions</u>	<u>Payments or</u> <u>Expenditures</u>	<u>Balance</u> <u>December 31, 2007</u>	<u>Due Within</u> <u>One Year</u>
Bond payable	\$ 490,000	\$ 0	\$ 12,000	\$ 478,000	\$ 12,000
Contract payable	<u>176,000</u>	<u>0</u>	<u>20,000</u>	<u>156,000</u>	<u>0</u>
Total	<u>\$ 666,000</u>	<u>\$ 0</u>	<u>\$ 32,000</u>	<u>\$ 634,000</u>	<u>\$ 12,000</u>

NOTE 5 - UNEMPLOYMENT COMPENSATION

The City is subject to the Michigan Employment Security Act and has elected the reimbursement method of financing. Under this method, the City must reimburse the Employment Agency for all benefits charged against the City. No liabilities were due as of December 31, 2007.

NOTE 6 - RISK MANAGEMENT

The Water and Sewer Funds are exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees and natural disasters. The Water and Sewer Funds continue to carry commercial insurance for risks of loss. Settled claims for the commercial insurance have not exceeded the amount of insurance coverage in any of the past three years.

NOTE 7 - RECONCILIATION OF NET OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES

	<u>Water Fund</u>	<u>Sewer Fund</u>	<u>Total</u> <u>Enterprise Fund</u>
Operating income (loss)	\$ (6,225)	\$ 25,271	\$ 19,046
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:			
Depreciation	34,298	33,899	68,197
Changes in assets and liabilities:			
Increase in accounts receivable	(1,576)	(985)	(2,561)
Decrease in accounts payable	<u>(4,545)</u>	<u>0</u>	<u>(4,545)</u>
Net cash provided by operating activities	<u>\$ 21,952</u>	<u>\$ 58,185</u>	<u>\$ 80,137</u>

OTHER INFORMATION

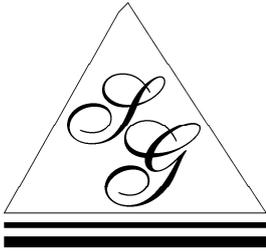
CITY OF HARRISVILLE  
 WATER AND SEWER FUNDS  
Alcona County, Michigan

SUPPLEMENTAL INFORMATION FOR FARMERS HOME ADMINISTRATION  
For the Year Ended December 31, 2007

1. Our audit was conducted in accordance with auditing standards generally accepted in the United States of America.
2. An evaluation of the internal control structure is included in the financial statements.
3. The accounting records maintained by the City of Harrisville for the Water and Sewer Funds are satisfactory and we have no recommendations for improvement.
4. The City's physical control of the assets is satisfactory.
5. The City is in financial compliance with the loan agreement. Certain reporting requirements will be met with the issuance of this report.
6. The financial reports included in this audit report are in agreement with the accounting records of the City and no major or unusual adjustments are necessary.
7. Deposit funds of the project are in financial institutions insured by the federal government.
8. The City of Harrisville has insurance coverage on all of its equipment at replacement cost.
9. The City of Harrisville is exempt from federal income tax.
10. No unsatisfactory conditions were noted during the audit.
11. An aging of accounts receivable as of December 31, 2007 is as follows:

	<u>Total</u>	<u>0 – 30</u>	<u>31 – 60</u>	<u>61 – 90</u>	<u>Over 90</u>
Customers:					
Water Fund	\$ 20,413	\$ 18,779	\$ 0	\$ 0	\$ 1,634
Sewer Fund	\$ 26,669	\$ 24,218	\$ 0	\$ 0	\$ 2,451

12. No other information is necessary for full disclosure.



*Stephenson Gracik & Co., P.C.*

Certified Public Accountants & Consultants

Alan J Stephenson, CPA  
Gerald D Gracik Jr., CPA  
James J Gracik, CPA  
E. Thad Gray, CPA  
Donald W. Brannan, CPA  
Kyle E Troyer, CPA  
-----  
Herman A Bertuleit, CPA

February 21, 2008

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON  
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS  
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

Members of the City Council  
City of Harrisville  
Alcona County, Michigan

We have audited the financial statements of the business-type activities of the City of Harrisville Water and Sewer Funds, as of and for the year ended December 31, 2007, which collectively comprise the City of Harrisville Water and Sewer Funds' basic financial statements, and have issued our report thereon dated February 21, 2008. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the City of Harrisville Water and Sewer Funds' internal control over financial reporting as a basis for designing our auditing procedures 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 Harrisville Water and Sewer Funds' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City of Harrisville Water and Sewer Funds' internal control over financial reporting.

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

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the City of Harrisville Water and Sewer Funds' ability to initiate, authorize, record, process or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the City of Harrisville Water and Sewer Funds' financial statements that is more than inconsequential will not be prevented or detected by the City of Harrisville Water and Sewer Funds' internal control. We consider the deficiencies described below to be significant deficiencies in internal control over financial reporting:

Separation of Duties in the Performance of Functions

Due to the limited number of staff of the City, there is an absence of appropriate segregation of duties. The clerk receives cash, has control over non-cash accounting records and writes and signs checks. To offset this deficiency, bank reconciliations and a dual signature are required of the City Treasurer.

Financial Statement Preparation

The City of Harrisville Water and Sewer Funds prepare various financial information throughout the year to assess operations and the financial condition of the City of Harrisville Water and Sewer Funds. However, prior to the closing of the year end, various entries material to the financial statements were proposed by our firm. Also, the City of Harrisville Water and Sewer Funds rely on our firm to assist in preparing the annual financial report in accordance with Generally Accepted Accounting Principles.

Members of the City Council  
City of Harrisville  
February 21, 2008  
Page Two

The City of Harrisville Water and Sewer Funds have individuals on staff to review that the financial report is accurate and the financial information reflects the recording of the proposed entries, however, not to review and determine that the financial report is a complete presentation in accordance with Generally Accepted Accounting Principles. As a result, the City of Harrisville Water and Sewer Funds is considered to have a significant control deficiency, since reporting errors or omissions could occur in the preparation of the annual financial report that would be departures from Generally Accepted Accounting Principles and the City of Harrisville Water and Sewer Funds would not be in a position to detect the errors or omissions.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the City of Harrisville Water and Sewer Funds' internal control.

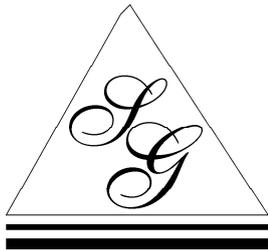
Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe the significant deficiencies described above to be material weaknesses.

#### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Harrisville Water and Sewer Funds' 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 tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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

*Stephenson, Grain & Co., P.C.*



*Stephenson Gracik & Co., P.C.*

Certified Public Accountants & Consultants

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-----  
Herman A Bertuleit, CPA

February 21, 2008

Members of the City Council  
City of Harrisville  
Alcona County, Michigan

Dear Council Members:

We have audited the financial statements of the business-type activities of the City of Harrisville Water and Sewer Funds for the year ended December 31, 2007, and have issued our report thereon dated February 21, 2008. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility Under U.S. Generally Accepted Auditing Standards and Government Auditing Standards

As stated in our engagement letter dated January 10, 2008, our responsibility, as described by professional standards, is to plan and perform our audit to obtain reasonable, but not absolute, assurance about whether the financial statements are free of material misstatement and are fairly presented in accordance with U.S. generally accepted accounting principles. Because an audit is designed to provide reasonable, but not absolute assurance and because we did not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by us.

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

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of the City of Harrisville Water and Sewer Funds' compliance with certain provisions of laws, regulations, contracts and grants. However, the objective of our tests was not to provide an opinion on compliance with such provisions.

Significant Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the City of Harrisville Water and Sewer Funds are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year. We noted no transactions entered into by the City of Harrisville Water and Sewer Funds during the year that were both significant and unusual, and of which, under professional standards, we are required to inform you, or transactions for which there is a lack of authoritative guidance or consensus.

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.

Audit Adjustments

For purposes of this letter, professional standards define an audit adjustment as a proposed correction of the financial statements that, in our judgment, may not have been detected except through our auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on the City of Harrisville Water and Sewer Funds' financial reporting process (that is, cause future financial statements to be materially misstated). In our judgment, none of the adjustments we proposed, whether recorded or unrecorded by the City of Harrisville Water and Sewer Funds, either individually or in the aggregate, indicate matters that could have a significant effect on the City of Harrisville Water and Sewer Funds' financial reporting process.

Members of the City Council  
City of Harrisville  
February 21, 2008  
Page Two

Disagreements with Management

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

Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of 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.

Issues Discussed Prior to Retention of Independent Auditors

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

Difficulties Encountered in Performing the Audit

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

Additional Information

As a result of our tests of controls and compliance as described in the third and fourth paragraphs, two matters came to our attention upon which we would like to comment.

Separation of Duties in the Performance of Functions

Due to the limited number of staff of the City, there is an absence of appropriate segregation of duties. The clerk receives cash, has control over non-cash accounting records and writes and signs checks. To offset this deficiency, bank reconciliations and a dual signature are required of the City Treasurer.

Financial Statement Preparation

The City of Harrisville Water and Sewer Funds prepare various financial information throughout the year to assess operations and the financial condition of the City of Harrisville Water and Sewer Funds. However, prior to the closing of the year end, various entries material to the financial statements were proposed by our firm. Also, the City of Harrisville Water and Sewer Funds rely on our firm to assist in preparing the annual financial report in accordance with Generally Accepted Accounting Principles.

The City of Harrisville Water and Sewer Funds have individuals on staff to review that the financial report is accurate and the financial information reflects the recording of the proposed entries, however, not to review and determine that the financial report is a complete presentation in accordance with Generally Accepted Accounting Principles. As a result, the City of Harrisville Water and Sewer Funds is considered to have a significant control deficiency, since reporting errors or omissions could occur in the preparation of the annual financial report that would be departures from Generally Accepted Accounting Principles and the City of Harrisville Water and Sewer Funds would not be in a position to detect the errors or omissions.

We wish to express our appreciation for the cooperation and courtesies extended our staff by management and employees of the City.

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

*Stephenson, Grubb & Co., P.C.*