

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 checked="" type="checkbox"/> Village <input type="checkbox"/> Other		Local Unit Name Village of Shelby	County Oceana
Fiscal Year End 2/28/07	Opinion Date 7/27/07	Date Audit Report Submitted to State 7/30/07	

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 | <input checked="" type="checkbox"/> <input type="checkbox"/> | 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 checked="" type="checkbox"/>		
The letter of Comments and Recommendations	<input checked="" type="checkbox"/>		
Other (Describe)	<input type="checkbox"/>	No other items required	
Certified Public Accountant (Firm Name) BRICKLEY DELONG, PLC		Telephone Number 231-726-5800	
Street Address 316 MORRIS AVENUE		City MUSKEGON	State MI
		Zip 49443	
Authorizing CPA Signature <i>Timothy D. Arter, CPA</i> for Buckley DeLong, PLC		Printed Name TIMOTHY D. ARTER	License Number 10253

Village of Shelby
Oceana County, Michigan

REPORT ON FINANCIAL STATEMENTS
(with required supplementary information)

Year ended February 28, 2007

Village of Shelby
LIST OF ELECTED AND APPOINTED OFFICIALS
February 28, 2007

ELECTED OFFICIALS

Bill Glover Village President
Pat Morningstar President Pro-Tem
Matt Cederquist Council Member
Ross Field Council Member
Andrea Garcia Council Member
Steve Lessens Council Member
Rich Setlack Council Member
Kelly Pastotnik Clerk
Yolanda Estrada Treasurer

APPOINTED OFFICIALS

Sandy Dean Deputy Clerk/Bookkeeper
Randal Phillips Superintendent of Public Works

Village of Shelby

TABLE OF CONTENTS

Management’s Discussion and Analysis..... i - viii

Independent Auditors’ Report..... 1

Basic Financial Statements

 Government-Wide Financial Statements

 Statement of Net Assets.....2

 Statement of Activities3

 Fund Financial Statements

 Governmental Funds

 Balance Sheet.....4

 Reconciliation of the Governmental Funds Balance Sheet
 to the Statement of Net Assets5

 Statement of Revenues, Expenditures and Changes
 in Fund Balances6

 Reconciliation of the Governmental Funds Statement of Revenues,
 Expenditures and Changes in Fund Balances to the Statement of
 Activities7

 Proprietary Funds

 Statement of Net Assets.....8

 Statement of Revenues, Expenses and Changes in Fund Net Assets9

 Statement of Cash Flows10

 Statement of Fiduciary Assets and Liabilities.....11

Notes to Financial Statements12

Required Supplementary Information

 Budgetary Comparison Schedule—General Fund26

 Budgetary Comparison Schedule—Major Streets Fund27

 Budgetary Comparison Schedule—Local Streets Fund28

As management of the Village of Shelby, we present to the readers of the Village's financial statements this overview and analysis of the financial activities of the Village for the fiscal year ended February 28, 2007. We encourage you to consider the information presented in these financial statements along with the additional information that has been furnished in this letter.

FINANCIAL HIGHLIGHTS

- Total net assets of all governmental activities increased by \$96,599.
- The General Fund fund balance decreased by \$1,339.
- The net assets in the Water Fund increased by \$37,660.
- The net assets in the Sewer Fund increased by \$111,640.

OVERVIEW OF THE FINANCIAL STATEMENTS

The discussion and analysis is intended to serve as an introduction to the Village's basic financial statements. The basic financial statements are comprised of three components: 1) government-wide financial statements, 2) fund financial statements and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

Government-wide Financial Statements

The government-wide financial statements are designed to provide the reader with a broad overview of the Village's finances. These statements are similar to those of a private sector business.

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

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

Both of the government-wide financial statements mentioned above distinguish functions of the Village that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are designed to recover all or a significant part of their costs through user fees and charges for services (business type activities). The governmental activities of the Village include general government, public safety, public works, and cultural and recreational activities. The business-type activities of the Village include water and sewer services.

Fund Financial Statements. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Village, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the Village can be divided into three categories-governmental funds, proprietary funds and fiduciary funds.

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

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

The Village maintains four individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for all four funds as they are all considered major funds.

Proprietary Funds. The Village has two enterprise proprietary funds. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The Village uses enterprise funds to account for its water distribution and sewer operations.

Enterprise funds provide the same type of information as the government-wide financial statements, only in more detail. The enterprise funds financial statements provide separate information for the Water and Sewer funds, both of which are major funds.

Fiduciary Funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the Village. Fiduciary funds are not reflected on the government-wide financial statements because the resources from those funds are not available to support the Village's programs. The accounting method used for fiduciary funds is much like that used for the proprietary funds.

Notes to Financial Statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The reader is encouraged to include the reading of this section in any attempt to analyze and understand these statements.

Other Information. In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information concerning the Village's budgetary information as it relates to the actual expenditures for the General Fund, Major Streets Fund and Local Streets Fund.

Government-wide Financial Analysis

The first table presented below is a summary of the government-wide statement of net assets for the Village. As stated earlier, the net assets may be used as an indicator of a government's financial health. As of February 28, 2007, the Village's net assets from governmental activities totaled \$3,508,740 (58%) and \$2,573,896 (42%) from business-type activities, creating a total government-wide net assets total of \$6,082,636.

In examining the composition of these net assets, the reader should note that governmental activities net assets are invested in capital assets (i.e., streets, buildings, land, vehicles, equipment, etc.) These assets are used to provide services to the Village's residents, and they are not available to pay salaries, operational expenses or fund capital projects. The unrestricted net assets for governmental activities actually depict a balance of \$936,784. This represents the amount of discretionary resources that can be used for general governmental operations.

For governmental activities, growth in current assets is similar to growth in unrestricted and restricted net assets. Restricted net assets are legally restricted for streets and debt service. Decreases in capital assets and noncurrent liabilities are attributable to regular depreciation expense and scheduled debt payments, respectively.

The business-type activities show a total of \$2,573,896 in net assets and \$739,945 in unrestricted net assets. The Sewer Fund and Water Fund unrestricted net assets are \$271,229 and \$483,370, respectively.

For business-type activities, capital assets and invested in capital assets, net of related debt, increased as a result of preliminary engineering work being done for sewer plant improvements. Noncurrent liabilities decreases are attributable to scheduled debt payments.

Net Assets

	Governmental Activities		Business-type Activities		Total	
	2007	2006	2007	2006	2007	2006
Current assets and other assets	\$ 2,142,109	\$ 1,945,275	\$ 605,173	\$ 607,595	\$ 2,747,282	\$ 2,552,870
Capital assets	2,774,478	2,983,389	3,130,990	3,085,751	5,905,468	6,069,140
Total assets	4,916,587	4,928,664	3,736,163	3,693,346	8,652,750	8,622,010
Current liabilities	157,645	151,116	82,267	121,128	239,912	272,244
Noncurrent liabilities	1,250,202	1,365,407	1,080,000	1,140,000	2,330,202	2,505,407
Total liabilities	1,407,847	1,516,523	1,162,267	1,261,128	2,570,114	2,777,651

	Governmental		Business-type		Total	
	Activities		Activities			
	2007	2006	2007	2006	2007	2006
Net assets						
Invested in capital assets, net of related debt	\$ 1,506,061	\$ 1,581,882	\$ 1,779,221	\$ 1,844,136	\$ 3,285,282	\$ 3,426,018
Restricted	1,065,895	917,138	54,730	41,615	1,120,625	958,753
Unrestricted	936,784	913,121	739,945	546,467	1,676,729	1,459,588
Total net assets	<u>\$ 3,508,740</u>	<u>\$ 3,412,141</u>	<u>\$ 2,573,896</u>	<u>\$ 2,432,218</u>	<u>\$ 6,082,636</u>	<u>\$ 5,844,359</u>

Governmental Activities

Net assets of governmental activities increased by \$96,599 (2.8%) during the 2007 fiscal year. Operating grants increased due to higher Act 51 revenues from the State due to the transfer of the jurisdiction of a road running through the Village to the Village. Property taxes increased due to growth in taxable values. The governmental activities did not dispose of any significant assets this year, accounting for the decrease in gain on sale of capital assets. Interest on long-term debt increased due to timing issues. The following table shows these results.

Business-type activities

At the end of the fiscal year, the net assets for business-type activities increased by \$141,678 (5.8%). Charges for services increased due to sewer rate increases. The following table shows these results.

Change in Net Assets

	Governmental		Business-type		Total	
	Activities		Activities			
	2007	2006	2007	2006	2007	2006
Revenues:						
Program revenues						
Charges for services	\$ 35,212	\$ 34,881	\$ 482,728	\$ 453,740	\$ 517,940	\$ 488,621
Operating grants	230,368	204,358	260	7,257	230,628	211,615
Capital grants	-	-	1,009	3,815	1,009	3,815
General revenues						
Property taxes	514,115	497,360	-	-	514,115	497,360
Grants and contributions not restricted	214,880	218,944	-	-	214,880	218,944
Unrestricted investment earnings	25,801	27,783	16,041	9,305	41,842	37,088
Miscellaneous	5,611	9,730	19,115	12,587	24,726	22,317
Gain on sale of capital assets	-	45,343	-	-	-	45,343
Total revenues	<u>1,025,987</u>	<u>1,038,399</u>	<u>519,153</u>	<u>486,704</u>	<u>1,545,140</u>	<u>1,525,103</u>

	Governmental		Business-type		Total	
	Activities		Activities			
	2007	2006	2007	2006	2007	2006
Expenses:						
General government	\$ 89,517	\$ 89,738	\$ -	\$ -	\$ 89,517	\$ 89,738
Public safety	251,955	257,891	-	-	251,955	257,891
Public works	504,306	534,647	-	-	504,306	534,647
Culture and recreation	20,536	24,397	-	-	20,536	24,397
Interest on long-term debt	63,074	27,380	-	-	-	27,380
Sewer Fund	-	-	118,046	115,290	118,046	115,290
Water Fund	-	-	259,429	258,600	259,429	258,600
Total expenses	<u>929,388</u>	<u>934,053</u>	<u>377,475</u>	<u>373,890</u>	<u>1,306,863</u>	<u>1,307,943</u>
Change in net assets	96,599	104,346	141,678	112,814	238,277	217,160
Net assets - Beginning	<u>3,412,141</u>	<u>3,307,795</u>	<u>2,432,218</u>	<u>2,319,404</u>	<u>5,844,359</u>	<u>5,627,199</u>
Net assets - Ending	<u>\$ 3,508,740</u>	<u>\$ 3,412,141</u>	<u>\$ 2,573,896</u>	<u>\$ 2,432,218</u>	<u>\$ 6,082,636</u>	<u>\$ 5,844,359</u>

Financial Analysis of the Government's Funds

As stated earlier in this discussion and analysis, the Village uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds. The focus of the Village's governmental funds is to provide information on near-term inflows, outflows, and balances in spendable resources. Such information is useful in assessing the Village's financing requirements. In particular, unreserved fund balances or the lack thereof, may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

At February 28, 2007, the Village governmental funds reported a combined fund balance of \$1,775,299. This number represents fund balance of \$709,404 in the General Fund and \$1,065,895 in other governmental funds. It is necessary to further distinguish between the unreserved and reserved fund balance. The unreserved balance represents what is available for spending at the Village's discretion. The remainder of the fund balance is reserved to indicate that it is not available for new spending because it has already been committed for advances to other funds of \$200,000 and to pay debt service of \$112,527.

The decrease in fund balance of \$1,339 in the General Fund is similar to the increase in fund balance of \$4,981 in the previous year.

Proprietary Funds. The Village's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail. Net assets of the Sewer and Water funds increased by \$111,640 and \$37,660, respectively. The result was an overall net increase in the proprietary funds of \$149,300.

General Fund Budget

During the current fiscal year, the Village did not make any amendments to the original revenue budget and only made a few minor reclassifications to the original expense budget that did not change total expenses.

The following comments summarize the major variations from the final budget to actual revenues and expenditures.

- Actual property taxes were over budget by \$20,337. This difference occurred because the Village was conservative in budgeting growth in taxable value.
- Village Clerk expenses were under budget by \$15,308. The difference occurred because the Clerk's wages were allocated to other areas differently than originally budgeted.
- Actual public works expenses were under budget by \$43,758. The difference occurred because funds budgeted for contracted services and sidewalks were not spent. In addition, health insurance costs were less than budgeted.
- Actual parks expenses were under budget by \$15,769. This difference occurred because all budgeted projects did not occur.

Capital Assets Administration

The Village's investment in capital assets for its governmental and business-type activities as of February 28, 2007 totaled \$5,905,468 (net of accumulated depreciation). This investment in capital assets includes land, buildings, infrastructure, improvements, machinery, equipment, plants and vehicles.

Major capital asset events during the current fiscal year included the following:

- A new spreader for a dump truck was purchased for \$8,500.
- A new police cruiser was purchased for \$16,771.
- Construction was completed on a new salt shed for \$26,432 in the current year.
- Preliminary work has continued on sewer plant improvements for \$164,102.

Capital Assets (Net of Accumulated Depreciation)

	Governmental Activities		Business-type Activities		Total	
	2007	2006	2007	2006	2007	2006
Land	\$ 295,593	\$ 295,593	\$ -	\$ -	\$ 295,593	\$ 295,593
Construction in progress	-	9,880	276,025	111,923	276,025	121,803
Buildings and improvements	87,447	62,719	-	-	87,447	62,719
Vehicles and equipment	237,003	261,190	-	-	237,003	261,190
Infrastructure	2,154,435	2,304,239	2,854,965	2,910,684	5,009,400	5,214,923
Total	\$ 2,774,478	\$ 2,933,621	\$ 3,130,990	\$ 3,022,607	\$ 5,905,468	\$ 5,956,228

Additional information on the Village's capital assets can be found in Note D of the "Notes to the Financial Statements" of this report.

Long-term debt. At the end of the 2007 fiscal year, the Village had total outstanding debt of \$2,530,202 consisting of general obligations bonds, revenue bonds and compensated absences. The general obligation debt of \$1,312,270 in governmental funds is backed by the full-faith and credit of the Village. \$1,140,000 of the Village's outstanding debt represented in table below is recorded as revenue bonds. The payment of this debt service is anticipated through the revenues generated from the water and sewer services in the enterprise funds.

Outstanding Debt

	Governmental Activities		Business-type Activities		Total	
	2007	2006	2007	2006	2007	2006
General obligation bonds	\$ 1,312,270	\$ 1,401,507	\$ -	\$ -	\$ 1,312,270	\$ 1,401,507
Compensated absences	77,932	103,900	-	-	77,932	103,900
Revenue bonds	-	-	1,140,000	1,200,000	1,140,000	1,200,000
Total	<u>\$ 1,390,202</u>	<u>\$ 1,505,407</u>	<u>\$ 1,140,000</u>	<u>\$ 1,200,000</u>	<u>\$ 2,530,202</u>	<u>\$ 2,705,407</u>

The Village's total debt decreased by \$175,205 during the fiscal year. This reduction was due to normal debt payoffs as provided for in the fiscal year 2007 budget.

Additional information on the Village's long-term debt can be found in Note G of the "Notes to the Financial Statements" of this report.

General Economic Overview

In future budgets the Village's finances may continue to dwindle as additional cuts in state revenue sharing are possible and the cost of providing services continues to rise.

In 2008, the Village will begin phase 2 of improvements to the Wastewater Treatment Plant. Completion of the project is anticipated in the fall of 2008. However, delays in land acquisition and the State Revolving Fund (SRF) re-financing proposal may cause construction schedules to change. The improvements will be financed with a Rural Development loan at 4.5% interest rate over a forty year term. The Village is anticipating that it will receive approximately \$690,000 in grant money leaving \$3,010,000 to finance. The Village of Shelby is on schedule to refinance the project using a State Revolving Fund (SRF) loan. The SRF re-finance will save the utility approximately \$2,500,000 dollars in interest because it will be over a twenty year term rather than a forty year term and will have a lower interest rate. However, customers will likely not see a reduction in the monthly cost to them as the SRF shorter term loan will keep the annual debt service nearly the same as the longer term higher interest rate Rural Development loan. One other benefit to the re-finance is the utility will be out of debt in twenty years and be in a position to begin more upgrades to the utility, if necessary, without piling new debt on top of old debt.

Other future expenditures that the Village can expect may include rehab of the elevated water storage facility, replacement of old and undersized water mains, replacement and construction of sidewalks, improvements to the Village parks, tree planting, street maintenance and construction of new Village facilities. These projects will occur over the next several years.

The Village Board and staff remain optimistic that the Village's economic stability will be enhanced by several projects in various stages of development among them is the current housing project known as Northland Crossing's which will provide thirteen new homes. The Northland Crossings project is nearing completion with all thirteen homes in various stages of construction. The Devonwood Drive Senior Condominium project has completed the infrastructure and street portion. Devonwood Drive has one unit finished and the developers are actively trying to sell additional units. A new development for the Village of Shelby called Barnett Station has been proposed as a multi-family apartment complex. This project has met with some difficulties in financing due to the economic state of Michigan and is currently on hold.

During the Village's budget process, it was recognized that further stabilization in revenues were needed in the water and sewer utilities. The water utility had a substantial increase in rates in 2001 and it appears, unless determined by an ongoing revenue review process, that no increase will be necessary until the 2008-2009 fiscal budget. The sewer utility revenue review indicates that a rate increase is necessary as soon as possible. The rate increase is driven by several factors, (1) wastewater treatment plant upgrades, (2) rate reduction in 2001 and (3) summer discounts. The rate increased in October of 2005 from a ready-to-serve charge of \$11.50 to \$30.00 per quarter and the commodity charge from \$0.85 to \$1.50 per hundred cubic feet. This was the first of three increases anticipated. The amount of the second increase is still under discussion.

The Village of Shelby anticipates taking steps to offset the declining revenues by trying to stabilize the increasing cost of providing services to the community. Some of these steps to offset the declining revenues may include review of the current employee benefit plan, reducing the level of services or, if it becomes necessary, reducing the labor force. The result of these actions may be reflected in the 2007-2008 final expenditures as adjustments are made, however, it should be noted that in some cases these actions may effectively only slow the rate of increase in expenditures but not actually reduce them.

Requests for Information

This financial report is designed to provide a general overview of the Village of Shelby's finances for all those with an interest. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Village of Shelby, 189 Maple Street, Suite B, Shelby, Michigan 49455, (231) 861-4400.

BRICKLEY DELONG

CERTIFIED PUBLIC ACCOUNTANTS

INDEPENDENT AUDITORS' REPORT

July 27, 2007

Village Council
Village of Shelby
Shelby, Michigan

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the Village of Shelby as of and for the year ended February 28, 2007, which collectively comprise the Village of Shelby's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Village of Shelby's management. Our responsibility is to express opinions of 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, each major fund and the aggregate remaining fund information of the Village of Shelby, as of February 28, 2007, and the respective changes in financial position and, where applicable, cash flows 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 budgetary comparison information on pages i - viii and 26 - 28, are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.



Village of Shelby
STATEMENT OF NET ASSETS
February 28, 2007

ASSETS

	<u>Governmental activities</u>	<u>Business-type activities</u>	<u>Total</u>
CURRENT ASSETS			
Cash and investments	\$ 1,676,828	\$ 665,117	\$ 2,341,945
Receivables	60,879	76,106	136,985
Due from other governmental units	113,895	-	113,895
Internal balances	246,654	(246,654)	-
Inventories	-	35,643	35,643
Total current assets	<u>2,098,256</u>	<u>530,212</u>	<u>2,628,468</u>
NONCURRENT ASSETS			
Restricted assets	-	54,730	54,730
Capital assets, net			
Nondepreciable	295,593	276,025	571,618
Depreciable	2,478,885	2,854,965	5,333,850
Bond issuance costs, net	43,853	20,231	64,084
Total noncurrent assets	<u>2,818,331</u>	<u>3,205,951</u>	<u>6,024,282</u>
Total assets	<u>4,916,587</u>	<u>3,736,163</u>	<u>8,652,750</u>
LIABILITIES AND NET ASSETS			
CURRENT LIABILITIES			
Accounts payable and accrued liabilities	17,645	22,267	39,912
Bonds and other obligations, due within one year	140,000	60,000	200,000
Total current liabilities	<u>157,645</u>	<u>82,267</u>	<u>239,912</u>
NONCURRENT LIABILITIES			
Bonds and other obligations, less amounts due within one year	1,250,202	1,080,000	2,330,202
Total liabilities	<u>1,407,847</u>	<u>1,162,267</u>	<u>2,570,114</u>
NET ASSETS			
Invested in capital assets, net of related debt	1,506,061	1,779,221	3,285,282
Restricted for:			
Streets and highways	953,368	-	953,368
Debt service	112,527	54,730	167,257
Unrestricted	936,784	739,945	1,676,729
Total net assets	<u>\$ 3,508,740</u>	<u>\$ 2,573,896</u>	<u>\$ 6,082,636</u>

The accompanying notes are an integral part of this statement.

Village of Shelby
STATEMENT OF ACTIVITIES
For the year ended February 28, 2007

<i>Functions/Programs</i>	Expenses	Program Revenue			Net (Expense) Revenue and Changes in Net Assets		
		Charges for services	Operating grants and contributions	Capital grants and contributions	Governmental activities	Business-type activities	Total
Governmental activities							
General government	\$ 89,517	\$ 35,212	\$ -	\$ -	\$ (54,305)	\$ -	\$ (54,305)
Public safety	251,955	-	-	-	(251,955)	-	(251,955)
Public works	504,306	-	230,368	-	(273,938)	-	(273,938)
Culture and recreation	20,536	-	-	-	(20,536)	-	(20,536)
Interest on long-term debt	63,074	-	-	-	(63,074)	-	(63,074)
Total governmental activities	929,388	35,212	230,368	-	(663,808)	-	(663,808)
Business-type activities							
Sewer	118,046	215,923	-	500	-	98,377	98,377
Water	259,429	266,805	260	509	-	8,145	8,145
Total business-type activities	377,475	482,728	260	1,009	-	106,522	106,522
Total government	\$ <u>1,306,863</u>	\$ <u>517,940</u>	\$ <u>230,628</u>	\$ <u>1,009</u>	(663,808)	106,522	(557,286)
General revenues							
Property taxes, levied for							
General purposes					305,337	-	305,337
Specific purposes					208,778	-	208,778
Grants and contributions not restricted to specific programs					214,880	-	214,880
Unrestricted investment earnings					25,801	16,041	41,842
Miscellaneous					5,611	19,115	24,726
Total general revenues					760,407	35,156	795,563
Change in net assets					96,599	141,678	238,277
Net assets at March 1, 2006					3,412,141	2,432,218	5,844,359
Net assets at February 28, 2007					\$ <u>3,508,740</u>	\$ <u>2,573,896</u>	\$ <u>6,082,636</u>

The accompanying notes are an integral part of this statement.

Village of Shelby
BALANCE SHEET
 Governmental Funds
 February 28, 2007

	General Fund	Major Streets Fund	Local Streets Fund	Debt Service Fund	Total governmental funds
ASSETS					
Cash and investments	\$ 414,907	\$ 404,150	\$ 498,774	\$ 97,211	\$ 1,415,042
Receivables					
Property taxes	35,288	-	8,812	15,316	59,416
Other	1,463	-	-	-	1,463
Due from other governmental units	64,015	27,936	21,945	-	113,896
Advances to other funds	200,000	-	-	-	200,000
Total assets	\$ 715,673	\$ 432,086	\$ 529,531	\$ 112,527	\$ 1,789,817
LIABILITIES AND FUND BALANCES					
Liabilities					
Accounts payable	\$ 1,886	\$ 3,877	\$ 4,372	\$ -	\$ 10,135
Accrued liabilities	4,383	-	-	-	4,383
Total liabilities	6,269	3,877	4,372	-	14,518
Fund balances					
Reserved for:					
Advances	200,000	-	-	-	200,000
Debt service	-	-	-	112,527	112,527
Unreserved, undesignated					
General Fund	509,404	-	-	-	509,404
Special revenue funds	-	428,209	525,159	-	953,368
Total fund balances	709,404	428,209	525,159	112,527	1,775,299
Total liabilities and fund balances	\$ 715,673	\$ 432,086	\$ 529,531	\$ 112,527	\$ 1,789,817

The accompanying notes are an integral part of this statement.

Village of Shelby
**RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET
 TO THE STATEMENT OF NET ASSETS**
 February 28, 2007

Total fund balance—governmental funds \$ 1,775,299

Amounts reported for governmental activities in the Statement of Net Assets
 are different because:

Capital assets used in governmental activities are not financial resources and
 are not reported in the governmental funds.

Cost of capital assets	\$ 3,767,117	
Accumulated depreciation	<u>(1,229,642)</u>	2,537,475

Bond issuance costs are not capitalized and amortized in the governmental funds.

Bond issuance costs	55,714	
Accumulated amortization	<u>(11,861)</u>	43,853

Long-term liabilities in governmental activities are not due and payable in the
 current period and are not reported in the governmental funds.

Bonds and notes payable	(1,312,270)	
Compensated absences	<u>(77,932)</u>	(1,390,202)

Internal service funds are used by management to charge the costs of certain activities
 to individual funds. The assets and liabilities of the internal service fund are reported
 with governmental activities in the Statement of Net Assets.

542,315

Net assets of governmental activities in the Statement of Net Assets	<u>\$ 3,508,740</u>
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The accompanying notes are an integral part of this statement.

Village of Shelby
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
 Governmental Funds
 For the year ended February 28, 2007

	General Fund	Major Streets Fund	Local Streets Fund	Debt Service Fund	Total governmental funds
REVENUES					
Property taxes	\$ 305,337	\$ -	\$ 76,244	\$ 132,534	\$ 514,115
Intergovernmental revenues - State	214,880	150,323	57,780	-	422,983
Charges for services	35,212	-	-	-	35,212
Fines and forfeitures	1,316	-	-	-	1,316
Investment earnings	17,572	10,521	11,744	1,958	41,795
Other	3,920	176	199	-	4,295
Total revenues	<u>578,237</u>	<u>161,020</u>	<u>145,967</u>	<u>134,492</u>	<u>1,019,716</u>
EXPENDITURES					
Current					
General government	79,031	-	-	-	79,031
Public safety	266,812	-	-	-	266,812
Public works	215,145	54,616	65,277	-	335,038
Culture and recreation	18,588	-	-	-	18,588
Debt service					
Principal	-	25,000	-	70,000	95,000
Interest and fees	-	3,094	-	48,303	51,397
Capital outlay	-	13,047	13,385	-	26,432
Total expenditures	<u>579,576</u>	<u>95,757</u>	<u>78,662</u>	<u>118,303</u>	<u>872,298</u>
Net change in fund balances	(1,339)	65,263	67,305	16,189	147,418
Fund balances at March 1, 2006	<u>710,743</u>	<u>362,946</u>	<u>457,854</u>	<u>96,338</u>	<u>1,627,881</u>
Fund balances at February 28, 2007	<u>\$ 709,404</u>	<u>\$ 428,209</u>	<u>\$ 525,159</u>	<u>\$ 112,527</u>	<u>\$ 1,775,299</u>

The accompanying notes are an integral part of this statement.

Village of Shelby
**RECONCILIATION OF THE GOVERNMENTAL FUNDS STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES TO THE STATEMENT OF ACTIVITIES**
For the year ended February 28, 2007

Net change in fund balances—total governmental funds \$ 147,418

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

Governmental funds report outlays for capital assets and bond issuance costs as expenditures; in the Statement of Activities, these costs are depreciated and amortized over their estimated useful lives, respectively.

Depreciation and amortization expense	\$ (167,303)	
Capital outlay	<u>26,432</u>	(140,871)

Repayment of principal on long-term debt is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the Statement of Net Assets.	89,237
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Compensated absences are reported on the accrual method in the Statement of Activities and reported as expenditures when financial resources are used in the governmental funds.	25,968
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The internal service funds are used by management to charge the costs of certain activities to individual funds. The net change of the internal service funds is reported with governmental activities.	<u>(25,153)</u>
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Change in net assets of governmental activities	<u><u>\$ 96,599</u></u>
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The accompanying notes are an integral part of this statement.

Village of Shelby
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
 Proprietary Funds
 For the year ended February 28, 2007

	Business-type activities - Enterprise funds			Governmental activities - Internal Service Fund
	Sewer	Water	Total	
REVENUES				
Charges for services	\$ 215,923	\$ 266,805	\$ 482,728	\$ 125,469
Other	5,066	14,309	19,375	1,139
Total operating revenues	220,989	281,114	502,103	126,608
OPERATING EXPENSES				
Operations and administration	95,247	180,474	275,721	116,196
Depreciation and amortization	19,827	44,690	64,517	49,458
Total operating expenses	115,074	225,164	340,238	165,654
Operating income (loss)	105,915	55,950	161,865	(39,046)
NONOPERATING REVENUES (EXPENSES)				
Investment earnings	5,465	10,576	16,041	6,271
Connection fees	500	509	1,009	-
Interest expense	(240)	(29,375)	(29,615)	-
Total nonoperating revenue (expenses)	5,725	(18,290)	(12,565)	6,271
Change in net assets	111,640	37,660	149,300	(32,775)
Net assets at March 1, 2006	1,070,143	1,369,107		560,436
Net assets at February 28, 2007	\$ 1,181,783	\$ 1,406,767		\$ 527,661
Adjustment to reflect the consolidation of internal service fund activities related to enterprise funds			(7,622)	
Change in net assets of business-type activities			\$ 141,678	

The accompanying notes are an integral part of this statement.

Village of Shelby
STATEMENT OF CASH FLOWS
 Proprietary Funds
 For the year ended February 28, 2007

	Business-type activities - Enterprise funds			Governmental
	Sewer	Water	Total	activities - Internal Service Fund
CASH FLOWS FROM OPERATING ACTIVITIES				
Receipts from customers	\$ 222,847	\$ 294,321	\$ 517,168	\$ -
Receipts from interfund services provided	-	-	-	126,608
Payments to suppliers	(32,723)	(85,747)	(118,470)	(71,449)
Payments to employees	(50,326)	(65,918)	(116,244)	(29,618)
Payment for interfund services used	(12,198)	(23,790)	(35,988)	(12,000)
Net cash provided by operating activities	127,600	118,866	246,466	13,541
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES				
Advances from other funds (net)	192,000	-	192,000	8,000
Connection fees	500	509	1,009	-
Purchases of capital assets	(210,664)	-	(210,664)	(25,271)
Principal paid on capital debt	-	(60,000)	(60,000)	-
Interest paid on capital debt	(240)	(30,000)	(30,240)	-
Net cash used for capital and related financing activities	(18,404)	(89,491)	(107,895)	(17,271)
CASH FLOW FROM INVESTING ACTIVITIES				
Investment earnings	5,465	10,576	16,041	6,271
Net increase in cash and investments	114,661	39,951	154,612	2,541
Cash and investments at March 1, 2006	124,263	440,972	565,235	259,246
Cash and investments at February 28, 2007	\$ 238,924	\$ 480,923	\$ 719,847	\$ 261,787
Reconciliation of cash and investments to the balance sheet				
Cash and investments	\$ 238,924	\$ 426,193	\$ 665,117	\$ 261,787
Restricted assets	-	54,730	54,730	-
	\$ 238,924	\$ 480,923	\$ 719,847	\$ 261,787
Reconciliation of operating income (loss) to net cash provided by operating activities				
Operating income (loss)	\$ 105,915	\$ 55,950	\$ 161,865	\$ (39,046)
Adjustments to reconcile operating income (loss) to net cash provided by operating activities				
Depreciation and amortization expense	19,827	44,690	64,517	49,458
Change in assets and liabilities				
Accounts receivable	1,858	13,207	15,065	-
Inventories	-	4,193	4,193	-
Accounts payable	-	826	826	3,129
Net cash provided by operating activities	\$ 127,600	\$ 118,866	\$ 246,466	\$ 13,541

The accompanying notes are an integral part of this statement.

Village of Shelby
STATEMENT OF FIDUCIARY ASSETS AND LIABILITIES
Fiduciary Funds
February 28, 2007

	<u>Agency Fund</u>
ASSETS	
Cash and investments	\$ <u><u> -</u></u>
LIABILITIES	
Deposits held for others	\$ <u><u> -</u></u>

The accompanying notes are an integral part of this statement.

Village of Shelby
NOTES TO FINANCIAL STATEMENTS
February 28, 2007

NOTE A—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Village of Shelby (Village) have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the Village's accounting policies are described below.

Reporting Entity

The Village is a municipal corporation governed by a seven-member council.

Generally accepted accounting principles require that if the Village has certain oversight responsibilities over other organizations, those organizations should be included in the Village's financial statements. Since no organizations met this criteria, none are included in the financial statements.

Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all of the nonfiduciary activities of the Village. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

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 requirement of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues. The Village does not allocate indirect costs.

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, as are the proprietary fund and fiduciary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Village of Shelby
NOTES TO FINANCIAL STATEMENTS
February 28, 2007

NOTE A—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Measurement Focus, Basis of Accounting and Financial Statement Presentation—Continued

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

The Village reports the following major governmental funds:

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

The Major Street Fund and Local Street Fund account for money distributed by the State of Michigan for street maintenance.

The Debt Service Fund is used to account for principal and interest payments on the Village's general debt.

The Village reports the following two major proprietary funds:

The Sewer Fund operates the Village's sewage pumping station, collection systems, and treatment systems.

The Water Fund operates the Village's water distribution system.

Additionally, the Village reports the following fund types:

Internal service funds account for equipment management services provided to other funds of the government on a cost reimbursement basis.

Agency funds account for all assets held by the Village on behalf of others in a fiduciary capacity.

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 Government 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 Village 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. Exceptions to this general rule are payments-in-lieu of taxes and other charges between the Village's water and sewer function and various other functions of the government. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

Village of Shelby
NOTES TO FINANCIAL STATEMENTS
February 28, 2007

NOTE A—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Measurement Focus, Basis of Accounting and Financial Statement Presentation—Continued

Amounts reported as program revenues 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. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues are charges to customers for sales and services. The enterprise funds also recognizes as operating revenue the portion of tap fees intended to recover the cost of connecting new customers to the system. Operating expenses for proprietary 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 Village's policy to use restricted resources first, then unrestricted resources as they are needed.

Assets, Liabilities and Net Assets or Equity

Deposits and Investments

The Village's cash and cash equivalents are considered to be cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition.

The Village reports its investments in accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. Under this standard, certain investments are valued at fair value as determined by quoted market prices or by estimated fair values when quoted market prices are not available. The standard also provides that certain investments are valued at cost (or amortized cost) when they are of short-term duration, the rate of return is fixed, and the Village intends to hold the investment until maturity.

The Village has adopted an investment policy in compliance with State of Michigan statutes. Those statutes authorize the Village to invest in obligations of the United States, certificates of deposit, prime commercial paper, securities guaranteed by United States agencies or instrumentalities, United States government or federal agency obligation repurchase agreements, bankers acceptances, state-approved investment pools and certain mutual funds.

Receivables and Payables

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds". Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances".

Village of Shelby
NOTES TO FINANCIAL STATEMENTS
February 28, 2007

NOTE A—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Assets, Liabilities and Net Assets or Equity—Continued

Receivables and Payables—Continued

Advances between funds, as reported in the fund financial statements, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

All trade and property tax receivables are shown net of allowance for uncollectibles.

The Village bills and collects its own property taxes. Taxes are levied on each July 1 on the taxable valuation of property (as defined by state statutes) located in the Local Governmental Unit as of the preceding December 31. Uncollected real property taxes as of September 15 are turned over by the Village to the County for collection. The County advances the Village all these delinquent real property taxes. The delinquent personal property taxes remain the responsibility of the Village. The Village recognizes available revenue from the current tax levy. Available means collected within the current period or expected to be collected soon enough thereafter to be used to pay liabilities of the current period (60 days).

The 2006 state taxable value for real/personal property of the Village totaled approximately \$27,729,000. The ad valorem taxes levied consisted of 10.9437 mills for operating purposes, 2.7328 mills for local streets and 4.75 for debt service. These amounts are recognized in the respective General Fund, Local Streets Fund and Debt Service Fund.

Inventories

All inventories are valued at cost using the first-in/first-out (FIFO) method. Inventories of governmental funds are recorded as expenditures when consumed rather than when purchased.

Restricted Assets

Certain proceeds of the Enterprise Fund revenue bonds, as well as certain resources set aside for their repayment, are classified as restricted assets on the balance sheet because they are maintained in separate bank accounts and their use is limited by applicable bond covenants.

Capital Assets

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

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

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets of business-type activities is included as part of the capitalized value of the assets constructed.

Village of Shelby
NOTES TO FINANCIAL STATEMENTS
February 28, 2007

NOTE A—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued

Assets, Liabilities and Net Assets or Equity—Continued

Capital Assets—Continued

In the case of the initial capitalization of general infrastructure assets (i.e., those reported by governmental activities), the Village chose to include all such items regardless of their acquisition date or amount. The Village was able to obtain the historical cost of the initial reporting of these assets by recording the actual costs incurred by the Village.

Property, plant and equipment are depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Buildings and improvements	40
Infrastructure	20
Plants and systems	20-80
Vehicles and equipment	5-10

Compensated Absences

Village employees are granted vacation and sick leave in varying amounts based on length of service. Accumulated vacation must be taken no later than two years after it is earned. Upon termination, employees are paid for unused vacation at their current rates. Sick leave is accumulated at the rate of one day per month of employment. Unused sick leave is accumulated up to 80 days for employees. Unused accumulated sick leave is paid to employees who resign or retire, limited to 50 percent of days accumulated up to a maximum of 35 days. All vacation and sick pay is accrued when incurred in the government-wide and proprietary fund financial statements. The current portion of this liability is estimated based on historical trends. A liability for these amounts is reported in governmental funds only if they have matured, for example, as a result of employee resignations and retirements.

Long-Term Obligations

In the government-wide financial statements and proprietary fund types in the fund financial statements, 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 on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

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.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures.

Village of Shelby
NOTES TO FINANCIAL STATEMENTS
February 28, 2007

NOTE B—STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Budgetary Information

Annual budgets are adopted on a basis consistent with generally accepted accounting principles for all governmental funds. All annual appropriations lapse at fiscal year end.

The Village follows these procedures in establishing the budgetary information provided in the financial statements:

- a. Prior to the first Monday of January, the Village president submits to the Village Council a proposed operating budget for the year commencing the following March 1. The operating budget includes proposed expenditures and the means of financing them.
- b. Public hearings are conducted at the Village Hall to obtain taxpayer comments.
- c. Not later than the second Monday in February, the budget is legally enacted through passage of a resolution.
- d. Supplemental appropriations, when required to provide for additional expenditures, are matched by additional anticipated revenues or an appropriation of available fund balance and must be approved by the Village Council. All appropriations lapse at year end.

The appropriated budget is prepared by fund, function and department. The Village's department heads may make transfers of appropriations within a department. Transfers of appropriations between departments require the approval of the Village Council. The legal level of budgetary control is the department level. The Village Council made several supplemental budgetary appropriations throughout the year.

NOTE C—DEPOSITS AND INVESTMENTS

As of February 28, 2007, the Village had the following investments:

Investment Type	<u>Fair value</u>	<u>Weighted average maturity (Days)</u>	<u>Moody's</u>	<u>Percent</u>
Money market mutual fund	\$ 762,591	41	AAA	100 %

Interest rate risk. The Village does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit risk. State law limits investments in commercial paper and corporate bonds to the two highest classifications issued by nationally recognized statistical rating organizations. The Village has no investment policy that would further limit its investment choices.

Village of Shelby
NOTES TO FINANCIAL STATEMENTS
February 28, 2007

NOTE C—DEPOSITS AND INVESTMENTS—Continued

Concentration of credit risk. The Village does not have a concentration of credit risk policy. Concentration of credit risk is the risk of loss attributed to the magnitude of the Village investment in a single issuer, by diversifying the investment portfolio so that the impact of potential losses from any one type of security or issuer will be minimized. The Village does not have any investments exposed to concentration of credit risk.

Custodial credit risk – deposits. In the case of deposits, this is the risk that in the event of a bank failure, the Village's deposits may not be returned to it. As of February 28, 2007, \$1,361,205 of the Village's bank balance of \$1,669,115 was exposed to custodial credit risk because it was uninsured and uncollateralized.

Custodial credit risk – investments. The Village does not have a custodial credit risk policy for investments. This is the risk that, in the event of the failure of the counterparty, the Village will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The Village does not have any investments exposed to custodial credit risk.

Foreign currency risk. The Village is not authorized to invest in investments which have this type of risk.

Restricted Assets

Restrictions are placed on assets by bond ordinance and Village Council action. At February 28, 2007, restricted cash in the Enterprise funds are restricted as follows:

Water Fund - Reserve Account	\$ <u>54,730</u>
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NOTE D—CAPITAL ASSETS

Capital asset activity for the year ended February 28, 2007 was as follows:

	Balance March 1, 2006	Additions	Deductions	Balance February 28, 2007
Governmental activities:				
Capital assets, not being depreciated:				
Land	\$ 295,593	\$ -	\$ -	\$ 295,593
Construction in progress	9,880	26,432	36,312	-
Total capital assets, not being depreciated	305,473	26,432	36,312	295,593
Capital assets, being depreciated:				
Buildings and improvements	439,140	36,312	-	475,452
Infrastructure	2,996,072	-	-	2,996,072
Vehicles and equipment	548,812	25,271	-	574,083
Total capital assets, being depreciated	3,984,024	61,583	-	4,045,607

Village of Shelby
NOTES TO FINANCIAL STATEMENTS
February 28, 2007

NOTE D—CAPITAL ASSETS—Continued

	Balance March 1, 2006	Additions	Deductions	Balance February 28, 2007
Governmental activities:—Continued				
Less accumulated depreciation:				
Buildings and improvements	\$ 376,421	\$ 11,584	\$ -	\$ 388,005
Infrastructure	691,833	149,804	-	841,637
Vehicles and equipment	287,622	49,458	-	337,080
Total accumulated depreciation	<u>1,355,876</u>	<u>210,846</u>	<u>-</u>	<u>1,566,722</u>
Total capital assets, being depreciated, net	<u>2,628,148</u>	<u>(149,263)</u>	<u>-</u>	<u>2,478,885</u>
Capital assets, net	<u>\$ 2,933,621</u>	<u>\$ (122,831)</u>	<u>\$ 36,312</u>	<u>\$ 2,774,478</u>
Business-type activities:				
Capital assets, not being depreciated:				
Construction in progress	\$ 111,923	\$ 164,102	\$ -	\$ 276,025
Capital assets, being depreciated:				
Plants and systems	4,127,127	7,500	-	4,134,627
Less accumulated depreciation	<u>(1,216,443)</u>	<u>(63,219)</u>	<u>-</u>	<u>(1,279,662)</u>
Total capital assets, being depreciated, net	<u>2,910,684</u>	<u>(55,719)</u>	<u>-</u>	<u>2,854,965</u>
Capital assets, net	<u>\$ 3,022,607</u>	<u>\$ 108,383</u>	<u>\$ -</u>	<u>\$ 3,130,990</u>

Depreciation expense has been charged to functions as follows:

Government activities:	
General government	\$ 10,486
Public safety	493
Public works	150,409
Internal Service Fund depreciation is charged to the various programs based on their usage of the assets	<u>49,458</u>
	<u>\$ 210,846</u>
Business-type activities:	
Sewer	\$ 19,827
Water	<u>43,392</u>
	<u>\$ 63,219</u>

Village of Shelby
NOTES TO FINANCIAL STATEMENTS
February 28, 2007

NOTE E—BOND ISSUANCE COSTS

Bond issuance cost activity for the year ended February 28, 2007 was as follows:

	Balance March 1, 2006	Additions	Deductions	Balance February 28, 2007
Governmental activities:				
Bond issuance costs	\$ 55,714	\$ -	\$ -	\$ 55,714
Less accumulated amortization	<u>5,946</u>	<u>5,915</u>	<u>-</u>	<u>11,861</u>
Bond issuance costs, net	<u>\$ 49,768</u>	<u>\$ (5,915)</u>	<u>\$ -</u>	<u>\$ 43,853</u>
Business-type activities:				
Bond issuance costs	\$ 25,964	\$ -	\$ -	\$ 25,964
Less accumulated amortization	<u>4,435</u>	<u>1,298</u>	<u>-</u>	<u>5,733</u>
Bond issuance costs, net	<u>\$ 21,529</u>	<u>\$ (1,298)</u>	<u>\$ -</u>	<u>\$ 20,231</u>

Amortization

Amortization expense has been charged to functions as follows:

Governmental activities:	
Interest on long-term debt	\$ <u>5,915</u>
Business-type activities:	
Water	\$ <u>1,298</u>

NOTE F—INTERFUND RECEIVABLES, PAYABLES AND TRANSFERS

Advances to/from other funds:

The Equipment Fund advance to the Sewer Fund of \$32,000 and the General Fund advance to the Sewer Fund of \$200,000 represent interfund loans used to pay for preliminary work on sewer plant improvements.

Village of Shelby
NOTES TO FINANCIAL STATEMENTS
February 28, 2007

NOTE G—LONG-TERM DEBT

Summary of Changes in Long-Term Liabilities

The following is a summary of long-term liabilities activity for the Village for the year ended February 28, 2007.

	Balance March 1, 2006	Additions	Reductions	Balance February 28, 2007	Due within one year
Governmental activities:					
General obligation bonds	\$ 1,401,507	\$ -	\$ 89,237	\$ 1,312,270	\$ 95,000
Compensated absences	<u>103,900</u>	<u>47,419</u>	<u>73,387</u>	<u>77,932</u>	<u>45,000</u>
Governmental activity long-term liabilities	<u>\$ 1,505,407</u>	<u>\$ 47,419</u>	<u>\$ 162,624</u>	<u>\$ 1,390,202</u>	<u>\$ 140,000</u>
Business-type activities:					
Revenue bonds	<u>\$ 1,200,000</u>	<u>\$ -</u>	<u>\$ 60,000</u>	<u>\$ 1,140,000</u>	<u>\$ 60,000</u>
Governmental activities:					
General obligation bonds:					
\$175,000 Michigan Transportation Fund bonds of 1999; payable in annual installments of \$25,000 through September 2008; interest at rates varying from 4% to 4.55%				\$ 50,000	
\$1,325,000 Unlimited Tax General Obligation Refunding Bonds of 2005; payable in annual installments of \$60,000 to \$130,000 through September 2019; interest at rates varying from 2.75% to 4.25%				1,305,000	
Plus issuance premium				12,395	
Less deferred amount on refunding				<u>(55,125)</u>	
				1,312,270	
Compensated absences				<u>77,932</u>	
				<u>\$ 1,390,202</u>	

Village of Shelby
NOTES TO FINANCIAL STATEMENTS
February 28, 2007

NOTE G—LONG-TERM DEBT—Continued

Summary of Changes in Long-Term Liabilities—Continued

Business-type activities:

Revenue bonds:

\$1,365,000 Water Supply System Revenue

Bonds, Series 2002 due in annual installments
of \$60,000 to \$85,000 through October 2022;
interest at 2.5%

\$ 1,140,000

For governmental activities, claims and judgments and compensated absences are generally liquidated by the General Fund.

The general obligation bonds are backed by the full faith and credit of the Village.

The Village was in compliance in all material respects with all the revenue bond ordinances at February 28, 2007.

Annual debt service requirements to maturity for debt outstanding as of February 28, 2007 follows:

Year ending February 28,	Governmental activities		Business-type activities	
	Principal	Interest	Principal	Interest
2008	\$ 95,000	\$ 47,300	\$ 60,000	\$ 28,500
2009	100,000	44,219	60,000	27,000
2010	85,000	40,775	60,000	25,500
2011	85,000	38,225	65,000	24,000
2012	100,000	35,450	65,000	22,375
2013-2017	580,000	123,489	350,000	86,750
2018-2022	310,000	16,998	395,000	40,875
2023	-	-	85,000	2,125
Total	\$ <u>1,355,000</u>	\$ <u>346,456</u>	\$ <u>1,140,000</u>	\$ <u>257,125</u>

Village of Shelby
NOTES TO FINANCIAL STATEMENTS
February 28, 2007

NOTE H—OTHER INFORMATION

Risk Management

The Village is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees and natural disasters. The Village manages its liability and property risk by participating in Michigan Municipal Liability and Property Pool (MMLPP), a public entity risk pool providing property and liability coverage to its participating members. The Village pays an annual premium to MMLPP for its insurance coverage. The MMLPP is self-sustaining through member premiums and provides, subject to certain deductibles, occurrence-based casualty coverage for each incident and occurrence-based property coverage to its members by internally assuring certain risks and reinsuring risks through commercial companies. Various deductibles are maintained to place the responsibility for small charges with the insured. Settled claims resulting from these risks have not exceeded insurance coverage in any of the past three fiscal years.

The Village manages its workers' compensation risk by participating in the Michigan Municipal Workers' Compensation Fund (MMWCF), a public entity risk pool providing workers' compensation coverage to its participating members. The Village pays an annual premium to MMWCF for its workers' compensation coverage. The MMWCF is self-sustaining through member premiums and provides statutory workers' compensation coverage to its members by internally assuring certain risks and reinsuring risks through commercial companies. Settled claims resulting from these risks have not exceeded insurance coverage in any of the past three fiscal years.

The Village carries commercial insurance for employee health and accident insurance. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

Contingent Liabilities

Amounts received or receivable from grant agencies are subject to audit and adjustment by grantor agencies, principally the federal government. Any disallowed claims, including amounts already collected, may constitute a liability to the applicable funds. The amount, if any, of expenditures that may be disallowed by the grantor cannot be determined at this time, although the Village expects such amounts, if any, to be immaterial.

NOTE I—PENSION PLAN

The Village provides pension benefits for all of its full-time employees through a defined contribution plan. In a defined contribution plan, benefits depend solely on amounts contributed to the Plan plus investment earnings. The Plan is administered through Lincoln Financial Group, an independent third party. The Village and employees are required to contribute 4 percent and 2 percent, respectively, of the qualified employees' annual compensation each plan year. For the year ended February 28, 2007, pension expense was approximately \$12,200. Employee contributions were approximately \$11,000.

Village of Shelby
NOTES TO FINANCIAL STATEMENTS
February 28, 2007

NOTE J—ECONOMIC DEPENDENCY

State of Michigan shared revenues represent 37 percent of General Fund revenues.

NOTE K—SUBSEQUENT EVENTS

In March 2007, the Village purchased a new street sweeper for \$35,000.

In May 2007, the Village approved a contract for \$2,050,000 for wastewater system improvements. The project will be funded by a combination of a grant and loan from Rural Development.

REQUIRED SUPPLEMENTARY INFORMATION

Village of Shelby
Required Supplementary Information
BUDGETARY COMPARISON SCHEDULE
General Fund
For the year ended February 28, 2007

	Budgeted amounts		Actual	Variance with final budget - positive (negative)
	Original	Final		
REVENUES				
Property taxes	\$ 285,000	\$ 285,000	\$ 305,337	\$ 20,337
Intergovernmental revenues - State	213,400	213,400	214,880	1,480
Charges for services	34,800	34,800	35,212	412
Fines and forfeitures	2,000	2,000	1,316	(684)
Investment earnings	13,000	13,000	17,572	4,572
Other	3,000	3,000	3,920	920
	<u>551,200</u>	<u>551,200</u>	<u>578,237</u>	<u>27,037</u>
EXPENDITURES				
Current				
General government				
Village Council	12,323	12,323	6,653	5,670
Elections Commission	3,250	3,250	844	2,406
Village Clerk	42,770	42,770	27,462	15,308
Village Treasurer	20,715	20,715	12,934	7,781
Village hall/grounds	10,996	10,996	5,752	5,244
Other general government	35,000	35,000	25,386	9,614
Public safety				
Police Department	263,237	263,237	266,812	(3,575)
Public works				
Department of Public Works	258,903	258,903	215,145	43,758
Culture and recreation				
Parks	34,357	34,357	18,588	15,769
	<u>681,551</u>	<u>681,551</u>	<u>579,576</u>	<u>101,975</u>
Net change in fund balance	\$ <u>(130,351)</u>	\$ <u>(130,351)</u>	(1,339)	\$ <u>129,012</u>
Fund balance at March 1, 2006			<u>710,743</u>	
Fund balance at February 28, 2007			\$ <u>709,404</u>	

Village of Shelby
 Required Supplementary Information
BUDGETARY COMPARISON INFORMATION
 Major Streets Fund
 For the year ended February 28, 2007

	Budgeted amounts		Actual	Variance with final budget - positive (negative)
	Original	Final		(negative)
REVENUES				
Intergovernmental revenues - State	\$ 140,000	\$ 140,000	\$ 150,323	\$ 10,323
Investment earnings	3,500	3,500	10,521	7,021
Other	-	-	176	176
Total revenues	143,500	143,500	161,020	17,520
EXPENDITURES				
Current				
Public works				
Routine maintenance	34,432	34,432	14,986	19,446
Traffic services	20,826	20,826	604	20,222
Winter maintenance	51,498	51,498	31,994	19,504
Administration	7,766	7,766	7,032	734
Debt service				
Principal	25,000	25,000	25,000	-
Interest and fees	3,800	3,800	3,094	706
Capital outlay	23,808	23,808	13,047	10,761
Total expenditures	167,130	167,130	95,757	71,373
Net change in fund balance	\$ (23,630)	\$ (23,630)	65,263	\$ 88,893
Fund balance at March 1, 2006			362,946	
Fund balance at February 28, 2007			\$ 428,209	

Village of Shelby
 Required Supplementary Information
BUDGETARY COMPARISON SCHEDULE
 Local Streets Fund
 For the year ended February 28, 2007

	Budgeted amounts		Actual	Variance with final budget - positive (negative)
	Original	Final		(negative)
REVENUES				
Property taxes	\$ 72,000	\$ 72,000	\$ 76,244	\$ 4,244
Intergovernmental revenues - State	46,500	46,500	57,780	11,280
Investment earnings	6,000	6,000	11,744	5,744
Other	100	100	199	99
Total revenues	124,600	124,600	145,967	21,367
EXPENDITURES				
Current				
Public works				
Routine maintenance	34,291	34,291	16,791	17,500
Traffic services	13,083	13,083	866	12,217
Winter maintenance	44,265	44,265	40,046	4,219
Administration	7,616	7,616	7,574	42
Capital outlay	37,566	37,566	13,385	24,181
Total expenditures	136,821	136,821	78,662	58,159
Net change in fund balance	\$ (12,221)	\$ (12,221)	67,305	\$ 79,526
Fund balance at March 1, 2006			457,854	
Fund balance at February 28, 2007			\$ 525,159	

BRICKLEY DELONG

CERTIFIED PUBLIC ACCOUNTANTS

July 27, 2007

Village Council
Village of Shelby
Shelby, Michigan

In planning and performing our audit of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the Village of Shelby as of and for the year ended February 28, 2007, in accordance with auditing standards generally accepted in the United States of America, we considered the Village of Shelby'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 Village of Shelby's internal control. Accordingly, we do not express an opinion on the effectiveness of the Village of Shelby's internal control.

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 a 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.

A material weakness is a significant deficiency, or a 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 internal control was for the limited purpose described in the first paragraph 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 that we consider to be material weaknesses, as defined above. However, we identified and we have attached deficiencies in internal control that we consider to be significant deficiencies.

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



SIGNIFICANT DEFICIENCIES

Recommendation 1: The internal controls surrounding the preparation of formal year end financial statements should be improved.

Small organizations with limited resources and personnel inherently have difficulty in establishing and maintaining effective internal accounting controls related to the preparation and review of the formal year end financial statements.

The Organization should review its procedures surrounding the preparation of year end financial statements to include the appointment of an individual with the requisite technical skills and experience to review the formal year end financial statements and accompanying footnotes, in relation to required disclosures in accordance with generally accepted accounting principles.

Recommendation 2: Receivables and payables should be recorded on the Village's system at year end.

During our detailed testing of account balances, we noted that both accounts receivable and accounts payable were not adjusted to detail at year end.

The performance of a reconciliation at year end would increase the opportunity for accounts receivable and accounts payable activity to be properly recorded in the general ledger. In addition, utility billings accounts receivable should be reconciled to the general ledger on a regular basis throughout the year to provide further assurance that receivables and the related revenue balances are properly stated in interim financial statements.

Recommendation 3: Internal controls should be improved in the police department.

During our interviews of employees and walkthrough of procedures as required under Statement of Auditing Standards No. 99, we became aware that there are inadequate controls over cash receipts in the police department.

Adequate controls over cash receipts, including the use of prenumbered receipts for ordinance infractions, would help to ensure that all cash collected by the police department was adequately controlled, recorded, and accounted for.

We consider the following item contained in our July 5, 2006 letter as still applicable:

Recommendation 1: All journal entries should have documented approval by an appropriate Village official.

We consider the following item contained in our June 27, 2005 letter as still applicable:

Recommendation 1: The internal control procedures should be further segregated within the utility record keeping function.