

Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended and P.A. 71 of 1919, as amended.

| | | | |
|---|--------------|--------------------------------------|--------|
| Local Unit of Government Type <input type="checkbox"/> County <input type="checkbox"/> City <input type="checkbox"/> Twp <input type="checkbox"/> Village <input type="checkbox"/> Other | | Local Unit Name | County |
| Fiscal Year End | Opinion Date | Date Audit Report Submitted to State | |

We affirm that:

We are certified public accountants licensed to practice in Michigan.

We further affirm the following material, "no" responses have been disclosed in the financial statements, including the notes, or in the Management Letter (report of comments and recommendations).

YES NO Check each applicable box below. (See instructions for further detail.)

1. All required component units/funds/agencies of the local unit are included in the financial statements and/or disclosed in the reporting entity notes to the financial statements as necessary.
2. There are no accumulated deficits in one or more of this unit's unreserved fund balances/unrestricted net assets (P.A. 275 of 1980) or the local unit has not exceeded its budget for expenditures.
3. The local unit is in compliance with the Uniform Chart of Accounts issued by the Department of Treasury.
4. The local unit has adopted a budget for all required funds.
5. A public hearing on the budget was held in accordance with State statute.
6. The local unit has not violated the Municipal Finance Act, an order issued under the Emergency Municipal Loan Act, or other guidance as issued by the Local Audit and Finance Division.
7. The local unit has not been delinquent in distributing tax revenues that were collected for another taxing unit.
8. The local unit only holds deposits/investments that comply with statutory requirements.
9. The local unit has no illegal or unauthorized expenditures that came to our attention as defined in the *Bulletin for Audits of Local Units of Government in Michigan*, as revised (see Appendix H of Bulletin).
10. There are no indications of defalcation, fraud or embezzlement, which came to our attention during the course of our audit that have not been previously communicated to the Local Audit and Finance Division (LAFD). If there is such activity that has not been communicated, please submit a separate report under separate cover.
11. The local unit is free of repeated comments from previous years.
12. The audit opinion is UNQUALIFIED.
13. The local unit has complied with GASB 34 or GASB 34 as modified by MCGAA Statement #7 and other generally accepted accounting principles (GAAP).
14. The board or council approves all invoices prior to payment as required by charter or statute.
15. To our knowledge, bank reconciliations that were reviewed were performed timely.

If a local unit of government (authorities and commissions included) is operating within the boundaries of the audited entity and is not included in this or any other audit report, nor do they obtain a stand-alone audit, please enclose the name(s), address(es), and a description(s) of the authority and/or commission.

I, the undersigned, certify that this statement is complete and accurate in all respects.

| We have enclosed the following: | Enclosed | Not Required (enter a brief justification) |
|--|--------------------------|--|
| Financial Statements | <input type="checkbox"/> | |
| The letter of Comments and Recommendations | <input type="checkbox"/> | |
| Other (Describe) | <input type="checkbox"/> | |
| Certified Public Accountant (Firm Name) | | Telephone Number |
| Street Address | City | State Zip |
| Authorizing CPA Signature | Printed Name | License Number |

City of Mason, Michigan

**Financial Report
with Supplemental Information
June 30, 2007**

City of Mason, Michigan

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Independent Auditor's Report

To the City Council
City of Mason, Michigan

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Mason, Michigan as of and for the year ended June 30, 2007, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City of Mason, Michigan'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. 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.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Mason, Michigan as of June 30, 2007 and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis and the budgetary comparison schedules, as identified in the table of contents, are not a required part of the basic financial statements but are supplemental information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management, regarding the methods of measurement and presentation of the required supplemental 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 Mason, Michigan's basic financial statements. The accompanying other supplemental information, as identified in the table of contents, is presented for the purpose of additional analysis and is not a required part of the basic financial statements.

To the City Council
City of Mason, Michigan

The other supplemental information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

As described in Note 11, the City has fully implemented the financial reporting for retroactive reporting of infrastructure, as required by the provisions of GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, and related statements, as of July 1, 2006.

Plante & Moran, PLLC

October 5, 2007

Our discussion and analysis of the City of Mason, Michigan's financial performance provides an overview of the City's financial activities for the fiscal year ended June 30, 2007. Please read it in conjunction with the City's financial statements.

Overview of the Financial Statements

This annual report consists of the following report sections: management's discussion and analysis (this section), the basic financial statements, required supplemental information, and other supplemental information section that presents combining statements for nonmajor governmental funds. The basic financial statements are presented in two different formats: government-wide financial statements and fund financial statements.

The government-wide financial statements include the statement of net assets (deficit) and the statement of activities. These statements provide both long-term and short-term information about the City's overall financial status.

The fund financial statements include the balance sheet and the statement of revenue, expenditures, and changes in net fund balances. These statements focus on individual parts of the City government and report the City's operations in more detail than the government-wide statements by providing information about the City's most significant funds.

The governmental fund statements tell how general government services, such as police and fire, were financed in the short term as well as what remains for future spending.

The proprietary fund statements present short- and long-term financial information about those activities that the City operates in a business-like manner, such as the water and sewer system.

The fiduciary fund statements provide information about the financial relationships in which the City acts solely as a trustee or agent for the benefit of others, to whom the resources in question belong.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of required supplemental information that further explains and supports the information presented in the financial statements. In addition to these required supplementary schedules, we have provided a section with combining statements that provide details about our nonmajor governmental and fiduciary funds.

City of Mason, Michigan

Management's Discussion and Analysis (Continued)

Government-wide Financial Statements

The City's government-wide statements begin on page 12 of this report. These statements report information about the City as a whole under the full accrual method of accounting, which is similar to the accounting used by most private-sector companies. The statement of net assets (deficit) includes all, both current and long-term, of the government's assets and liabilities and the statement of activities includes all of the current year's revenues and expenses regardless of when cash is received or paid.

The combined objective of the government-wide statements is to report the City's net assets and how they have changed. The reporting of net assets is one way to measure the City's financial health or position.

Over time, increases or decreases in the City's net assets can be viewed as indicators of whether its financial health is improving or deteriorating, respectively.

In addition to the financial factors, you will need to consider additional information such as changes in the City's property tax base to assess the overall health.

The City's government-wide financial statements divide the reported information into three categories:

- Governmental activities - Most of the City's basic services are included here, such as police, fire, cemetery, parks, and general administration. Property taxes and state revenue sharing are used to finance most of these activities.
- Business-type activities - The City charges fees to customers to help it cover the costs of certain services it provides. The City's water and sewer system is included in this category.
- Component units - The City includes other legal entities in its report such as the Downtown Development Authority and the Local Development Finance Authority. The City is financially accountable for these "component units" although they are legally separate entities.

City of Mason, Michigan

Management's Discussion and Analysis (Continued)

Fund Financial Statements

The City's fund financial statements begin on page 15 of this report. These statements provide more detailed information about the City's most significant funds. The City uses funds to account for specific sources of funding and spending for particular purposes. Some funds are required by state law and others are established by the City to control and manage money for particular purposes or to show that it is properly using certain taxes and grants.

The City has three kinds of funds that use different accounting approaches:

- Governmental funds - Most of the City's basic services are included in governmental funds. These funds 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. These funds are reported using the modified accrual accounting method that measures cash and all other financial assets that can be readily converted to cash. The governmental fund statements provide a detailed short-term view of the City's general government operations and the basic services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs. Because governmental fund information has a short-term focus and the government-wide statement incorporates long-term information, we describe the relationship (or differences) between government activities and governmental funds in a reconciliation on pages 16 and 18).
- Proprietary funds - When the City charges customers fees for the services it provides, the fees are generally reported in proprietary funds. Similar to the reporting method used on the government-wide statements, proprietary funds provide both long- and short-term financial information.
 - In fact, the City's Enterprise Fund (water and sewer) is the same as its business-type activity, but provides more detail and additional information.
 - We use an Internal Service Fund (the other type of proprietary fund) to report activities that provide services and supplies to other programs and activities within the City. The City's Motor Vehicle Pool Fund falls into this category.
- Fiduciary funds - The City is responsible for ensuring that the assets reported in these funds are used for their intended purpose. The delinquent tax and payroll funds are fiduciary funds.

City of Mason, Michigan

Management's Discussion and Analysis (Continued)

Financial Highlights

As discussed in further detail in this discussion and analysis, the following represents the most significant financial highlights for the year ended June 30, 2007:

- The City's total net assets increased as a result of the fiscal year's operations and the addition of previously unrecorded capital assets. The net assets of our business-type activities increased by \$473,000, or 3.4 percent, and net assets of our governmental activities increased by \$1,021,000, or 5.5 percent. As discussed in Note 11, a prior period adjustment to reflect the reporting of retroactive infrastructure was recorded in the governmental activities, which resulted in an increase in net assets. This addition fulfilled the reporting requirements for GASB 34 implementation and amounted to \$9.5 million.
- During the year, the City had revenues that were \$1,021,000 more than the \$4.1 million in expenses.
- Improved interest rates boosted investment income as a revenue source.
- In the City's business-type activities, revenues were \$2.4 million while expenses were \$1.9 million.
- Total costs of all the City's programs were \$6.0 million.
- The General Fund reported an increase of \$736,500.

City of Mason, Michigan

Management's Discussion and Analysis (Continued)

The City as a Whole

As described in Note 11, net assets for the prior year have been restated. The following table shows, in a condensed format, the current year's net assets for the years ended June 30, 2007 and 2006, including restated amounts:

Table 1

| | Governmental Activities (as restated) | | Business-type Activities | | Total | |
|------------------------------|--|----------------------|--------------------------|----------------------|----------------------|----------------------|
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| Assets | | | | | | |
| Current assets | \$ 6,118,529 | \$ 5,415,231 | \$ 5,055,824 | \$ 5,031,704 | \$ 11,174,353 | \$ 10,446,935 |
| Noncurrent assets | 15,916,443 | 15,519,685 | 9,406,133 | 8,980,602 | 25,322,576 | 24,500,287 |
| Total assets | 22,034,972 | 20,934,916 | 14,461,957 | 14,012,306 | 36,496,929 | 34,947,222 |
| Liabilities | | | | | | |
| Current liabilities | 396,962 | 380,648 | 137,856 | 102,485 | 534,818 | 483,133 |
| Long-term liabilities | 1,954,423 | 1,892,080 | 91,548 | 150,339 | 2,045,971 | 2,042,419 |
| Total liabilities | 2,351,385 | 2,272,728 | 229,404 | 252,824 | 2,580,789 | 2,525,552 |
| Net Assets | | | | | | |
| Invested in capital assets - | | | | | | |
| Net of related debt | 14,015,976 | 13,719,798 | 9,347,820 | 8,909,257 | 23,363,796 | 22,629,055 |
| Restricted | 2,090,511 | 1,942,422 | - | - | 2,090,511 | 1,942,422 |
| Unrestricted | 3,577,100 | 2,999,968 | 4,884,733 | 4,850,225 | 8,461,833 | 7,850,193 |
| Total net assets | <u>\$ 19,683,587</u> | <u>\$ 18,662,188</u> | <u>\$ 14,232,553</u> | <u>\$ 13,759,482</u> | <u>\$ 33,916,140</u> | <u>\$ 32,421,670</u> |

The City's combined net assets were increased from a year ago from \$32.4 million to \$33.9 million.

Approximately 71.0 percent of the City's net assets of governmental activities reflect its investment in capital less any related debt used to acquire those assets. The City's capital assets are used to provide services to citizens. Consequently, these assets are not available for future spending. Restricted net assets represent resources that are subject to external restrictions on how they may be used. Unrestricted net assets of governmental activities of \$3.6 million represent the amount that may be used to meet the City's ongoing obligations.

Prior year net assets of the City's governmental activities were restated, resulting in an increase of nearly 104.0 percent to \$18.7 million. This increase was due to the City having recognized assets owned by the City but not previously recorded. These amounts have also been added to capital assets as infrastructure additions.

The net assets of our business-type activities increased by 3.4 percent or to \$14.2 million during the fiscal year. This increase is due to revenues exceeding expenses and continued investment in infrastructure (water and sewer mains) without additional debt being incurred.

City of Mason, Michigan

Management's Discussion and Analysis (Continued)

The following table illustrates the varying results of the governmental activities and business-type activities, which combine to capture the City's total net assets, for the years ended June 30, 2007 and 2006.

Table 2

| | Governmental Activities | | Business-type Activities | | Total | |
|------------------------------------|-------------------------|---------------------|--------------------------|---------------------|---------------------|---------------------|
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| Revenue | | | | | | |
| Program revenue: | | | | | | |
| Charges for services | \$ 1,031,497 | \$ 811,023 | \$ 2,127,058 | \$ 1,897,891 | \$ 3,158,555 | \$ 2,708,914 |
| Operating grants and contributions | 440,218 | 503,624 | - | - | 440,218 | 503,624 |
| Capital grants and contributions | 83,747 | 1,021,723 | - | 909,444 | 83,747 | 1,931,167 |
| General revenue: | | | | | | |
| Property taxes | 2,735,046 | 2,453,396 | - | - | 2,735,046 | 2,453,396 |
| State-shared revenue | 651,730 | 659,474 | - | - | 651,730 | 659,474 |
| Investment earnings | 155,924 | 115,376 | 292,469 | 67,658 | 448,393 | 183,034 |
| Miscellaneous | 2,962 | 3,371 | - | - | 2,962 | 3,371 |
| Total revenue | 5,101,124 | 5,567,987 | 2,419,527 | 2,874,993 | 7,520,651 | 8,442,980 |
| Program Expenses | | | | | | |
| General government | 1,197,777 | 1,193,132 | - | - | 1,197,777 | 1,193,132 |
| Public safety | 1,289,605 | 1,235,424 | - | - | 1,289,605 | 1,235,424 |
| Public works | 1,263,037 | 772,718 | - | - | 1,263,037 | 772,718 |
| Community and economic development | 6,362 | 7,710 | - | - | 6,362 | 7,710 |
| Recreation and culture | 235,549 | 193,025 | - | - | 235,549 | 193,025 |
| Interest on long-term debt | 87,395 | 55,203 | - | - | 87,395 | 55,203 |
| Water and sewer | - | - | 1,946,456 | 1,827,573 | 1,946,456 | 1,827,573 |
| Total program expenses | 4,079,725 | 3,457,212 | 1,946,456 | 1,827,573 | 6,026,181 | 5,284,785 |
| Change in Net Assets | \$ 1,021,399 | \$ 2,110,775 | \$ 473,071 | \$ 1,047,420 | \$ 1,494,470 | \$ 3,158,195 |

Governmental Activities

- The cost of all governmental activities this year was \$4.1 million.
- The amount that City taxpayers paid for these activities through City taxes was only \$2.7 million.
- Some of the cost was paid by the beneficiaries of the program's activities (\$1.0 million), or by other governments and organizations that subsidized certain programs with grants and contributions (\$0.5 million).
- Charges for services increased due to one large building permit for an addition to an industrial facility.
- Public works expense increased primarily due to the depreciation on infrastructure assets that were retroactively recognized.
- Capital grants and contributions decreased due to a nonrecurring special assessment project that was recognized in 2006.

City of Mason, Michigan

Management's Discussion and Analysis (Continued)

Business-type Activities

- Total revenues of the City's business-type activities, water and sewer, decreased to \$2.4 million for 2007 from \$2.9 million in 2006 and total expenses increased to \$1.9 million in 2007 from \$1.8 million in 2006. The City experienced a change in net assets of \$475,000 in its water and sewer operations. Factors contributing to these results include:
 - Increased interest income of \$225,000
 - Increased user fees
 - Capital grants and contributions decreased due to a nonrecurring special assessment project that was recognized in 2006

The City's Funds

Our analysis of the City's major funds begins on page 15, following the government-wide financial statements. The fund financial statements provide detailed information about the most significant funds, not the City as a whole. The City creates funds to help manage money for specific purposes as well as to show accountability for certain activities. The City's major funds for 2007 include the General Fund, the Local Street Fund, and the Special Assessment Fund. These funds, along with the remaining nonmajor funds, reported a combined fund balance of \$3.4 million, representing an increase over last year's combined fund balance of \$2.7 million.

General Fund Budgetary Highlights

Over the course of the year, the City Council revised the City budget several times. We began the year expecting to set aside additional funds in the General Fund earmarked specifically for future City Hall improvements. The original budget predicted a surplus of \$347,000. The City ended the year with a surplus of \$736,500.

City of Mason, Michigan

Management's Discussion and Analysis (Continued)

Capital Asset and Debt Administration

At the end of the 2007 fiscal year, the City had invested approximately \$25.3 million in a broad range of capital assets, including police equipment, buildings and improvements, computer equipment and software, parks and recreational facilities, roads, and water and sewer lines (see Table 3 below).

Table 3

| | Governmental Activities (as restated) | | Business-type Activities | | Total | |
|----------------------------|--|----------------------|--------------------------|---------------------|----------------------|----------------------|
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| | Land | \$ 1,426,251 | \$ 1,426,251 | \$ 25,609 | \$ 25,609 | \$ 1,451,860 |
| Construction in progress | - | 960,050 | 713,363 | 1,039,002 | 713,363 | 1,999,052 |
| Land improvements | 875,043 | 793,000 | - | - | 875,043 | 793,000 |
| Buildings and improvements | 1,535,960 | 1,535,960 | 455,637 | 455,637 | 1,991,597 | 1,991,597 |
| Infrastructure | 20,858,784 | 19,216,358 | 13,887,118 | 12,746,179 | 34,745,902 | 31,962,537 |
| Vehicles and equipment | 2,445,188 | 2,121,002 | - | - | 2,445,188 | 2,121,002 |
| Subtotal assets | 27,141,226 | 26,052,621 | 15,081,727 | 14,266,427 | 42,222,953 | 40,319,048 |
| Accumulated depreciation | 11,224,783 | 10,479,175 | 5,675,594 | 5,285,825 | 16,900,377 | 15,765,000 |
| Net capital assets | \$ 15,916,443 | \$ 15,573,446 | \$ 9,406,133 | \$ 8,980,602 | \$ 25,322,576 | \$ 24,554,048 |

This year's major additions to capital assets included:

- Purchase of a pumper/tanker truck for the fire department for \$280,000
- Construction of a new playground in Laylin Park for \$65,000
- Construction of roads and sidewalks amounting to approximately \$680,000

Debt

At year end, the City had \$2.0 million in bonds and notes outstanding. This represents an \$87,550 increase from the previous year (see Table 4 below). More detailed information about the City's long-term liabilities is presented in Note 7 to the basic financial statements.

Table 4

| | Governmental Activities | | Business-type Activities | | Total | |
|--------------------------------|-------------------------|---------------------|--------------------------|------------------|---------------------|---------------------|
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| General obligations debt | \$ 918,467 | \$ 752,887 | \$ - | \$ - | \$ 918,467 | \$ 752,887 |
| Special assessment obligations | 982,000 | 1,047,000 | - | - | 982,000 | 1,047,000 |
| Revenue bonds | - | - | 58,313 | 71,345 | 58,313 | 71,345 |
| Total | \$ 1,900,467 | \$ 1,799,887 | \$ 58,313 | \$ 71,345 | \$ 1,958,780 | \$ 1,871,232 |

The City has been given a bond rating of "A" by Standards and Poor.

City of Mason, Michigan

Management's Discussion and Analysis (Continued)

Economic Factors and Next Year's Budgets and Rates

The City's budget for the 2007/2008 fiscal year is balanced with no property tax rate increase. Estimated property tax revenues are expected to increase by approximately \$300,000 from the prior year due mainly to added tax base from new development in the industrial area and increases in commercial and residential.

Total expenses in the General Fund for the 2007/2008 fiscal year are estimated to be \$5.5 million. Included in those costs are the General Fund's contributions to support the streets program (\$400,000). A portion of the anticipated surplus will be used to finance future improvements to City Hall.

Due to revised radium standards, the City of Mason is in the process of planning construction of a water treatment plant. At least one new well site is also needed. Testing over the last two years has ruled out several potential sites. The City is conducting a cost study for water and sewer user fees during the 2007/2008 fiscal year to ensure that user fees adequately cover current and future needs.

Contacting the City of Mason's Management

This financial report is intended to provide citizens, taxpayers, customers, and investors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have any questions about this report or need additional information, we welcome you to contact the City administrator's office at the City of Mason, 517-676-9155.

City of Mason, Michigan

Statement of Net Assets (Deficit) June 30, 2007

| | Primary Government | | | Component Units |
|---|----------------------------|-----------------------------|---------------|--------------------|
| | Governmental Activities | Business-type Activities | Total | |
| Assets | | | | |
| Cash and cash equivalents (Note 3) | \$ 3,840,308 | \$ 4,642,737 | \$ 8,483,045 | \$ 1,030,997 |
| Receivables: | | | | |
| Taxes | 29,025 | - | 29,025 | 11,748 |
| Customer | 13,386 | 372,140 | 385,526 | - |
| Assessments | 1,923,847 | - | 1,923,847 | - |
| Due from other governmental units | 295,591 | - | 295,591 | 21,596 |
| Other | 5,774 | - | 5,774 | 1,292 |
| Inventories | - | 28,606 | 28,606 | - |
| Prepaid costs and other assets | 10,598 | 12,341 | 22,939 | - |
| Capital assets - Net (Note 4): | | | | |
| Nondepreciable | 1,426,251 | 738,972 | 2,165,223 | - |
| Depreciable | 14,490,192 | 8,667,161 | 23,157,353 | 213,175 |
| Total assets | 22,034,972 | 14,461,957 | 36,496,929 | 1,278,808 |
| Liabilities | | | | |
| Accounts payable | 10,555 | 113,090 | 123,645 | 3,899 |
| Accrued and other liabilities | 65,970 | - | 65,970 | 8,289 |
| Due to other governmental units | 12,015 | - | 12,015 | 21,596 |
| Deferred revenue (Note 6) | 9,100 | - | 9,100 | - |
| Current portion of long-term liabilities: | | | | |
| Compensated absences | 105,763 | 11,153 | 116,916 | - |
| Long-term debt (Note 7) | 193,559 | 13,613 | 207,172 | 334,448 |
| Noncurrent portion of long-term liabilities: | | | | |
| Compensated absences | 247,515 | 46,848 | 294,363 | - |
| Long-term debt (Note 7) | 1,706,908 | 44,700 | 1,751,608 | 1,134,964 |
| Total liabilities | 2,351,385 | 229,404 | 2,580,789 | 1,503,196 |
| Net Assets (Deficit) | | | | |
| Invested in capital assets - Net of related debt | 14,015,976 | 9,347,820 | 23,363,796 | 213,175 |
| Restricted: | | | | |
| Streets and highways | 643,614 | - | 643,614 | - |
| Debt service funds | 273,003 | - | 273,003 | - |
| Capital improvements | 42,039 | - | 42,039 | - |
| Cemetery | 316,702 | - | 316,702 | - |
| Rayner Bond | 505,941 | - | 505,941 | - |
| Construction code activities | 309,212 | - | 309,212 | - |
| Unrestricted (deficit) | 3,577,100 | 4,884,733 | 8,461,833 | (437,563) |
| Total net assets (deficit) | \$ 19,683,587 | \$ 14,232,553 | \$ 33,916,140 | \$ (224,388) |

City of Mason, Michigan

| | Program Revenues | | | |
|--|---------------------|----------------------|------------------------------------|----------------------------------|
| | Expenses | Charges for Services | Operating Grants and Contributions | Capital Grants and Contributions |
| Functions/Programs | | | | |
| Primary government: | | | | |
| Governmental activities: | | | | |
| General government | \$ 1,197,777 | \$ 517,729 | \$ - | \$ 83,747 |
| Public safety | 1,289,605 | 171,483 | 1,410 | - |
| Public works | 1,263,037 | 309,435 | 438,808 | - |
| Community and economic development | 6,362 | 29,770 | - | - |
| Recreation and culture | 235,549 | 3,080 | - | - |
| Interest expense | 87,395 | - | - | - |
| Total governmental activities | 4,079,725 | 1,031,497 | 440,218 | 83,747 |
| Business-type activities - Water and sewer | 1,946,456 | 2,127,058 | - | - |
| Total primary government | \$ 6,026,181 | \$ 3,158,555 | \$ 440,218 | \$ 83,747 |
| Component units: | | | | |
| Local Development Finance Authority | \$ 141,052 | \$ - | \$ - | \$ - |
| Downtown Development Authority | 113,417 | - | - | - |
| Economic Development Committee | - | - | - | - |
| Total component units | \$ 254,469 | \$ - | \$ - | \$ - |
| General revenues: | | | | |
| Property taxes | | | | |
| State-shared revenues | | | | |
| Investment earnings | | | | |
| Miscellaneous | | | | |
| Total general revenues | | | | |
| Change in Net Assets | | | | |
| Net Assets (Deficit) - Beginning of year, as restated (Note 11) | | | | |
| Net Assets (Deficit) - End of year | | | | |

Statement of Activities
Year Ended June 30, 2007

| Net (Expense) Revenue and Changes in Net Assets | | | |
|---|-----------------------------|----------------------|---------------------|
| Primary Government | | | |
| Governmental Activities | Business-type Activities | Total | Component Units |
| \$ (596,301) | \$ - | \$ (596,301) | \$ - |
| (1,116,712) | - | (1,116,712) | - |
| (514,794) | - | (514,794) | - |
| 23,408 | - | 23,408 | - |
| (232,469) | - | (232,469) | - |
| (87,395) | - | (87,395) | - |
| (2,524,263) | - | (2,524,263) | - |
| - | 180,602 | 180,602 | - |
| (2,524,263) | 180,602 | (2,343,661) | - |
| - | - | - | (141,052) |
| - | - | - | (113,417) |
| - | - | - | - |
| - | - | - | (254,469) |
| 2,735,046 | - | 2,735,046 | 422,047 |
| 651,730 | - | 651,730 | - |
| 155,924 | 292,469 | 448,393 | 71,731 |
| 2,962 | - | 2,962 | - |
| 3,545,662 | 292,469 | 3,838,131 | 493,778 |
| 1,021,399 | 473,071 | 1,494,470 | 239,309 |
| 18,662,188 | 13,759,482 | 32,421,670 | (463,697) |
| \$ 19,683,587 | \$ 14,232,553 | \$ 33,916,140 | \$ (224,388) |

City of Mason, Michigan

Governmental Funds Balance Sheet June 30, 2007

| | General Fund | Local Street Fund | Special Assessment Fund | Other Governmental Funds | Total Governmental Funds |
|--|---------------------|-------------------|-------------------------|--------------------------|--------------------------|
| Assets | | | | | |
| Cash and cash equivalents (Note 3) | \$ 1,575,715 | \$ 60,690 | \$ 272,710 | \$ 1,380,861 | \$ 3,289,976 |
| Receivables: | | | | | |
| Property taxes | 29,025 | - | - | - | 29,025 |
| Special assessments | - | - | 1,923,847 | - | 1,923,847 |
| Other governmental units | 105,953 | 19,926 | - | 53,179 | 179,058 |
| Other | 17,629 | - | - | - | 17,629 |
| Prepaid costs and other assets | 10,598 | - | - | - | 10,598 |
| Due from other funds (Note 5) | - | 80,425 | - | - | 80,425 |
| Total assets | \$ 1,738,920 | \$ 161,041 | \$ 2,196,557 | \$ 1,434,040 | \$ 5,530,558 |
| Liabilities and Fund Balances | | | | | |
| Liabilities | | | | | |
| Accounts payable | \$ 4,423 | \$ 5,000 | \$ - | \$ 1,064 | \$ 10,487 |
| Accrued and other liabilities | 51,278 | - | - | - | 51,278 |
| Due to other governmental units | 12,015 | - | - | - | 12,015 |
| Due to other funds (Note 5) | - | - | - | 80,425 | 80,425 |
| Deferred revenue (Note 6) | 9,100 | - | 1,923,850 | - | 1,932,950 |
| Total liabilities | 76,816 | 5,000 | 1,923,850 | 81,489 | 2,087,155 |
| Fund Balances | | | | | |
| Reserved for: | | | | | |
| Construction code activities | 309,212 | - | - | - | 309,212 |
| Cemetery trust | - | - | - | 316,702 | 316,702 |
| Designated for City Hall Project | 500,000 | - | - | - | 500,000 |
| Unreserved, reported in: | | | | | |
| General Fund | 852,892 | - | - | - | 852,892 |
| Special Revenue Funds | - | 156,041 | 272,707 | 993,514 | 1,422,262 |
| Debt Service Funds | - | - | - | 296 | 296 |
| Capital Projects Funds | - | - | - | 42,039 | 42,039 |
| Total fund balances | 1,662,104 | 156,041 | 272,707 | 1,352,551 | 3,443,403 |
| Total liabilities and fund balances | \$ 1,738,920 | \$ 161,041 | \$ 2,196,557 | \$ 1,434,040 | \$ 5,530,558 |

City of Mason, Michigan

Governmental Funds Reconciliation of the Balance Sheet to the Statement of Net Assets (Deficit) June 30, 2007

Fund Balance - Total Governmental Funds \$ 3,443,403

Amounts reported for governmental activities in the statement of net assets (deficit) are different because:

Capital assets used in governmental activities are not financial resources and are not reported in the funds 15,679,698

Internal Service Funds are included as part of governmental activities 777,835

Special assessment receivables are expected to be collected over several years and are not available to pay for current year expenditures 1,923,850

Various receivables are not expected to be collected within 60 days of year end and are not available to pay for current year expenditures 116,533

Accumulated employee paid time off is recorded when earned in the statement of activities (342,573)

Long-term liabilities and accrued interest are not due and payable in the current period and are not reported in the funds (1,915,159)

Net Assets - Governmental Activities **\$ 19,683,587**

City of Mason, Michigan

Governmental Funds Statement of Revenue, Expenditures, and Changes in Fund Balances Year Ended June 30, 2007

| | General Fund | Local Street Fund | Special Assessment Fund | Other Governmental Funds | Total Governmental Funds |
|--|---------------------|----------------------|-------------------------------|--------------------------------|--------------------------------|
| Revenue | | | | | |
| Property taxes | \$ 2,735,046 | \$ - | \$ - | \$ - | \$ 2,735,046 |
| Licenses and permits | 213,951 | - | - | - | 213,951 |
| State-shared revenues and state grants | 653,140 | 114,917 | - | 323,891 | 1,091,948 |
| Local sources | 462,495 | 83,747 | - | - | 546,242 |
| Special assessment revenue | - | - | 161,476 | - | 161,476 |
| Refuse collection | 288,677 | - | - | - | 288,677 |
| Charges for services | 203,656 | 21,942 | - | 8,470 | 234,068 |
| Cable franchise fees | 31,974 | - | - | - | 31,974 |
| Fines and forfeitures | 143,938 | - | - | - | 143,938 |
| Interest and rentals | 81,065 | 3,876 | 14,354 | 102,367 | 201,662 |
| Other | 74,946 | - | - | 1,167 | 76,113 |
| Total revenue | 4,888,888 | 224,482 | 175,830 | 435,895 | 5,725,095 |
| Expenditures | | | | | |
| Current: | | | | | |
| General government | 1,570,525 | - | - | - | 1,570,525 |
| Public safety | 1,538,783 | - | - | - | 1,538,783 |
| Public works | 381,066 | 739,771 | - | 411,553 | 1,532,390 |
| Community and economic development | 6,362 | - | - | - | 6,362 |
| Recreation and culture | 231,638 | - | - | - | 231,638 |
| Capital outlay | 74,164 | - | - | 17,805 | 91,969 |
| Debt service | - | - | 116,680 | 101,940 | 218,620 |
| Total expenditures | 3,802,538 | 739,771 | 116,680 | 531,298 | 5,190,287 |
| Excess of Revenue Over (Under) Expenditures | 1,086,350 | (515,289) | 59,150 | (95,403) | 534,808 |
| Other Financing Sources (Uses) | | | | | |
| Transfers in (Note 5) | 107,600 | 531,941 | - | 237,480 | 877,021 |
| Transfers out (Note 5) | (688,996) | - | (60,235) | (127,790) | (877,021) |
| Financing proceeds from debt | 231,530 | - | - | - | 231,530 |
| Total other financing sources (uses) | (349,866) | 531,941 | (60,235) | 109,690 | 231,530 |
| Net Change in Fund Balances | 736,484 | 16,652 | (1,085) | 14,287 | 766,338 |
| Fund Balances - Beginning of year | 925,620 | 139,389 | 273,792 | 1,338,264 | 2,677,065 |
| Fund Balances - End of year | \$ 1,662,104 | \$ 156,041 | \$ 272,707 | \$ 1,352,551 | \$ 3,443,403 |

City of Mason, Michigan

Governmental Funds Reconciliation of the Statement of Revenue, Expenditures, and Changes in Fund Balance of Governmental Funds to the Statement of Activities Year Ended June 30, 2007

Net Change in Fund Balances - Total Governmental Funds \$ 766,338

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

Governmental funds report capital outlays as expenditures; in the statement of activities, these costs are allocated over their estimated useful lives as depreciation:

| | |
|----------------|-----------|
| Capital outlay | 1,106,031 |
| Depreciation | (710,352) |

| | |
|--|--------|
| Internal Service Funds are included as part of governmental activities | 57,620 |
|--|--------|

| | |
|--|----------|
| Special assessment revenues are recorded in the statement of activities when the assessment is set; they are not reported in the funds until collected or collectible within 60 days of year end | (78,714) |
|--|----------|

| | |
|---|-------|
| Interest expense is recorded in the statement of activities when incurred; it is not reported in the funds until paid or payable within 60 days of year end | 9,865 |
|---|-------|

| | |
|---|---------|
| State-shared revenue reported in the statement of activities that does not provide current financial resources and is not reported as revenue in the governmental funds | (9,353) |
|---|---------|

| | |
|---|---------|
| Repayment of bond principal is an expenditure in the governmental funds, but not in the statement of activities (where it reduces long-term debt) | 130,950 |
|---|---------|

| | |
|--|-----------|
| Bond proceeds are not reported as financing sources on the statement of activities | (231,530) |
|--|-----------|

| | |
|---|-----------------|
| Change in accumulated employee sick and vacation pay, as well as estimated general liability claims, is recorded when earned in the statement of activities | <u>(19,456)</u> |
|---|-----------------|

Change in Net Assets of Governmental Activities **\$ 1,021,399**

City of Mason, Michigan

Proprietary Funds Statement of Net Assets June 30, 2007

| | Business-type Activities | Governmental Activities |
|--|-----------------------------|--|
| | Water and Sewer | Internal Service Fund - Motor Pool |
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents (Note 3) | \$ 4,642,737 | \$ 550,332 |
| Customer receivables | 372,140 | 1,531 |
| Inventory | 28,606 | - |
| Prepaid and other assets | 12,341 | - |
| Total current assets | 5,055,824 | 551,863 |
| Noncurrent assets - Capital assets (Note 4) | 9,406,133 | 236,745 |
| Total assets | 14,461,957 | 788,608 |
| Liabilities | | |
| Current liabilities: | | |
| Accounts payable | 113,090 | 68 |
| Current portion of long-term liabilities: | | |
| Compensated absences | 11,153 | 3,883 |
| Long-term debt (Note 7) | 13,613 | - |
| Total current liabilities | 137,856 | 3,951 |
| Noncurrent liabilities: | | |
| Compensated absences | 46,848 | 6,822 |
| Long-term debt (Note 7) | 44,700 | - |
| Total noncurrent liabilities | 91,548 | 6,822 |
| Total liabilities | 229,404 | 10,773 |
| Net Assets | | |
| Investment in capital assets - Net of related debt | 9,347,820 | 236,745 |
| Unrestricted | 4,884,733 | 541,090 |
| Total net assets | \$ 14,232,553 | \$ 777,835 |

City of Mason, Michigan

Proprietary Funds Statement of Revenue, Expenses, and Changes in Net Assets Year Ended June 30, 2007

| | Business-type Activities | Governmental Activities |
|---------------------------------------|-----------------------------|--|
| | Water and Sewer | Internal Service Fund - Motor Pool |
| Operating Revenue | | |
| User charges | \$ 1,883,326 | \$ 287,560 |
| Interest and penalty charges | 34,427 | - |
| Other charges for services | 209,305 | 9,389 |
| Total operating revenue | 2,127,058 | 296,949 |
| Operating Expenses | | |
| Cost of water produced | 120,563 | - |
| Cost of sewage treatment | 729,768 | - |
| Operation and maintenance | 628,862 | 184,445 |
| Billing and administrative costs | 74,244 | - |
| Depreciation | 389,769 | 74,439 |
| Total operating expenses | 1,943,206 | 258,884 |
| Operating Income | 183,852 | 38,065 |
| Nonoperating Revenue (Expense) | | |
| Investment income | 292,469 | 19,555 |
| Interest expense | (3,250) | - |
| Change in Net Assets | 473,071 | 57,620 |
| Net Assets - Beginning of year | 13,759,482 | 720,215 |
| Net Assets - End of year | \$ 14,232,553 | \$ 777,835 |

City of Mason, Michigan

Proprietary Funds Statement of Cash Flows Year Ended June 30, 2007

| | Business-type Activities | Governmental Activities |
|--|-----------------------------|--|
| | Water and Sewer | Internal Service Fund - Motor Pool |
| Cash Flows from Operating Activities | | |
| Receipts from customers | \$ 2,090,287 | \$ 296,102 |
| Payments to suppliers | (1,014,337) | (142,517) |
| Payments to employees | (537,327) | (40,202) |
| Net cash provided by operating activities | 538,623 | 113,383 |
| Cash Flows from Capital and Related Financing Activities - | | |
| Principal and interest paid on capital debt | (16,282) | - |
| Cash Flows from Investing Activities | | |
| Purchase of capital assets | (815,300) | (75,519) |
| Interest received on investments | 292,469 | 19,555 |
| Net cash used in investing activities | (522,831) | (55,964) |
| Net (Decrease) Increase in Cash and Cash Equivalents | (490) | 57,419 |
| Cash and Cash Equivalents - Beginning of year | 4,643,227 | 492,913 |
| Cash and Cash Equivalents - End of year | \$ 4,642,737 | \$ 550,332 |
| Reconciliation of Operating Income to Net Cash from Operating Activities | | |
| Operating income | \$ 183,852 | \$ 38,065 |
| Adjustments to reconcile operating income to net cash from operating activities: | | |
| Depreciation | 389,769 | 74,439 |
| Changes in assets and liabilities: | | |
| Receivables | (36,771) | (850) |
| Due from other funds | 1,200 | - |
| Due from other governmental units | 1,018 | - |
| Inventory | (52) | - |
| Prepaid and other assets | 10,676 | - |
| Accounts payable | 61,426 | 68 |
| Accrued and other liabilities | (72,495) | 1,661 |
| Net cash provided by operating activities | \$ 538,623 | \$ 113,383 |

Noncash Capital and Related Financing Activities – There were no noncash financing activities during the year ended June 30, 2007.

City of Mason, Michigan

Fiduciary Funds Statement of Fiduciary Assets and Liabilities June 30, 2007

| | <u>Agency Funds</u> |
|--|-----------------------------|
| Assets - Cash and cash equivalents (Note 3) | <u>\$ 25,778</u> |
| Liabilities | |
| Accrued and other liabilities | \$ 25,446 |
| Due to other governmental units | <u>332</u> |
| Total liabilities | <u>\$ 25,778</u> |

City of Mason, Michigan

Component Units Statement of Net Assets (Deficit) June 30, 2007

| | Local Development Finance Authority | Downtown Development Authority | Economic Development Corporation | Total |
|--|--|--------------------------------------|--|---------------------|
| Assets | | | | |
| Cash and cash equivalents (Note 3) | \$ 905,231 | \$ 105,415 | \$ 20,351 | \$ 1,030,997 |
| Receivables: | | | | |
| Taxes | - | 11,748 | - | 11,748 |
| Other | - | 1,292 | - | 1,292 |
| Due from other governmental units | 21,596 | - | - | 21,596 |
| Prepaid costs and other assets | - | - | - | - |
| Net capital assets (Note 4) | <u>213,175</u> | <u>-</u> | <u>-</u> | <u>213,175</u> |
| Total assets | 1,140,002 | 118,455 | 20,351 | 1,278,808 |
| Liabilities | | | | |
| Accounts payable | 3,899 | - | - | 3,899 |
| Accrued and other liabilities | 8,289 | - | - | 8,289 |
| Due to other governmental units | - | 21,596 | - | 21,596 |
| Current portion of long-term debt (Note 7) | 334,448 | - | - | 334,448 |
| Noncurrent liabilities - Long-term debt - Net of current portion (Note 7) | <u>1,134,964</u> | <u>-</u> | <u>-</u> | <u>1,134,964</u> |
| Total liabilities | <u>1,481,600</u> | <u>21,596</u> | <u>-</u> | <u>1,503,196</u> |
| Net Assets (Deficit) | | | | |
| Invested in capital assets - Net of related debt | 213,175 | - | - | 213,175 |
| Unrestricted (deficit) | <u>(554,773)</u> | <u>96,859</u> | <u>20,351</u> | <u>(437,563)</u> |
| Total net assets (deficit) | <u>\$ (341,598)</u> | <u>\$ 96,859</u> | <u>\$ 20,351</u> | <u>\$ (224,388)</u> |

City of Mason, Michigan

| | Expenses | Program Revenues | | |
|-------------------------------------|-------------------|----------------------|------------------------------------|----------------------------------|
| | | Charges for Services | Operating Grants and Contributions | Capital Grants and Contributions |
| Local Development Finance Authority | \$ 141,052 | \$ - | \$ - | \$ - |
| Downtown Development Authority | 113,417 | - | - | - |
| Economic Development Corporation | - | - | - | - |
| Total component units | <u>\$ 254,469</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> |

General revenues:

Property taxes

Investment earnings

Total general revenues

Change in Net Assets

Net Assets (Deficit) - Beginning of year

Net Assets (Deficit) - End of year

**Component Units
Statement of Activities
June 30, 2007**

| Net (Expense) Revenue and Changes in Net Assets | | | |
|---|--------------------------------------|--|---------------------|
| Local | | | |
| Development Finance Authroity | Downtown Development Authority | Economic Development Corporation | Total |
| \$ (141,052) | \$ - | \$ - | \$ (141,052) |
| - | (113,417) | - | (113,417) |
| - | - | - | - |
| (141,052) | (113,417) | - | (254,469) |
| 349,097 | 72,950 | - | 422,047 |
| 67,223 | 3,506 | 1,002 | 71,731 |
| 416,320 | 76,456 | 1,002 | 493,778 |
| 275,268 | (36,961) | 1,002 | 239,309 |
| (616,866) | 133,820 | 19,349 | (463,697) |
| \$ (341,598) | \$ 96,859 | \$ 20,351 | \$ (224,388) |

Note I - Summary of Significant Accounting Policies

The accounting policies of the City of Mason, Michigan (the "City") conform to accounting principles generally accepted in the United States of America (GAAP) as applicable to governmental units. The following is a summary of the significant accounting policies used by the City of Mason, Michigan:

Reporting Entity

The City of Mason is governed by an elected seven-member council. The accompanying financial statements present the City and its component units, entities for which the City is considered to be financially accountable. Each discretely presented component unit is reported in a separate column in the government-wide financial statements to emphasize that it is legally separate from the City (see discussion below for description).

The criteria established by GASB for determining which of the City's various organizations and activities are to be included in the reporting entity's financial statements include oversight responsibility, scope of public service, and special financial relationships. On this basis, the financial statements of certain other governmental organizations are not included in the financial statements of the City.

Blended Component Units

The City of Mason has one blended component unit, the Mason Building Authority, which was established for the purpose of acquiring, furnishing, equipping, owning, improving, enlarging, operating, and maintaining a building or buildings, and automobile parking lots or structures, recreational facilities and the necessary site or sites therefore, and the payment of the bond principal and interest for any related debt incurred. The Mason Building Authority is blended with the primary government in the Mason Building Authority Debt Service Fund, in conformity with GASB 14, as the component unit provides services entirely to the primary government.

Discretely Presented Component Units

The following entities are listed as discretely presented component units of the City in the component unit column to emphasize their legally separate status from the primary government. The City is financially accountable, and exclusion from the government-wide financial statements would be misleading or incomplete. Separate financial statements for the component units are not available.

Note I - Summary of Significant Accounting Policies (Continued)

The Downtown Development Authority (DDA) was established in order to work in cooperation with the City Council in order to correct and prevent deterioration of the downtown district of the City, to promote economic growth and revitalization, to encourage historic preservation, to address problems of urban decline, and to strengthen existing areas and encourage new private development within the downtown district. The DDA's governing body, which consists of the City mayor and eight other individuals, is appointed by the City Council. Additionally, the DDA's budget is subject to approval by the City Council. The DDA may issue debt payable solely from tax increment revenues. The full faith and credit of the City may be given for the debt of the DDA.

The Local Development Finance Authority (LDFA) was established by the City of Mason and the Township of VeVay as a condition of an agreement to transfer approximately 134 acres of land from the Township to the City. The purpose of the LDFA is to help stimulate economic growth, improve employment, stimulate new private investment in the City of Mason and VeVay Township, and to broaden the local tax base.

The Economic Development Corporation was created to provide means and methods for the encouragement and assistance of industrial and commercial enterprises in relocating, purchasing, constructing, improving, and expanding within the City so as to provide needed services and facilities of such enterprises to the residents of the City. The Corporation's governing body, which consists of nine individuals, is appointed by the City administrator with the approval of the City Council.

Government-wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets (deficit) and the statement of activities) report information on all of the nonfiduciary activities of the City of Mason and its component units. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, normally supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for services. The primary government of the City of Mason is reported separately from certain legally separate component units for which the City of Mason is financially accountable.

Note I - Summary of Significant Accounting Policies (Continued)

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

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual Enterprise Funds are reported as separate columns in the fund financial statements.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. In the individual fund statements and schedules, the proprietary funds and the fiduciary fund financial statements are also reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are reported when a liability is incurred, regardless of the timing of related cash flows. 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. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available if it is collectible within the current period or soon enough thereafter to pay liabilities of the current period. Expenditures are recorded when a liability is incurred, as under accrual accounting. However, expenditures for debt service, compensated absences, and claims and judgments are recorded only when payment is due.

Property taxes, franchise fees, licenses, and interest associated with the current fiscal period are all considered to be susceptible to accrual and have been recognized as revenues of the current fiscal period. 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 City of Mason.

Note I - Summary of Significant Accounting Policies (Continued)

The City of Mason reports the following major governmental funds:

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

Local Street Fund - The Local Street Fund accounts for local street improvement and resurfacing projects.

Special Assessment Fund - The Special Assessment Fund accounts for the payment of interest and principal on all special assessment debt.

The City of Mason reports the following major proprietary fund:

Water and Sewer Fund - The Water and Sewer Fund accounts for utility operations that are financed primarily by user charges.

Additionally, the City of Mason reports the following fund types:

Special Revenue Funds - The Special Revenue Funds are used to finance particular activities and are created out of receipts of specific taxes or other earmarked revenues. Such funds are authorized by statutory provisions to pay for certain activities with some special form of continuing revenues.

Debt Service Funds - The Debt Service Funds are used to account for payment of interest and principal on general obligation debt of governmental funds.

Capital Projects Funds - The Capital Projects Funds account for resources expended to acquire assets of a relatively permanent nature.

Permanent Funds - The Permanent Funds account for resources which are restricted, and only the income earned may be apportioned toward expenditures.

Internal Services Fund - The Internal Services Fund is used to account for Motor Vehicles Pool Services provided to other departments on a cost reimbursement basis.

Fiduciary Funds - The Fiduciary Funds account for resources reserved and held by a governmental unit as the trustee or as the agent for others.

Note I - Summary of Significant Accounting Policies (Continued)

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989 generally are followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The City of Mason has elected not to follow subsequent private sector guidance.

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements.

Amounts reported as program revenue include: (1) charges to customers or applicants for goods, services, or privileges provided; (2) operating grants and contributions; and (3) capital grants and contributions, including special assessments. All taxes are reported as general revenue.

Proprietary funds distinguish operating revenue and expenses from nonoperating items. Operating revenue and expenses generally result from provided services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Operating expense for enterprise funds and Internal Services 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.

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

Property Tax Revenue - Properties are assessed as of December 31 and the related property taxes become a lien on July 1 of the following year. These taxes are due on August 31, with the final collection date of February 28 before they are returned to the County as delinquent.

The 2006 taxable valuation of the City totaled \$205 million, on which ad valorem taxes levied consisted of 13.250 mills for operating purposes. This resulted in \$2.7 million for operating purposes. These amounts are recognized in the General Fund financial statements as tax revenue.

Note I - Summary of Significant Accounting Policies (Continued)

Assets, Liabilities, and Net Assets or Equity

Cash and Cash Equivalents - Cash and cash equivalents include cash on hand, demand deposits, and short-term investments with a maturity of three months or less when acquired. Investments are stated at fair value.

Receivables and Payables - In general, outstanding balances between funds are reported as "due to/from other funds." Any residual balances outstanding between the governmental activities and the business-type activities are reported in the government-wide financial statements as "internal balances."

Receivables have been recognized for all significant amounts due to the City. No allowances have been made for noncollectible accounts because most delinquent receivables can be added to the tax roll if they remain unpaid and become a lien against the property.

Inventories - Inventories of materials and supplies are stated at the lower of cost (first-in, first-out) or market. The cost is accounted for as an expenditure at the time the inventories are used.

Capital Assets - Capital assets, which include property, plant, and equipment, and infrastructure assets (e.g., bridges, sidewalks, and similar items since the adoption of GASB 34), are reported in the applicable governmental or business-type activities column in the government-wide financial statements. Capital assets are defined by the City of Mason as assets with an initial individual cost of more than \$2,500 and an estimated useful life in excess of one year.

All capital assets are valued at historical cost or estimated historical cost if actual cost is not available. 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 assets or materially extend assets lives are not capitalized.

Depreciation of all exhaustible capital assets used is charged as an expense against their operations in government-wide statements and all proprietary financial statements. Accumulated depreciation is reported on the government-wide and proprietary statement of net assets. Straight-line depreciation methods are applied over the estimated useful lives of capital assets.

Note I - Summary of Significant Accounting Policies (Continued)

Capital assets are depreciated using the straight-line method over the following useful lives:

| | |
|----------------------------|-------------|
| Land improvements | 10-40 years |
| Buildings and improvements | 10-40 years |
| Equipment | 5-20 years |
| Vehicles | 3-10 years |
| Utility systems | 20-67 years |
| Infrastructure | 33-40 years |

Compensated Absences (Vacation and Sick Leave) - It is the City's policy to permit employees to accumulate earned but unused sick and vacation pay benefits. City employees are granted vacation amounts based on length of service. Sick pay is earned at the rate of eight hours per month. The City's policy provides for payment of unused vacation, but not sick pay, to terminated employees. Retiring employees are paid for unused vacation and a portion of sick pay. All vacation and sick pay is accrued when incurred in the government-wide and proprietary fund financial statements. A liability for these amounts is reported in the governmental funds only when they have matured or come due for payment, generally when an individual's employment has terminated as of year end.

Long-term Obligations - In the government-wide financial statements and the 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 assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest 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.

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 are reported as other financing uses. Issuance costs are reported as debt service expenditures.

Fund Equity - In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

Note 1 - Summary of Significant Accounting Policies (Continued)

Use of Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

Note 2 - Stewardship, Compliance, and Accountability

Budgetary Information - Annual budgets are adopted on a basis consistent with accounting principles generally accepted in the United States of America for the General Fund and Special Revenue Funds. All annual appropriations lapse at fiscal year end.

The budget document presents information by fund, function, department, and line items. The legal level of budgetary control adopted by the governing body is the activity level.

Amounts encumbered for purchase orders, contracts, etc., are not tracked during the year. Budget appropriations are considered to be spent once the goods are delivered or the services rendered.

Excess of Expenditures Over Appropriations in Budgeted Funds - The City had an expenditure budget variance in the Fire Department within the General Fund. Budgeted expenditures were \$279,210, while actual expenditures were \$477,636. The Fire Department purchased a new tanker truck near the end of the fiscal year, and while this expenditure was approved by the City Council before the end of the year, a budget amendment was unable to be prepared by June 30, 2007.

Fund Deficits - The Local Development Finance Authority had an unrestricted net asset deficit at the government-wide basis at year end of \$554,773; however, on the modified accrual basis of accounting which is used on the fund based statements, there was not a deficit balance. The Local Development Finance Authority will capture property taxes in the future to eliminate this deficit.

Note 3 - Deposits and Investments

Michigan Compiled Laws Section 129.91 (Public Act 20 of 1943, as amended) authorizes local governmental units to make deposits and invest in the accounts of federally insured banks, credit unions, and savings and loan associations that have offices in Michigan. The local unit is allowed to invest in bonds, securities, and other direct obligations of the United States or any agency or instrumentality of the United States; repurchase agreements; bankers' acceptances of United States banks; commercial paper rated within the two highest classifications, which matures not more than 270 days after the date of purchase; obligations of the State of Michigan or its political subdivisions, which are rated as investment grade; and mutual funds composed of investment vehicles that are legal for direct investment by local units of government in Michigan.

The City has designated three banks for the deposit of its funds. The investment policy adopted by the board is in accordance with Public Act 196 of 1997, as amended. The City's policy further restricts investment purchases to banks that maintain a principal branch within the City of Mason, and that commercial paper must be within the highest classification established by two or more standard rating services. In addition, the City's investment policy indicates that the treasurer shall diversify the investments by security type and institution. With the exception of U.S. Treasury securities and authorized investment pools, no more than 60 percent of the total investment portfolio will be invested in a single security type or with a single financial institution. Also, the City's securities purchased will have a maximum maturity of no longer than 270 days.

The City's cash and investments are subject to custodial credit risk, which is examined in more detail below:

Custodial Credit Risk of Bank Deposits

Custodial credit risk is the risk that in the event of a bank failure, the City's deposits may not be returned to it. At year end, the City and the component units of the City had \$8,805,012 and \$1,030,997 of bank deposits (certificates of deposit, checking and savings accounts), respectively, of which \$500,000 and \$300,000 is covered by federal depository insurance, respectively, and the remainder is uninsured and uncollateralized. The City and the component units of the City believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all deposits. As a result, the City and the component units of the City evaluate each financial institution with which they deposits funds and assess the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

City of Mason, Michigan

Notes to Financial Statements June 30, 2007

Note 4 - Capital Assets

Capital asset activity of the primary government's governmental and business-type activities and component units was as follows:

| Governmental Activities | Balance July 1, 2006, as restated (Note 11) | Reclassifi- cations | Additions | Disposals | Balance June 30, 2007 |
|---------------------------------------|--|------------------------|-------------------|-------------|--------------------------|
| Capital assets not being depreciated: | | | | | |
| Land | \$ 1,426,251 | \$ - | \$ - | \$ - | \$ 1,426,251 |
| Construction in progress | 960,050 | (960,050) | - | - | - |
| Subtotal | 2,386,301 | (960,050) | - | - | 1,426,251 |
| Capital assets being depreciated: | | | | | |
| Land improvements | 793,000 | - | 82,043 | - | 875,043 |
| Buildings and improvements | 1,535,960 | - | - | - | 1,535,960 |
| Infrastructure | 19,216,358 | 960,050 | 682,376 | - | 20,858,784 |
| Vehicles and equipment | 2,121,002 | - | 363,369 | (39,183) | 2,445,188 |
| Subtotal | 23,666,320 | 960,050 | 1,127,788 | (39,183) | 25,714,975 |
| Accumulated depreciation: | | | | | |
| Land improvements | 417,933 | - | 26,676 | - | 444,609 |
| Buildings and improvements | 614,511 | - | 33,297 | - | 647,808 |
| Infrastructure | 7,523,097 | - | 616,966 | - | 8,140,063 |
| Vehicles and equipment | 1,923,634 | - | 107,852 | (39,183) | 1,992,303 |
| Subtotal | 10,479,175 | - | 784,791 | (39,183) | 11,224,783 |
| Net capital assets being depreciated | 13,187,145 | 960,050 | 342,997 | - | 14,490,192 |
| Net capital assets | <u>\$ 15,573,446</u> | <u>\$ -</u> | <u>\$ 342,997</u> | <u>\$ -</u> | <u>\$ 15,916,443</u> |

City of Mason, Michigan

Notes to Financial Statements June 30, 2007

Note 4 - Capital Assets (Continued)

| Business-type Activities | Balance July 1, 2006 | Reclassifi- cations | Additions | Disposals | Balance June 30, 2007 |
|---|-------------------------|------------------------|--------------------|-------------|--------------------------|
| Capital assets not being depreciated: | | | | | |
| Land | \$ 25,609 | \$ - | \$ - | \$ - | \$ 25,609 |
| Construction in progress | <u>1,039,002</u> | <u>(965,391)</u> | <u>639,752</u> | <u>-</u> | <u>713,363</u> |
| Subtotal | 1,064,611 | (965,391) | 639,752 | - | 738,972 |
| Capital assets being depreciated: | | | | | |
| Buildings and improvements | 455,637 | - | - | - | 455,637 |
| Infrastructure | <u>12,746,179</u> | <u>965,391</u> | <u>175,548</u> | <u>-</u> | <u>13,887,118</u> |
| Subtotal | 13,201,816 | 965,391 | 175,548 | - | 14,342,755 |
| Accumulated depreciation: | | | | | |
| Buildings and improvements | 153,202 | - | 80,439 | - | 233,641 |
| Infrastructure | <u>5,132,623</u> | <u>-</u> | <u>309,330</u> | <u>-</u> | <u>5,441,953</u> |
| Subtotal | <u>5,285,825</u> | <u>-</u> | <u>389,769</u> | <u>-</u> | <u>5,675,594</u> |
| Net capital assets being depreciated | <u>7,915,991</u> | <u>965,391</u> | <u>(214,221)</u> | <u>-</u> | <u>8,667,161</u> |
| Net capital assets | <u>\$ 8,980,602</u> | <u>\$ -</u> | <u>\$ 425,531</u> | <u>\$ -</u> | <u>\$ 9,406,133</u> |
| | | | | | |
| Component Units | Balance July 1, 2006 | Reclassifi- cations | Additions | Disposals | Balance June 30, 2007 |
| Capital assets being depreciated - Equipment | \$ 710,587 | \$ - | \$ - | \$ - | \$ 710,587 |
| Accumulated depreciation - Equipment | <u>426,353</u> | <u>-</u> | <u>71,059</u> | <u>-</u> | <u>497,412</u> |
| Net capital assets | <u>\$ 284,234</u> | <u>\$ -</u> | <u>\$ (71,059)</u> | <u>\$ -</u> | <u>\$ 213,175</u> |

City of Mason, Michigan

Notes to Financial Statements June 30, 2007

Note 4 - Capital Assets (Continued)

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

Governmental activities:

| | | |
|-------------------------------|----|----------------|
| General government | \$ | 113,738 |
| Public safety | | 49,505 |
| Public works | | 617,591 |
| Recreation and culture | | <u>3,957</u> |
| Total governmental activities | \$ | <u>784,791</u> |
| Business-type activities | \$ | <u>389,769</u> |
| Component units | \$ | <u>71,059</u> |

Subsequent Events

To comply with MDEQ's mandate to remove radium from drinking water, subsequent to year end, the City entered into an agreement to complete a water treatment plant and water main project over the next several years. The total cost of the project is estimated to be approximately \$8.9 million. The City has awarded bids amounting to \$7.4 million to various contractors, but no signed contracts exist. Subsequent to June 30, 2007, the City has obtained financing through the Michigan State Drinking Water Revolving Loan Fund in an amount not to exceed \$8.0 million for the funding of a water treatment plant and water main project.

Note 5 - Interfund Receivables, Payables, and Transfers

The composition of interfund balances is as follows:

| Receivable Fund | Payable Fund | Amount |
|--------------------------------|-----------------------------|-----------|
| Due to/from Other Funds | | |
| Local Street Fund | Nonmajor governmental funds | \$ 80,425 |

Note 5 - Interfund Receivables, Payables, and Transfers (Continued)

These balances result from the time lag between the dates that goods and services are provided or reimbursable expenditures occur, transactions are recorded in the accounting system, and payments between funds are made.

Interfund transfers reported in the fund financial statements are comprised of the following:

| Fund Providing Resources | Fund Receiving Resources | Amount |
|-----------------------------|-----------------------------|-------------------|
| Interfund Transfers | | |
| General Fund | Local Street | \$ 451,516 |
| General Fund | Nonmajor governmental funds | 237,480 |
| Special Assessment Fund | General Fund | 60,235 |
| Nonmajor governmental funds | General Fund | 37,000 |
| Nonmajor governmental funds | Local Street | 80,425 |
| Nonmajor governmental funds | Nonmajor governmental funds | <u>10,365</u> |
| Total | | <u>\$ 877,021</u> |

The transfer from the General Fund to the Local Street Fund represents the use of tax revenue for street construction and repair. The transfer from the General Fund to the nonmajor governmental funds represents transfers for various debt service payments. The transfer from the nonmajor governmental funds to the Local Street Fund represents application of residual funds toward local street construction and repair. The transfer from nonmajor governmental funds to the General Fund was for the reimbursement of debt service payments covered by the General Fund.

Note 6 - Deferred Revenue

Governmental funds report deferred revenue in connection with receivables for revenue that is not considered to be available to liquidate liabilities of the current period. Governmental funds and governmental activities also defer revenue recognition in connection with resources that have been received but not yet earned. At the end of the current fiscal year, the various components of deferred revenue are as follows:

| | Unavailable | Unearned | Total |
|-------------------------------|---------------------|-----------------|---------------------|
| Special assessments and other | <u>\$ 1,923,850</u> | <u>\$ 9,100</u> | <u>\$ 1,932,950</u> |

Note 7 - Long-term Debt

The City issued bonds to provide for the acquisition and construction of major capital facilities. General obligation bonds are direct obligations and pledge the full faith and credit of the City. Special assessment bonds provide for capital improvements that benefit specific properties, and will be repaid from amounts levied against those properties that benefited from the construction. In the event that a deficiency exists because of unpaid or delinquent special assessments at the time a debt service payment is due, the City is obligated to provide resources to cover the deficiency until other resources (such as tax sale proceeds or a re-assessment of the district) are reviewed.

City of Mason, Michigan

Notes to Financial Statements June 30, 2007

Note 7 - Long-term Debt (Continued)

Long-term obligations are summarized as follows:

| | Interest Rate Ranges | Principal Maturity Ranges | Beginning Balance | Additions (Reductions) | Ending Balance | Due Within One Year |
|--|----------------------------|---------------------------------|----------------------|---------------------------|---------------------|------------------------|
| Governmental Activities | | | | | | |
| General Obligations: | | | | | | |
| Dart National Bank Loan - Computer System: | | | | | | |
| Amount of issue - \$247,000 | 4.90% | \$21,000- \$23,000 | \$ 64,000 | \$ (20,000) | \$ 44,000 | \$ 21,000 |
| Maturing through 2009 | | | | | | |
| Dart National Bank Loan - Fire Truck: | | | | | | |
| Amount of issue - \$231,530 | 4.50% | \$41,275- \$50,800 | - | 231,530 | 231,530 | 44,408 |
| Maturing through 2012 | | | | | | |
| Dart National Bank Loan - Land Purchase: | | | | | | |
| Amount of issue - \$325,877 | 4.80% | \$20,261- \$29,828 | 241,951 | (19,359) | 222,592 | 20,261 |
| Maturing through 2016 | | | | | | |
| Mason State Bank Loan - Land Purchase: | | | | | | |
| Amount of issue - \$115,500 | 4.65% | \$6,890- \$10,384 | 91,936 | (6,591) | 85,345 | 6,890 |
| Maturing through 2017 | | | | | | |
| 1997 Building Authority Bonds | | | | | | |
| Amount of issue - \$450,000 | 3.85%- 5.15% | \$20,000- \$40,000 | 355,000 | (20,000) | 335,000 | 20,000 |
| Maturing through 2018 | | | | | | |
| Special Assessment Obligation Bonds: | | | | | | |
| 1996 Special Assessment | | | | | | |
| Amount of issue - \$205,000 | 4.45%- 5.50% | \$15,000 | 75,000 | (15,000) | 60,000 | 15,000 |
| Maturing through 2010 | | | | | | |
| 1998 Special Assessment | | | | | | |
| Amount of issue - \$90,000 | 4.90% | \$7,000 | 48,000 | (6,000) | 42,000 | 7,000 |
| Maturing through 2012 | | | | | | |
| 1999 Special Assessment | | | | | | |
| Amount of issue - \$52,000 | 4.90% | \$4,000- \$5,000 | 34,000 | (4,000) | 30,000 | 4,000 |
| Maturing through 2013 | | | | | | |
| 2001 Special Assessment | | | | | | |
| Amount of issue - \$205,000 | 4.30%- 5.00% | \$10,000- \$20,000 | 140,000 | (20,000) | 120,000 | 15,000 |
| Maturing through 2007 | | | | | | |
| 2006 Special Assessment | | | | | | |
| Amount of issue - \$750,000 | 3.60%- 4.55% | \$20,000- \$55,000 | 750,000 | (20,000) | 730,000 | 40,000 |
| Maturing through 2014 | | | | | | |
| Total governmental activities | | | <u>\$ 1,799,887</u> | <u>\$ 100,580</u> | <u>\$ 1,900,467</u> | <u>\$ 193,559</u> |

City of Mason, Michigan

Notes to Financial Statements June 30, 2007

Note 7 - Long-term Debt (Continued)

| | Interest Rate Ranges | Principal Maturity Ranges | Beginning Balance | Additions (Reductions) | Ending Balance | Due Within One Year |
|---|----------------------------|---------------------------------|----------------------|---------------------------|----------------|------------------------|
| Business-type Activities | | | | | | |
| 2005 Water and Sewage Disposal System | | | | | | |
| Revenue Refunding Bonds | | | | | | |
| Amount of issue - \$100,000 | | | | | | |
| 4.50% | \$13,027- | \$ 71,345 | \$ (13,032) | \$ 58,313 | \$ 13,613 | |
| | | \$15,572 | | | | |
| Maturing through 2011 | | | | | | |
| Total business-type and governmental activities | | | | | | |
| | | \$ 1,871,232 | \$ 87,548 | \$ 1,958,780 | \$ 207,172 | |
| Component Units | | | | | | |
| General Obligations: | | | | | | |
| 1992 Local Development Finance Authority | | | | | | |
| Amount of issue: \$425,000 | | | | | | |
| 5.75%- | \$25,000- | \$ 235,000 | \$ (25,000) | \$ 210,000 | \$ 25,000 | |
| 8.00% | \$35,000 | | | | | |
| Maturing through 2013 | | | | | | |
| 1994 Local Development Finance Authority | | | | | | |
| Amount of issue - \$1,125,000 | | | | | | |
| 6.10%- | \$85,000 | 340,000 | (85,000) | 255,000 | 85,000 | |
| 7.65% | | | | | | |
| Maturing through 2010 | | | | | | |
| 1998 Local Development Finance Authority | | | | | | |
| Michigan Jobs Commission, Series A | | | | | | |
| Amount of issue - \$1,386,000 | | | | | | |
| 0.00% | \$106,615 | 639,693 | (106,615) | 533,078 | 106,615 | |
| Maturing through 2011 | | | | | | |
| 1998 Local Development Finance Authority | | | | | | |
| Michigan Jobs Commission, Series B | | | | | | |
| Amount of issue - \$1,414,000 | | | | | | |
| 1.48% | \$117,833 | 589,167 | (117,833) | 471,334 | 117,833 | |
| Maturing through 2011 | | | | | | |
| Total component units | | | | | | |
| | | \$ 1,803,860 | \$ (334,448) | \$ 1,469,412 | \$ 334,448 | |

Note 7 - Long-term Debt (Continued)

Annual debt service requirements to maturity for all debt are as follows:

| | Governmental Activities | | | Business-type Activities | | | Component Unit Activities | | |
|-----------|-------------------------|-------------------|---------------------|--------------------------|-----------------|------------------|---------------------------|------------------|---------------------|
| | Principal | Interest | Total | Principal | Interest | Total | Principal | Interest | Total |
| 2008 | \$ 193,559 | \$ 84,439 | \$ 277,998 | \$ 13,613 | \$ 2,668 | \$ 16,281 | \$ 334,448 | \$ 30,778 | \$ 365,226 |
| 2009 | 208,965 | 75,462 | 284,427 | 14,241 | 2,040 | 16,281 | 334,448 | 23,221 | 357,669 |
| 2010 | 199,448 | 65,849 | 265,297 | 14,892 | 1,390 | 16,282 | 339,450 | 15,489 | 354,939 |
| 2011 | 203,102 | 56,888 | 259,990 | 15,567 | 710 | 16,282 | 254,450 | 7,582 | 262,032 |
| 2012 | 180,064 | 48,189 | 228,253 | - | - | - | 136,616 | 5,610 | 142,226 |
| 2013-2017 | 630,329 | 138,537 | 768,876 | - | - | - | 70,000 | 4,620 | 74,620 |
| 2018-2022 | 285,000 | 22,680 | 307,680 | - | - | - | - | - | - |
| Total | <u>\$ 1,900,467</u> | <u>\$ 492,044</u> | <u>\$ 2,392,521</u> | <u>\$ 58,313</u> | <u>\$ 6,808</u> | <u>\$ 65,126</u> | <u>\$ 1,469,412</u> | <u>\$ 87,300</u> | <u>\$ 1,556,712</u> |

Note 8 - Risk Management

The City is exposed to various risks of loss related to property loss, torts, errors and omissions, and employee injuries (workers' compensation), as well as medical benefits provided to employees. The City has purchased commercial insurance for medical benefit claims, and participates in the Michigan Municipal League risk pool program for claims relating to workers' compensation, and in the Michigan Municipal Risk Management Authority for claims relating to property loss, torts, and errors and omissions. Settled claims relating to the commercial insurance have not exceeded the amount of insurance coverage in any of the past three fiscal years.

The Michigan Municipal League risk pool program operates as a common risk-sharing management program for local units of government in Michigan; member premiums are used to purchase commercial excess insurance coverage and to pay member claims in excess of deductible amounts.

The Michigan Municipal Risk Management Authority operates as an insurance purchasing pool for local units of government in Michigan. The plan purchases commercial insurance on behalf of its members at a lower cost than would be available on an individual basis.

Note 9 - Defined Benefit Pension Plan

Plan Description

The City participates in the Municipal Employees' Retirement System, an agent multiple-employer defined benefit pension plan that covers all employees of the City. The system provides retirement, disability, and death benefits to plan members and their beneficiaries. The Municipal Employees' Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the system. That report may be obtained by writing to the system at 1134 Municipal Way, Lansing, MI 48917.

Funding Policy

The obligation to contribute to and maintain the system for these employees was established by negotiation with the City's competitive bargaining units and requires a contribution from the employees, based on actuarial calculations.

Annual Pension Cost

For the year ended June 30, 2007, the City's annual pension cost of \$159,731 for the plan was equal to the City's required and actual contribution. The annual required contribution was determined as part of an actuarial valuation at December 31, 2004, using the entry age actuarial cost method. Significant actuarial assumptions used include (a) an 8 percent investment rate of return, (b) projected salary increases of 4.5 percent per year attributable to inflation, (c) additional projected salary increases ranging from 0 percent to 8.40 percent per year, depending on age, attributable to seniority/merit, and (d) postretirement benefit increases of 2.5 percent annually. The actuarial value of assets is determined on the basis of a method that calculates expected investment income at the valuation rate of return and adds a portion of the difference between the expected investment income and actual investment income earned on a market value basis. The difference in investment income between expected return and market return is recognized over a 10-year period at the rate of 10 percent per year. The unfunded actuarial liability is being amortized as a level of percentage of payroll over a period of 29 years.

City of Mason, Michigan

Notes to Financial Statements June 30, 2007

Note 9 - Defined Benefit Pension Plan (Continued)

Three-year trend information:

| | Fiscal Year Ended June 30 | | |
|--------------------------------------|-----------------------------|---------------|---------------|
| | 2005 | 2006 | 2007 |
| Annual pension costs (APC) | \$ 127,453 | \$ 137,330 | \$ 159,731 |
| Percentage of APC contributed | 100% | 100% | 100% |
| Net pension obligation | \$ - | \$ - | \$ - |
| | Valuation as of December 31 | | |
| | 2004 | 2005 | 2006 |
| Actuarial value of assets | \$ 8,769,133 | \$ 9,198,600 | \$ 9,789,872 |
| Actuarial accrued liability (AAL) | \$ 10,254,712 | \$ 10,865,189 | \$ 11,418,642 |
| Unfunded AAL (UAAL) | \$ 1,485,579 | \$ 1,666,589 | \$ 1,628,770 |
| Funded ratio | 86% | 85% | 86% |
| Covered payroll | \$ 1,949,928 | \$ 1,987,320 | \$ 2,037,410 |
| UAAL as a percent of covered payroll | 76% | 84% | 80% |

Note 10 - Other Postemployment Benefits

The City has elected to provide postemployment health benefits to certain retirees and their beneficiaries. The City pays the full cost of coverage for these benefits. Also, retirees can purchase coverage for their dependents at the City's group rates. Currently, 19 retirees are eligible for postemployment health benefits. For the fiscal year ended June 30, 2007, the City made payments for postemployment health benefit premiums of \$47,568. The City obtains healthcare coverage through private insurers.

Upcoming Reporting Change

The Governmental Accounting Standards Board has recently released Statement Number 45, *Accounting and Reporting by Employers for Postemployment Benefits Other Than Pensions*. The new pronouncement provides guidance for local units of government in recognizing the cost of retiree healthcare, as well as any "other" postemployment benefits (other than pensions).

The new rules will cause the government-wide financial statements to recognize the cost of providing retiree healthcare coverage over the working life of the employee, rather than at the time the healthcare premiums are paid. The new pronouncement is effective for the year ending June 30, 2010.

City of Mason, Michigan

Notes to Financial Statements June 30, 2007

Note 11 - Prior Period Adjustments

During the year ended June 30, 2007, the City of Mason fully implemented GASB 34, and recorded the amount of infrastructure and roads that the City has constructed, or have been dedicated by various subdivisions within the City of Mason, retroactively back to 1980. The prior period adjustment reflects the net book value of the assets as follows:

Governmental Activities

| | |
|--|----------------------|
| Net assets as stated June 30, 2006 | \$ 9,155,851 |
| Adjustment to record infrastructure assets | 16,964,841 |
| Adjustment to record infrastructure accumulated depreciation | <u>(7,458,504)</u> |
| Net assets as restated June 30, 2006 | <u>\$ 18,662,188</u> |

Note 12 - Construction Code Fees

The City oversees building construction, in accordance with the State's Construction Code Act, including inspection of building construction and renovation to ensure compliance with the building codes. The City charges fees for these services. Beginning January 1, 2000, the law requires that collection of these fees be used only for construction code costs, including an allocation of estimated overhead costs. A summary of the activity since January 1, 2000 is as follows:

| | |
|--------------------------------------|-------------------|
| Surplus at July 1, 2006 | \$ 190,977 |
| Current year building permit revenue | 201,706 |
| Related expenses - Direct costs | (75,883) |
| Related expenses - Indirect costs | <u>(7,588)</u> |
| Cumulative surplus at June 30, 2007 | <u>\$ 309,212</u> |

Required Supplemental Information

City of Mason, Michigan

Required Supplemental Information Budgetary Comparison Schedule - General Fund Year Ended June 30, 2007

| | Original Budget | Amended Budget | Actual | Variance with Amended Budget Favorable (Unfavorable) |
|--|--------------------|-------------------|--------------|--|
| Revenues | | | | |
| Property taxes | \$ 2,729,375 | \$ 2,693,915 | \$ 2,735,046 | 41,131 |
| Licenses and permits | 33,560 | 197,515 | 213,951 | 16,436 |
| State-shared revenues and state grants | 666,570 | 656,645 | 653,140 | (3,505) |
| Federal sources | 55,000 | - | - | - |
| Local sources | 940,085 | 940,085 | 462,495 | (477,590) |
| Refuse collection | 286,145 | 288,675 | 288,677 | 2 |
| Charges for services | 210,995 | 198,745 | 203,656 | 4,911 |
| Cable franchise fees | 30,000 | 31,975 | 31,974 | (1) |
| Fines and forfeitures | 110,710 | 138,035 | 143,938 | 5,903 |
| Interest and rentals | 51,200 | 77,195 | 81,065 | 3,870 |
| Other | 105,735 | 69,130 | 74,946 | 5,816 |
| Total revenues | 5,219,375 | 5,291,915 | 4,888,888 | (403,027) |
| Expenditures | | | | |
| General government: | | | | |
| Council | 37,100 | 39,890 | 36,230 | 3,660 |
| Administrator | 401,595 | 380,725 | 379,512 | 1,213 |
| Assessing | 123,655 | 117,525 | 117,351 | 174 |
| Board of review | 700 | 690 | 690 | - |
| Treasurer | 508,025 | 490,255 | 361,372 | 128,883 |
| Technology | 66,150 | 48,935 | 43,694 | 5,241 |
| Election | 64,980 | 74,495 | 23,556 | 50,939 |
| Building official and City Hall | 125,865 | 127,640 | 121,940 | 5,700 |
| Legal | 55,000 | 60,435 | 60,368 | 67 |
| Property | 72,165 | 94,635 | 92,020 | 2,615 |
| Cemetery | 188,390 | 202,080 | 158,440 | 43,640 |
| Planning and zoning | 97,540 | 103,965 | 97,061 | 6,904 |
| Civil defense | 485 | 575 | 326 | 249 |
| Engineering | 245 | 245 | - | 245 |
| Planning commission | 1,480 | 165 | - | 165 |
| Burden | 45,115 | 31,805 | 32,297 | (492) |
| Retiree benefits | 58,085 | 47,570 | 47,568 | 2 |
| Contingencies | 430 | 430 | - | 430 |
| Surplus to fund balance | 346,645 | 659,575 | - | 659,575 |
| Total general government | 2,193,650 | 2,481,635 | 1,572,425 | 909,210 |

City of Mason, Michigan

Required Supplemental Information Budgetary Comparison Schedule - General Fund (Continued) Year Ended June 30, 2007

| | Original Budget | Amended Budget | Actual | Variance with Amended Budget Favorable (Unfavorable) |
|---|--------------------|-------------------|-------------------|--|
| Expenditures (Continued) | | | | |
| Public safety: | | | | |
| Police administration | \$ 248,774 | \$ 246,070 | \$ 205,263 | \$ 40,807 |
| Crossing guards | 41,905 | 42,425 | 36,147 | 6,278 |
| Police patrolling | 940,830 | 960,095 | 827,802 | 132,293 |
| Fire department | <u>284,972</u> | <u>279,210</u> | <u>477,636</u> | <u>(198,426)</u> |
| Total public safety | 1,516,481 | 1,527,800 | 1,546,848 | (19,048) |
| Public works: | | | | |
| Public services | 7,155 | 6,155 | 3,974 | 2,181 |
| Street lighting | 93,865 | 91,430 | 88,471 | 2,959 |
| Street construction and repair | 698,775 | - | - | - |
| Sidewalk construction repair | 68,100 | 11,430 | 9,717 | 1,713 |
| Refuse collection | <u>285,595</u> | <u>292,065</u> | <u>278,904</u> | <u>13,161</u> |
| Total public works | 1,153,490 | 401,080 | 381,066 | 20,014 |
| Recreation and culture: | | | | |
| Forestry | 83,152 | 65,545 | 53,459 | 12,086 |
| Parks and ball diamonds | 249,100 | 247,560 | 224,157 | 23,403 |
| Senior citizens | 7,630 | 7,630 | 6,495 | 1,135 |
| Library | <u>11,737</u> | <u>14,200</u> | <u>11,726</u> | <u>2,474</u> |
| Total recreation and culture | 351,619 | 334,935 | 295,837 | 39,098 |
| Community and economic development: | | | | |
| Cable commission | 5,060 | 4,360 | 3,264 | 1,096 |
| Christmas decorations | <u>5,005</u> | <u>3,885</u> | <u>3,098</u> | <u>787</u> |
| Total community and economic development | <u>10,065</u> | <u>8,245</u> | <u>6,362</u> | <u>1,883</u> |
| Total expenditures | 5,225,305 | 4,753,695 | 3,802,538 | 951,157 |
| Other financing sources (uses): | | | | |
| Proceeds from issuance of debt | - | - | 231,530 | (231,530) |
| Transfers in | 107,600 | 107,600 | 107,600 | - |
| Transfers out | <u>(101,670)</u> | <u>(645,820)</u> | <u>(688,996)</u> | <u>43,176</u> |
| Total other financing sources (uses) | <u>5,930</u> | <u>(538,220)</u> | <u>(349,866)</u> | <u>(188,354)</u> |
| Surplus | <u>\$ -</u> | <u>\$ -</u> | <u>\$ 736,484</u> | <u>\$ 736,484</u> |

City of Mason, Michigan

Required Supplemental Information Budgetary Comparison Schedule - Local Street Fund Year Ended June 30, 2007

| | Original Budget | Amended Budget | Actual | Variance with Amended Budget Favorable (Unfavorable) |
|--|--------------------|-------------------|------------------|--|
| Revenues | | | | |
| Property taxes | \$ 45,000 | \$ 43,180 | \$ - | \$ (43,180) |
| State-shared revenues and state grants | 112,575 | 114,100 | 114,917 | 817 |
| Local sources | 613,745 | - | 83,747 | 83,747 |
| Charges for services | 21,000 | 21,440 | 21,942 | 502 |
| Interest and rentals | 3,650 | 3,825 | 3,876 | 51 |
| Transfers in | - | 572,505 | 531,941 | (40,564) |
| Total revenues | 795,970 | 755,050 | 756,423 | 1,373 |
| Expenditures | | | | |
| Street construction | 667,550 | 561,540 | 561,537 | 3 |
| Street maintenance | 107,910 | 168,035 | 165,172 | 2,863 |
| Traffic services | 4,975 | 2,445 | 1,996 | 449 |
| Winter maintenance | 11,430 | 11,080 | 11,066 | 14 |
| Surplus to fund balance | 4,105 | 11,950 | - | 11,950 |
| Total expenditures | 795,970 | 755,050 | 739,771 | 15,279 |
| Surplus | \$ - | \$ - | \$ 16,652 | \$ 16,652 |

City of Mason, Michigan

Required Supplemental Information Budgetary Comparison Schedule - Special Assessment Fund Year Ended June 30, 2007

| | Original Budget | Amended Budget | Actual | Variance with Amended Budget Favorable (Unfavorable) |
|---------------------------|--------------------|-------------------|-------------------|--|
| Revenues | | | | |
| Special assessments | \$ 158,955 | \$ 159,060 | \$ 161,476 | \$ 2,416 |
| Interest and rentals | 10,355 | 14,000 | 14,354 | 354 |
| Surplus from fund balance | - | 3,855 | - | (3,855) |
| Total revenues | 169,310 | 176,915 | 175,830 | (1,085) |
| Expenditures | | | | |
| Debt service | 101,495 | 116,680 | 116,680 | - |
| Surplus to fund balance | 7,580 | - | - | - |
| Transfers to other funds | 60,235 | 60,235 | 60,235 | - |
| Total expenditures | 169,310 | 176,915 | 176,915 | - |
| Shortfall | \$ - | \$ - | \$ (1,085) | \$ (1,085) |

Other Supplemental Information

City of Mason, Michigan

| | Special Revenue Funds | | Debt Service Fund | |
|--------------------------------------|-----------------------|-------------------|------------------------|--------------------------|
| | Major Streets Fund | Rayner Bond | Park St. Property Fund | Mason Building Authority |
| Assets | | | | |
| Cash and investments | \$ 515,883 | \$ 505,941 | \$ - | \$ 296 |
| Due from other governmental units | 53,179 | - | - | - |
| Total assets | <u>\$ 569,062</u> | <u>\$ 505,941</u> | <u>\$ -</u> | <u>\$ 296</u> |
| Liabilities and Fund Balances | | | | |
| Liabilities | | | | |
| Accounts payable | \$ 1,064 | \$ - | \$ - | \$ - |
| Due to other funds | 80,425 | - | - | - |
| Total liabilities | 81,489 | - | - | - |
| Fund Balances | | | | |
| Reserved | - | - | - | - |
| Unreserved | 487,573 | 505,941 | - | 296 |
| Total fund balances | <u>487,573</u> | <u>505,941</u> | <u>-</u> | <u>296</u> |
| Total liabilities and fund balances | <u>\$ 569,062</u> | <u>\$ 505,941</u> | <u>\$ -</u> | <u>\$ 296</u> |

**Other Supplemental Information
Combining Balance Sheet
Nonmajor Governmental Funds
June 30, 2007**

| <u>Capital Projects Fund</u> | <u>Permanent Fund</u> | |
|----------------------------------|---------------------------|---|
| Capital Improvement Fund | Cemetery Trust | Total Nonmajor Governmental Funds |
| \$ 42,039 | \$ 316,702 | \$ 1,380,861 |
| <u>-</u> | <u>-</u> | <u>53,179</u> |
| <u>\$ 42,039</u> | <u>\$ 316,702</u> | <u>\$ 1,434,040</u> |
| | | |
| \$ - | \$ - | \$ 1,064 |
| <u>-</u> | <u>-</u> | <u>80,425</u> |
| - | - | 81,489 |
| - | 316,702 | 316,702 |
| <u>42,039</u> | <u>-</u> | <u>1,035,849</u> |
| <u>42,039</u> | <u>316,702</u> | <u>1,352,551</u> |
| | | |
| <u>\$ 42,039</u> | <u>\$ 316,702</u> | <u>\$ 1,434,040</u> |

City of Mason, Michigan

| | Special Revenue Funds | | | Debt Service |
|---|-----------------------|-------------------|-------------------|--------------------------|
| | Major Streets | Rayner Bond | Park St. Property | Mason Building Authority |
| | Fund | | Fund | Authority |
| Revenue | | | | |
| State and local sources | \$ 323,891 | \$ - | \$ - | \$ - |
| Charges for services | - | - | - | - |
| Interest income | 21,260 | 24,979 | - | 30 |
| Rent and royalties | - | 37,453 | - | - |
| Other | 872 | - | - | - |
| Total revenue | 346,023 | 62,432 | - | 30 |
| Expenditures | | | | |
| Current - Public works department | 411,553 | - | - | - |
| Capital outlay | - | - | - | - |
| Debt service | - | - | 41,982 | 36,827 |
| Total expenditures | 411,553 | - | 41,982 | 36,827 |
| Excess of Revenue Over (Under) | | | | |
| Expenditures | (65,530) | 62,432 | (41,982) | (36,797) |
| Other Financing Sources (Uses) | | | | |
| Transfers in | 135,815 | - | 41,982 | 36,828 |
| Transfers out | (80,425) | (43,105) | - | - |
| Total other financing sources (uses) | 55,390 | (43,105) | 41,982 | 36,828 |
| Net Change in Fund Balances | (10,140) | 19,327 | - | 31 |
| Fund Balances - Beginning of year | 497,713 | 486,614 | - | 265 |
| Fund Balances - End of year | \$ 487,573 | \$ 505,941 | \$ - | \$ 296 |

Other Supplemental Information
Combining Statement of Revenue, Expenditures, and Changes
in Fund Balances - Nonmajor Governmental Funds
Year Ended June 30, 2007

| Capital Projects Fund | Permanent Fund | Total Nonmajor Governmental Funds |
|--------------------------|-------------------|--|
| \$ - | \$ - | \$ 323,891 |
| - | 8,470 | 8,470 |
| 2,883 | 15,762 | 64,914 |
| - | - | 37,453 |
| 295 | - | 1,167 |
| 3,178 | 24,232 | 435,895 |
| - | - | 411,553 |
| 17,805 | - | 17,805 |
| 23,131 | - | 101,940 |
| 40,936 | - | 531,298 |
| (37,758) | 24,232 | (95,403) |
| 22,855 | - | 237,480 |
| - | (4,260) | (127,790) |
| 22,855 | (4,260) | 109,690 |
| (14,903) | 19,972 | 14,287 |
| 56,942 | 296,730 | 1,338,264 |
| \$ 42,039 | \$ 316,702 | \$ 1,352,551 |

City of Mason, Michigan

Other Supplemental Information Combining Statement of Assets and Liabilities Fiduciary Funds June 30, 2007

| | Delinquent Tax Fund | Payroll Fund | Totals |
|---|------------------------|------------------|------------------|
| Assets - Cash and cash equivalents | \$ 324 | \$ 25,454 | \$ 25,778 |
| Liabilities | | | |
| Accrued and other liabilities | \$ - | \$ 25,446 | \$ 25,446 |
| Due to other governmental units | 324 | 8 | 332 |
| Total liabilities | \$ 324 | \$ 25,454 | \$ 25,778 |

City of Mason, Michigan

**Report to the City Council
June 30, 2007**

To the Honorable Mayor and
 Members of the City Council
 City of Mason, Michigan

We recently completed our audit of the financial statements of the City of Mason, Michigan for the year ended June 30, 2007. During the performance of our audit, we noted items related to the internal controls systems and operations as a whole that we would like to bring to your attention. All items are presented for your consideration on attachments as outlined below:

| TITLE | PAGE |
|--|-------|
| Significant Deficiency | 2 |
| Recommendations | |
| Certain Cash Receipts | 3 |
| Property Tax Adjustments | 3 |
| Retiree Healthcare Benefits | 4 |
| Legislative Issues | |
| Revenue Sharing | 5-6 |
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| Other Legislative Items | 9 |
| Property Tax Legislation | 10 |
| 911 Surcharge Sunset Extended Temporarily | 10 |
| Bonding to Fund Liability for Other Post Employment Benefits | 11 |
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We appreciate the opportunity to be of service to the City of Mason. The cooperation extended to us by your staff throughout the audit was greatly appreciated. We look forward to continuing our relationship with the City. Should you wish to discuss any of the items included in this letter, we would be happy to do so.

Plante & Moran, PLLC

October 5, 2007

City of Mason, Michigan

Significant Deficiency

June 30, 2007

In planning and performing our audit of the financial statements of the City of Mason, Michigan (the "City") as of and for the year ended June 30, 2007, in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

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

A 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 entity's 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 entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the following deficiency to be a significant deficiency in internal control.

The City does not record an accrued salary and wage expense in its general ledger, in accordance with generally accepted accounting principles. Additionally, the City does not review the potential amount of the accrual at year end. For most funds, this accrual would be immaterial. However, there is the potential that a more than inconsequential misstatement would result in the General Fund when the accrual period becomes greater than three days. We recommend that the City review the amount of accrued salary and wages at the end of the year and record the applicable amounts in the appropriate funds.

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 entity's 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 internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

City of Mason, Michigan

Recommendations

June 30, 2007

Certain Cash Receipts

During the testing of journal entries, it came to our attention that the City has been collecting contributions from employees for the funding of retirement parties. Additionally, we noted that the City is actually recording these contributions into the General Fund as cash receipts, and when expenses are incurred, checks are written out of the General Fund for an amount not to exceed the amount that was collected. While the collection of these funds is in itself a legitimate and allowable activity, the recording of these amounts in the City's general ledger creates an appearance of improper spending. The *Bulletin for Audits of Local Units of Government in Michigan* specifically identifies expenditures - such as retirement recognition events, flowers to the sick or departed, and a myriad of others - for which governmental funds are not allowed to be used. Although we are not aware of any prohibited expenditures that the City has made, we recommend that the City consider not recording these contributions as revenue and these disbursements as expenditures into its general ledger but consider reflecting this activity within an agency account (funds held for others) in order to avoid the appearance of making prohibited expenditures.

Property Tax Adjustment

Upon review and testing of property taxes, we noted two instances of amounts recorded in the general ledger had not been adjusted for certain economic conditions. The first instance involves amounts held as receivable and revenue that were unavailable on a full accrual basis at June 30. Although this is not a typical entry that the City would make as it does not affect the day-to-day records maintained on the fund, or modified accrual level, it is important for the City to consider the potential impact that fiscal activity has on its full accrual statements. We recommend that, during the year-end closing procedures, all receivable accounts be evaluated for collectibility and availability and adjusted to reflect those determinations.

The second instance involves property tax revenue that was recognized in the Local Street Fund. While the City remains diligent in designating portions of its operating millage to the construction and maintenance of its local streets, and maintains its Local Street Fund to monitor those activities, the General Fund is responsible for collecting all operating property tax revenue and allocating it after it is initially recorded. We recommend that all operating tax millage amounts be first recorded in the General Fund as property tax revenue, then, using operating transfers, allocate the amount the council has designated to the Local Street Fund. This will allow for better tracking of all property tax revenue amounts and more accurately depict the council's intent of using portions of the operating millage toward the conservation and betterment of the City's roads.

City of Mason, Michigan

Recommendations

June 30, 2007

Retiree Healthcare Benefits

The Governmental Accounting Standards Board has released Statement Number 45, *Accounting and Reporting by Employers for Postemployment Benefits Other Than Pensions*. The new pronouncement provides guidance for local units of government in recognizing the cost of retiree health care, as well as any “other” postemployment benefits (other than pensions). The intent of the new rules is to recognize the cost of providing retiree healthcare coverage over the working life of the employee, rather than at the time the healthcare premiums are paid. These new rules will apply to the government-wide financial statements, rather than the individual fund level. Therefore, the manner in which retiree healthcare benefits are budgeted will not change, unless you begin funding the benefits (however, as discussed below, there are incentives to do so).

The new pronouncement will require a valuation of the obligation to provide retiree healthcare benefits, including an amortization of the past service cost over a period of up to 30 years. The valuation must include an annual recommended contribution (ARC). While the ARC does not need to be funded each year, any underfunding must be reported as a liability on the government-wide statement of net assets.

This valuation will need to be performed by an actuary if the total participants exceed 100. Participants are defined as employees in active service, terminated employees not yet receiving benefits, plus retirees and beneficiaries currently receiving benefits. For plans with 100 to 200 participants, the actuarial valuation must be at least every three years; for those over 200 participants, at least every other year.

This statement is being phased in over a three year-period, similar to GASB 34. It is effective for fiscal years beginning after December 15, 2006, 2007, or 2008 depending on whether your revenues are over \$100 million, between \$10 million and \$100 million, or under \$10 million. Remember that planning to make the annual recommended contribution generally requires up to three to six months for an actuarial valuation plus six months’ lead time to work the numbers into the budget. Therefore, we recommend that you begin the actuarial valuation at least one year prior to the above dates.

The GASB statement has provided substantial incentive to fund the obligation in accordance with the annual recommended contribution. In addition to the normal fairness issue of paying for a service as you use it, the GASB has directed that lower rates of return be used for evaluating the annual recommended contribution in situations where the recommended contribution is not being funded. This will significantly increase the calculation of the following year’s contribution. Therefore, funding the contribution will actually reduce your long-run cost.

City of Mason, Michigan

Legislative Issues

June 30, 2007

Revenue Sharing

The future of the State's revenue-sharing program continues to be directly tied to the condition of the State's budget. Reductions to statutory revenue sharing started in 2001 as shortfalls began occurring in the State's budget. The State's budget shortfalls continue to be significant. The State was approximately \$1.8 billion short of the revenue needed to cover basic services for the State's upcoming fiscal year 2007/2008 budget. The legislature and the governor acted on October 1 to increase the income tax rate (from 3.9 percent to 4.35 percent, raising more than \$750 million) and to enact a new 6 percent tax on certain services (raising approximately \$700 million per year). As part of the continuation budget that was also passed on October 1, there are still approximately \$400 million of "to-be-determined" cuts that remain to be agreed upon and announced for the fiscal year 2007/2008 budget. It is not completely clear whether the State's fiscal year 2006/2007 budget has been completely balanced as well. The outcome of other matters will also impact revenue sharing and those matters include:

- **Future of County Participation in Statutory Revenue Sharing** - In 2004, the State terminated payment of statutory revenue sharing to counties (which was approximately \$182 million) but allowed counties to move their operating tax levy to July from December. Counties are required to deposit the additional monies from the earlier levy into a "reserve fund" which is to be used by the counties to replace lost statutory revenue sharing in future years. The question that remains is, when the reserve funds established by counties are depleted, will counties come back into the "revenue-sharing formula" and to what extent? Will the size of the statutory pot grow to accommodate counties or will there be a shift of the same monies from cities, villages, and townships to the counties?
- **Statutory Revenue-sharing Formula Expires in 2007** - Legislative action is required on this Act for appropriations to continue into 2008 and beyond.
- **Changes to Michigan's Tax Structure** - The Michigan single business tax has been eliminated effective December 31, 2007 which will result in the loss of \$1.9 billion from the State's budget in 2008. In June 2007, a replacement for the single business tax - called the new Michigan business tax - was approved by the legislature. More details on this new tax structure are included below. In the overview, the plan creates a new tax structure for Michigan businesses, provides further personal property tax relief to business taxpayers and is forecasted by the State to generate about the same revenue (\$1.9 billion) as the single business tax. Technical corrections on this recently passed law are still pending and the law is lengthy and complex. The true financial impact on the State's budget is hard to predict. Further changes to Michigan's tax structure were made on October 1 as described above to partially close the structural budget deficit that exists.

City of Mason, Michigan

Legislative Issues

June 30, 2007

Revenue Sharing (Continued)

As introduced, the governor's budget for fiscal year 2007/2008 includes a revenue-sharing increase of \$27 million to be distributed using the three-part formula currently contained in the revenue-sharing act (taxable value per capita, population/unit type and yield equalization) with an additional \$14.5 million for public safety funding. While specific details have not been announced yet, communities would only be eligible for the increase if they can demonstrate service sharing with other local governments. Many observers have indicated that it is likely that revenue sharing for fiscal year 2007/2008 will more than likely be tied to fiscal year 2006/2007 funding levels.

It is unclear what the outcome will be regarding the short-term and long-term funding of statutory revenue sharing. Decisions still remain on the ultimate funding level for revenue sharing for the State's fiscal years 2006/2007 and 2007/2008. Local governments may need to react with budget amendments when these final decisions are made by the State.

Personal Property Tax Update

Over the last seven years, the State's personal property tax laws and regulations have changed substantially. In 2000, the State Tax Commission updated the general business depreciation tables that are used to calculate personal property taxes, resulting in an approximately 10 percent drop in property tax revenue. In addition, the State Tax Commission also approved new personal property tax tables for utilities which made drastic changes to transmission and distribution property of utilities (resulting in an approximately 30 percent revenue loss to local units of government). Also, the Michigan Supreme Court in *WPW Acquisition Co v. City of Troy* ruled that the Proposal A cap prevents assessors from increasing the taxable value of commercial rental property above the rate of inflation using the occupancy methodology even when reductions in taxable value were previously granted due to a decrease in occupancy.

The new Michigan business tax also provides more personal property tax relief to business taxpayers (see details below). Even with this most recent relief provided in June 2007 in the MBT, further reductions to personal property tax remain part of the State's tax structure discussions. Personal property taxes are a significant revenue source to many local governments. If the State's new business tax structure provides personal property tax relief, the question is will local governments be held harmless by the State and to what extent? The governor's tax plan as introduced proposes to change the property tax system to mitigate the impact of the WPW case. A similar attempt to make this correction occurred in 2005 and 2006 with no success.

City of Mason, Michigan

Legislative Issues

June 30, 2007

New Michigan Business Tax

As previously indicated, the new Michigan business tax (MBT) was approved by the legislature in June 2007 and replaces the single business tax (SBT) which expires December 31, 2007. According to the State, the new MBT is intended to generate about the same \$1.9 billion generated by the expiring SBT.

While the MBT intended to simplify the old SBT, the MBT is a very lengthy and complicated new law. The new MBT imposes two taxes - a modified gross receipts tax and a business income tax. The modified gross receipts tax is imposed at .8 percent on a tax base composed of gross receipts less certain purchases. The business income tax will be imposed at a rate of less than 5 percent on business income. The MBT provides for new investment, compensation, and research and development credits to businesses. The MBT also allows certain qualified small businesses to opt out of the MBT and pay a straight 1.8 percent tax on adjusted business income.

More personal property tax relief is also part of the new MBT. Business personal property classified as "industrial" or "commercial" will be exempt from certain personal property taxes - specifically from the State Education Tax (SET) and local school operating mills. "Industrial" personal property will receive exemptions from the 6 SET mills and the 18 schools operating mills (for a total 24 mill exemption). "Commercial" personal property will be exempt from 12 of the 18 school operating mills.

These newly enacted personal property tax exemptions will mean that local governments will collect less school taxes on these properties. For local governments that have enacted an administrative fee on tax collections, they will likely see a decrease in the administration fees that have traditionally been collected. Also, for those local governments with tax increment financing authorities that continue to have existing eligible obligations outstanding and are therefore allowed to capture school taxes (to the extent of these eligible obligations), the personal property tax exemptions on school millages will likely decrease the amount of school taxes available to capture.

Given the favorable tax treatment of industrial versus commercial personal property, it is expected that businesses will be re-reviewing the classification of their personal property. Your assessor will likely receive more frequent inquiries and requests to change classification of personal property to take the most advantage of the tax break afforded to industrial property and commercial property and the additional relief available for industrial property.

As we understand it now, these are the areas at the local governmental level (i.e., impact on administrative fees; impact on school dollars available for capture for certain tax increment financing authorities; property classifications) that are the most directly impacted by the new MBT.

We will keep you updated as we continue to explore these and other issues regarding the impact of the MBT on local units of government.

City of Mason, Michigan

Legislative Issues

June 30, 2007

New Cable Franchise Legislation

The governor signed cable franchise legislation (House Bill 6456) into law effective January 1, 2007. The new law (Public Act 480 of 2006) creates the “Uniform Video Services Local Franchise Act,” which provides a statewide framework for franchising agreements instead of individual community agreements. This Act requires video service providers to obtain a local franchise, good for 10 years, from the franchising entity (the local unit of government). As part of the local franchise, the provider is required to pay an annual video service provider fee, not to exceed 5 percent of gross revenue, as well as an annual fee for the costs of the PEG access facilities, not to exceed 2 percent of gross revenue. The Act allows providers to terminate the current franchise contracts before their expiration date in order to enter into this new local franchise agreement under the statewide framework.

Local units of government will be impacted in the following ways:

- Under the Act, no additional fees or charges other than those stipulated under the Act may be written into the local franchise agreements.
- To the extent existing cable franchise agreements provided more funding than provided for under the new Act, municipalities will see reduced fees from these new local franchise agreements.
- A credit, based on annual maintenance fees paid for use of public rights of way, to video service providers is allowed under the Act. This credit could eliminate or significantly reduce any revenue the local unit might receive under the bill’s franchise fee.
- Audits of the video service providers’ calculation of gross revenue are limited to once every two years.

It is expected that local governments will receive their first payment under the new Act beginning in May 2007 or shortly thereafter. We strongly encourage you to review this payment compared to payments previously received and follow up with your provider as required.

Subsequent to the passage of the Act, amendments have been proposed in both the House and the Senate (House Bill 5047 and Senate Bill 636) to clarify language about the ability of local governments to receive PEG fees.

City of Mason, Michigan

Legislative Issues

June 30, 2007

Recent Revisions to State Transportation Funding Program

Current legislation modified Act 51 to allow local governments to transfer monies from their Major Street Fund to their Local Street Fund at a level of 50 percent of annual major street funding received. In addition, greater than 50 percent can be transferred. However, the amended law requires that certain conditions be met to allow for a transfer in excess of 50 percent including the adoption of an asset management process for the major and local street systems as well as a detailed resolution passed by the City. It is important to note that major street monies transferred for use on local streets cannot be used for construction but may be used for preservation, and these provisions sunset December 31, 2008. Without an extension of this provision, a transfer from the Major Street Fund to the Local Street Fund can only be done to the extent that local revenues exist in the Major Street Fund. Current legislation also includes a pilot program that would allow for the combination of the Major Street Fund and the Local Street Fund if certain conditions are met.

Other Legislative Items

In addition to the legislature's main focus on the business tax structure and solving the budget deficit, the following are a summary of a few other matters impacting local government finance receiving attention in Lansing these days:

- **Act 312** - Several articles have been written about recent discussions on potential revisions to Act 312, which governs collective bargaining between local governments and their police and fire bargaining units.
- **Local Government Consolidation** - Two bills to eliminate potential barriers to consolidation efforts have received attention by the legislature (House Bills 4266 and 4246).
- **Drain Code Revisions** - A series of bills dealing with revisions to the Drain Code were voted on by the House in August (House Bills 4641, 4642, 4643, 4644, and 4688).
- **Transportation Tax Increase** - There continues to be ongoing discussion about the need for additional monies to properly fund Michigan transportation system. More information can be found at http://www.drivemi.org/mtt_members.php.

City of Mason, Michigan

Legislative Issues

June 30, 2007

Property Tax Legislation

A series of House bills were introduced in 2007 dealing with the treatment of the uncapping of value on sale or transfer of property. With the passage of Proposal A in 1994, changes to the taxable value of an individual property are limited to the lesser of the rate of inflation or 5 percent - until the property is sold or transferred. The difference between the capped taxable value amount and state equalized value at the time of transfer is referred as the “uncapped” value or the “pop-up” value. As several published studies and reports have demonstrated, the treatment of “uncapped” values or the “pop up” amount when a property is transferred or sold as growth on existing property subject to the Headlee rollback calculation has resulted in continued downward pressure on millage rates. This treatment is due to definitional changes made to the General Property Tax Act in 1994.

The three bills in the package are House Bills 4440, 4441, and 4442 and would propose to do the following:

- **House Bill 4440** - This bill establishes an 18-month moratorium on the “pop-up” or “uncapping” of taxable value to state equalized value at the time of sale or transfer of a property. Property sales or transfers occurring in the time frame of the moratorium would continue to pay property taxes at the previous taxable value amount. The “pop-up” or “uncapping” of taxable value would be delayed until the property was sold or transferred in later years.
- **House Bill 4441** - This bill increases the real estate transfer tax by .10 percent and earmarks the money to be returned to local government for potential loss in revenue occurring from House Bill 4440.
- **House Bill 4442** - This bill would change the General Property Tax Act to exempt the “pop-up” or “uncapped” value from the Headlee rollback calculation. If this legislation were enacted, increases in taxable value resulting from property sales or transfers would be treated as “additions” to taxable value or new growth versus growth on existing property.

House Bills 4440 and 4441 passed the House on March 14 (HB 4440 has been assigned to the Senate Finance Committee). House Bill 4442 has not been voted on yet in the House. The bills are not tie barred.

911 Surcharge Sunset Extended Temporarily

Local governments receiving monies under the Emergency Service Enabling Act to support 911 operations faced the potential elimination or change in the funding formula at December 31, 2006. To allow further analysis of this issue, the sunset of the Act was extended one year to December 31, 2007 (Public Act 249 of 2006). The surcharge to fund 911 operations has been the subject of considerable discussions over the last several months with the approaching expiration at December 31, 2007. Action is required by the legislature to continue this charge beyond December 31, 2007 so discussions will continue on this subject into September and perhaps the remainder of the fall legislative session.

City of Mason, Michigan

Legislative Issues

June 30, 2007

Bonding to Fund Liability for Other Post Employment Benefits

The day quickly approaches for local governments to measure the liability for non-pension benefits granted to government employees at retirement (most notably retiree health care). Once these benefits are measured, local governments will face the tough choice of advance funding these benefits (which some are doing now), remain on a pay-as-you go plan (which is the path for most local governments), or a combination thereof. To provide local governments with additional funding options, legislation was introduced in 2006 which would allow for bonding as a funding tool. The legislation was passed by the Michigan Legislature and vetoed by the governor. It was expected that the legislation was going to be reconsidered in 2007.

Property Assessment Cap

As you recall, Proposal A limits the growth in taxable value to the lesser of inflation or 5 percent. The inflation factor for this calculation is published by the State Tax Commission and is:

| | |
|------|-------------|
| 2007 | 3.7 percent |
| 2006 | 3.3 percent |
| 2005 | 2.3 percent |
| 2004 | 2.3 percent |
| 2003 | 1.5 percent |
| 2002 | 3.2 percent |
| 2001 | 3.2 percent |
| 2000 | 1.9 percent |
| 1999 | 1.6 percent |
| 1998 | 2.7 percent |
| 1997 | 2.8 percent |
| 1996 | 2.8 percent |
| 1995 | 2.6 percent |
| 1994 | 3.0 percent |

Also, as you probably recall, the Headlee Amendment to the Michigan Constitution limits the amount of taxes that can be levied by the City. In general terms, if growth on the City's existing property tax base exceeds inflation for a particular year, the Headlee Amendment requires the City to "roll back" its property tax rate to inflation. Prior to the passage of Proposal A in 1994, during years when the growth on the City's existing property tax base was less than inflation, the Headlee Amendment allowed the City to "roll up" its property tax rate and recover from years when the property tax rate was "rolled back". However, subsequent to the passage of Proposal A and as a result of changes made to the State's General Property Tax Act, the City is no longer allowed to "roll up" its property tax rate in years when growth on its existing tax base is less than inflation.

City of Mason, Michigan

Legislative Issues

June 30, 2007

Property Assessment Cap (Continued)

For the year ended June 30, 2007, the City's Headlee maximum property tax rate for its operating levy was 18.4853 mills even though City Charter would allow the City to levy 20 mills for operations. Because of changes made to the General Property Tax Act in 1994, this reduction in millage rate is permanent absent a Headlee override vote. Additionally, as demonstrated in several published studies and reports, due to definitional changes made to the General Property Tax Act in 1994, the treatment of uncapped values or the "pop up" amount when a property is transferred or sold (as growth on existing property subject to the Headlee rollback calculation), the downward pressure on millage rates will continue particularly given the significant gap that now exists between taxable value and state equalized value.

Municipal Finance Act Revisions

The Municipal Finance Act was amended several years ago. Communities are now required to submit a filing once a year with the Michigan Department of Treasury. The old 10-day "exemption from prior approval" process has been eliminated and is replaced with this qualification process. This filing will serve as a pre-approval for future debt issues. The current filing is due within six months of the City's year end (December 31, 2007) and is good for one year thereafter. The City should consider the need to file a qualifying statement for each of its component units.