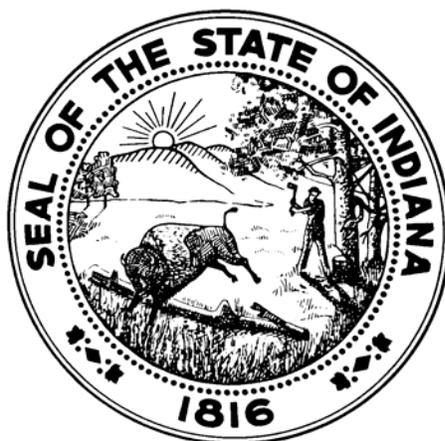


STATE BOARD OF ACCOUNTS
302 West Washington Street
Room E418
INDIANAPOLIS, INDIANA 46204-2765

ANNUAL FINANCIAL REPORT

2005

SANITARY DISTRICT
CITY OF MICHIGAN CITY
LAPORTE COUNTY, INDIANA



FILED
09/11/2006

TABLE OF CONTENTS

<u>Description</u>	<u>Page</u>
Officials	2
Independent Auditor's Report.....	3
Statement of Net Assets.....	4
Statement of Revenues, Expenses and Other Changes in Fund Net Assets	5
Statement of Cash Flows	6
Notes to Financial Statements	7-17
Required Supplementary Information: Schedule of Funding Progress	18
Audit Results and Comments: Capital Asset Records	19
Overdrawn Cash Balance	19
Exit Conference	20
Official Response	21-22

OFFICIALS

<u>Office</u>	<u>Official</u>	<u>Term</u>
Office Manager	Doretha M. Sanders	01-01-05 to 12-31-06
General Manager	Alan J. Walus	01-01-05 to 12-31-06
Controller	John J. Schaefer	01-01-05 to 12-31-06
President of the Board of Sanitary District Commissioners	Boyd Phelps	01-01-05 to 12-31-06
Mayor	Charles E. Oberlie	01-01-04 to 12-31-07



STATE OF INDIANA
AN EQUAL OPPORTUNITY EMPLOYER

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INDEPENDENT AUDITOR'S REPORT

TO: THE OFFICIALS OF THE SANITARY DISTRICT, CITY OF MICHIGAN CITY,
LAPORTE COUNTY, INDIANA

We have audited the accompanying financial statements of the business-type activities of the Sanitary District, a department of the City of Michigan City, as of and for the year ended December 31, 2005. These financial statements are the responsibility of the Sanitary District's management. Our responsibility is to express an opinion 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 opinion.

As discussed in Note I, the financial statements of the Sanitary District, City of Michigan City, are intended to present the financial position, and the changes in financial position and cash flows of only that portion of the business-type activities of the City that is attributable to the transactions of the Sanitary District. They do not purport to, and do not, present fairly the financial position of the City of Michigan City as of December 31, 2005, and the changes in its financial position and its cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of the Sanitary District as of December 31, 2005, and the respective changes in financial position and cash flows, where applicable, thereof and for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

The Schedule of Funding Progress, as listed in the table of contents, is not a required part of the basic financial statements but is supplementary 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 supplementary information. However, we did not audit the information and express no opinion on it.

The Sanitary District has not presented Management's Discussion and Analysis that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be part of, the basic financial statements.

STATE BOARD OF ACCOUNTS

July 6, 2006

SANITARY DISTRICT
CITY OF MICHIGAN CITY
STATEMENT OF NET ASSETS
December 31, 2005

Assets

Current assets:	
Cash and cash equivalents	\$ 1,250,929
Accounts receivable (net of allowance)	693,028
Taxes receivable (net of allowance)	185,886
Intergovernmental receivable	149,559
Prepaid items	<u>68,093</u>
Total current assets	<u>2,347,495</u>
Noncurrent assets:	
Restricted:	
Bond and interest cash and cash equivalents	1,449,866
Improvement cash and cash equivalents	802,159
Excess levy cash and cash equivalents	284,393
Loan receivable	964,990
Taxes receivable (net of allowance)	173,674
Intergovernmental receivable	<u>66,459</u>
Total restricted assets	<u>3,741,541</u>
Deferred charges	<u>228,371</u>
Capital assets:	
Land and construction in progress	14,191,888
Other capital assets (net of accumulated depreciation)	<u>69,897,260</u>
Total capital assets	<u>84,089,148</u>
Total noncurrent assets	<u>88,059,060</u>
Total assets	<u>90,406,555</u>

Liabilities

Current liabilities:	
Accounts payable	165,167
Accrued wages payable	133,467
Accrued withholdings payable	1,012
Current liabilities payable from restricted assets:	
Contracts payable	78,427
Loan payable	23,580
General obligation bonds payable	1,910,000
Revenue bonds payable	665,000
Accrued interest payable	<u>106,579</u>
Total current liabilities	<u>3,083,232</u>
Noncurrent liabilities:	
Loan payable	941,410
General obligation bonds payable (net of unamortized discounts)	4,102,384
Revenue bonds payable (net of unamortized premium and deferred amount on refunding)	6,848,894
Compensated absences	<u>48,207</u>
Total noncurrent liabilities	<u>11,940,895</u>
Total liabilities	<u>15,024,127</u>

Net Assets

Invested in capital assets, net of related debt	70,791,241
Restricted for debt service	1,583,420
Restricted for improvements	802,159
Restricted for excess levy	284,393
Unrestricted	<u>1,921,215</u>
Total net assets	<u>\$ 75,382,428</u>

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

SANITARY DISTRICT
CITY OF MICHIGAN CITY
STATEMENT OF REVENUES, EXPENSES AND OTHER CHANGES IN FUND NET ASSETS
As Of And For The Year Ended December 31, 2005

Operating revenues:	
Residential sales	\$ 4,132,281
Commercial and industrial sales	588,037
Governmental	1,367,073
Local tax distributions for stormwater and refuse	2,587,080
Tap fees	33,037
Penalties	96,272
Other	<u>315,318</u>
 Total operating revenues	 <u>9,119,098</u>
Operating expenses:	
Sewer operations and maintenance:	
Salaries	606,444
Employee pension and benefits	317,753
Purchased power	40,362
Materials and supplies	102,219
Contractual services	197,376
Repair and maintenance	49,633
Other	100,660
Plant operations and maintenance:	
Salaries	901,209
Employee pension and benefits	437,356
Purchased power	475,402
Fuel	30,007
Materials and supplies	67,229
Repair and maintenance	31,500
Chemicals	61,132
Contractual services	34,116
Other	27,253
Disposal charge	149,340
Stormwater operations and maintenance:	
Salaries	32,064
Employee pension and benefits	17,114
Contractual services	215,908
Refuse operations and maintenance:	
Salaries	936,353
Employee pension and benefits	631,634
Purchased power	23,994
Fuel	81,675
Materials and supplies	19,692
Contractual services	34,997
Insurance	87,747
Landfill charges	449,188
Repair and maintenance	63,143
Other	9,801
Administrative and general:	
Salaries	312,710
Employee pension and benefits	145,103
Supplies	58,466
Contractual services	153,569
Insurance	204,274
Professional services	43,420
Other	23,897
Bad debt expense	6,517
Depreciation	<u>2,330,486</u>
 Total operating expenses	 <u>9,510,743</u>
 Operating loss	 <u>(391,645)</u>
Nonoperating revenues (expenses):	
Interest revenue	82,843
Local tax distributions for debt service	2,014,993
Intergovernmental revenue	200,212
Amortization of bond issuance cost	(32,940)
Interest expense	<u>(686,052)</u>
 Total nonoperating revenues	 <u>1,579,056</u>
 Income before contributions	 1,187,411
Capital contributions	<u>10,325,174</u>
 Change in net assets	 11,512,585
Restated total net assets - beginning (Note II. F.)	<u>63,869,843</u>
Total net assets - ending	<u>\$ 75,382,428</u>

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

SANITARY DISTRICT
CITY OF MICHIGAN CITY
STATEMENT OF CASH FLOWS
As Of And For The Year Ended December 31, 2005

Cash flows from operating activities:	
Receipts from customers and users	\$ 8,982,460
Payments to suppliers and contractors	(4,384,649)
Payments to employees	<u>(2,867,257)</u>
Net cash provided by operating activities	<u>1,730,554</u>
Cash flows from noncapital financing activities:	
Intergovernmental revenue	<u>200,212</u>
Cash flows from capital and related financing activities:	
Local tax distributions	2,090,323
Proceeds from state revolving loan fund	120,481
Acquisition and construction of capital assets	(1,889,868)
Principal paid on capital debt	(2,410,000)
Interest paid on capital debt	(730,684)
Principal paid on loan	(25,010)
Loan to Indian Springs	<u>(95,471)</u>
Net cash used by capital and related financing activities	<u>(2,940,229)</u>
Cash flows from investing activities:	
Interest received	<u>82,843</u>
Net decrease in cash and cash equivalents	(926,620)
Cash and cash equivalents, January 1 (Including \$1,628,109 and \$1,128,995 for the servicing of debt and improvements, respectively, reported in restricted accounts)	<u>4,713,967</u>
Cash and cash equivalents, December 31 (Including \$1,449,866, \$802,159, and \$284,393 for the servicing of debt, improvements, and excess levy, respectively, reported in restricted accounts)	<u>\$ 3,787,347</u>
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	<u>\$ (391,645)</u>
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation expense	2,330,486
Bad debt expense	6,517
(Increase) decrease in assets:	
Accounts receivable	(181,889)
Taxes receivable	72,172
Intergovernmental receivable	(26,921)
Prepaid items	(68,093)
Increase (decrease) in liabilities:	
Accounts payable	64,014
Accrued wages payable	(1,819)
Accrued withholdings payable	(18,251)
Contracts payable	(10,757)
Compensated absence payable	<u>(43,260)</u>
Total adjustments	<u>2,122,199</u>
Net cash provided by operating activities	<u>\$ 1,730,554</u>
Noncash investing, capital and financing activities:	
Contributions of capital assets from government	\$ 10,325,174
Transfer of completed construction in progress projects	1,202,249
Deletion of obsolete capital assets	368,724

On January 6, 2005, the Sanitary District issued \$8,000,000 in refunding revenue bonds to refund \$7,845,000 of outstanding 1994 revenue bonds. The net proceeds of \$7,868,576 (after payment of \$161,925 in issuance costs) were deposited in an irrevocable trust with an escrow agent. The accounting loss of \$210,613 has been recognized on the Statement of Net Assets as a deferral of loss on refunding, netted against bonds payable, and will be amortized using the straight-line method and charged to interest expense over the next ten years.

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

SANITARY DISTRICT
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS

I. Summary of Significant Accounting Policies

A. Reporting Entity

The financial statements reflect only the activity of the Sanitary District and are not intended to present fairly the position of the City of Michigan City (City), and the results of its operations and cash flows of its enterprise funds. The Sanitary District, whose operations are controlled by the City, represents a substantial portion of the City's enterprise funds.

B. Fund Financial Statements

Business-type activity financial statements consist of the Statement of Net Assets; Statement of Revenues, Expenses, and Other Changes in Fund Net Assets; and the Statement of Cash Flows. Business-type activities rely to a significant extent on fees and charges for support.

C. Measurement Focus, Basis of Accounting and Financial Statement Presentation

The accounts of the business-type activity are maintained and the financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized when incurred.

Proprietary funds distinguish operating revenues 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 of the enterprise funds are charges to customers for sales and services. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

D. Assets, Liabilities and Net Assets or Equity

1. Deposits and Investments

The Sanitary District'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.

State statute (IC 5-13-9) authorizes the Sanitary District to invest in securities, including but not limited to, federal government securities, repurchase agreements, and certain money market mutual funds. Certain other statutory restrictions apply to all investments made by local governmental units.

Investment income, including changes in the fair value of investments, is reported as revenue in the operating statement.

SANITARY DISTRICT
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

2. Prepaid Items

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in the Sanitary District's financial statements.

3. Property Taxes

Property taxes levied are collected by the County Treasurer and are distributed to the Sanitary District in June and in December. State statutes (IC 6-1.1-17-16) require the Indiana Department of Local Government Finance to establish property tax rates and levies by February 15. These rates were based upon the preceding year's March 1 (lien date) assessed valuations adjusted for various tax credits. Taxable property is assessed at 100% of the true tax value (determined in accordance with rules and regulations adopted by the Indiana Department of Local Government Finance). Taxes may be paid in two equal installments that become delinquent if not paid by May 10 and November 10, respectively. Delinquent property taxes outstanding at year end, net of allowances for uncollectible accounts, are recorded as a receivable. The property taxes collected for the stormwater and refuse operations and maintenance function are classified as operating revenue since the maintenance expenses are an operating expense. The property taxes collected for debt repayment are classified as nonoperating.

4. Restricted Assets

Certain resources set aside for repayment of debt and Sanitary District improvements are classified as restricted assets on the statement of net assets balance sheet in accordance with the debt instruments.

5. Capital Assets

Capital assets, which include property, plant, and equipment, are reported in the financial statements.

Capital assets are reported at actual or estimated historical cost based on appraisals or deflated current replacement cost. Contributed or donated assets are reported at estimated fair value at the time received.

Capitalization thresholds (the dollar values above which asset acquisitions are added to the capital asset accounts), depreciation methods and estimated useful lives of capital assets are as follows:

	Capitalization Threshold	Depreciation Method	Percentage or Years
Buildings	\$ 50,000	Composite rate	2%
Improvements other than buildings	20,000	Composite rate	2%
Machinery and equipment			
– Wastewater Utility	5,000	Composite rate	14%
Machinery and equipment – refuse	5,000	Straight-line	4 to 20 years
Transportation equipment	5,000	Composite rate	20%

For depreciated assets, the cost of normal maintenance and repairs that do not add to the value of the asset or materially extend asset lives are not capitalized.

SANITARY DISTRICT
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

6. Compensated Absences

- a. Sick Leave – Sanitary District employees earn sick leave at the rate of 12 days per year. Unused sick leave may be accumulated to a maximum of 36 days. Accumulated sick leave is paid to employees through cash payments only upon retirement.
- b. Vacation Leave – Sanitary District employees earn vacation leave at rates from 10 days to 25 days per year based upon the number of years of service. Vacation leave does not accumulate from year to year.

Sick leave is accrued when incurred in proprietary funds and reported as a liability.

No liability is reported for vacation leave.

7. Long-Term Obligations

Long-term debt and other long-term obligations are reported as liabilities in the statement of net assets. Bond premiums and discounts, deferral of loss on refunding, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable bond premium or discount and deferral of loss on refunding. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

II. Detailed Notes on All Funds

A. Deposits and Investments

1. Deposits

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. Indiana Code 5-13-8-1 allows a political subdivision of the State of Indiana to deposit public funds in a financial institution only if the financial institution is a depository eligible to receive state funds; and has a principal office or branch that qualifies to receive public funds of the political subdivision. The bank balances were insured by the Federal Deposit Insurance Corporation or the Public Deposit Insurance Fund, which covers all public funds held in approved depositories.

2. Investments

Authorization for investment activity is stated in Indiana Code 5-13. As of December 31, 2005, the Sanitary District had no investments.

B. Capital Assets

Capital asset activity for the year ended December 31, 2005, was as follows:

SANITARY DISTRICT
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

	<u>Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Balance</u>
Capital assets, not being depreciated:				
Land	\$ 718,563	\$ 1,668	\$ -	\$ 720,231
Construction in progress	<u>3,173,103</u>	<u>11,500,803</u>	<u>1,202,249</u>	<u>13,471,657</u>
 Total capital assets, not being depreciated	 <u>3,891,666</u>	 <u>11,502,471</u>	 <u>1,202,249</u>	 <u>14,191,888</u>
Capital assets, being depreciated:				
Buildings and improvements	86,429,460	1,522,861	-	87,952,321
Machinery and equipment	3,793,946	353,981	315,273	3,832,654
Transportation equipment	<u>1,504,186</u>	<u>33,186</u>	<u>53,451</u>	<u>1,483,921</u>
 Totals	 <u>91,727,592</u>	 <u>1,910,028</u>	 <u>368,724</u>	 <u>93,268,896</u>
Less accumulated depreciation for:				
Buildings and improvements	16,886,513	1,724,570	-	18,611,083
Machinery and equipment	3,152,153	439,752	315,273	3,276,632
Transportation equipment	<u>1,371,208</u>	<u>166,164</u>	<u>53,451</u>	<u>1,483,921</u>
 Totals	 <u>21,409,874</u>	 <u>2,330,486</u>	 <u>368,724</u>	 <u>23,371,636</u>
 Total capital assets, being depreciated, net	 <u>70,317,718</u>	 <u>(420,458)</u>	 <u>-</u>	 <u>69,897,260</u>
 Total capital assets, net	 <u>\$ 74,209,384</u>	 <u>\$ 11,082,013</u>	 <u>\$ 1,202,249</u>	 <u>\$ 84,089,148</u>

C. Construction Commitments

Construction work in progress is composed of the following:

<u>Project</u>	<u>Total Project Authorized</u>	<u>Expended to December 31, 2005</u>	<u>Committed</u>	<u>Required Future Funding</u>
Streibel Arm - Earl Road	\$ 7,346,232	\$ 6,864,357	\$ 481,875	\$ -
Lafayette/Barker	5,660,000	151,747	8,253	5,500,000
Meer Road	1,485,060	347,328	1,137,732	-
Wabash/Washington	2,187,331	2,084,821	102,510	-
Pretreatment stage improvement/ headworks project	<u>4,675,775</u>	<u>4,023,404</u>	<u>652,371</u>	<u>-</u>
 Totals	 <u>\$ 21,354,398</u>	 <u>\$ 13,471,657</u>	 <u>\$ 2,382,741</u>	 <u>\$ 5,500,000</u>

SANITARY DISTRICT
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

D. Long-Term Liabilities

1. General Obligation Bonds

The Sanitary District issues general obligation bonds to provide funds for the acquisition and construction of major capital facilities.

General obligation bonds are direct obligations and pledge the full faith and credit of the government. General obligation bonds currently outstanding at year end are as follows:

Purpose	Interest Rates	Amount
1995 Improvement bonds	4.95% to 5%	<u>\$ 6,080,000</u>

General obligation bonds debt service requirements to maturity are as follows:

Year Ended December 31	Principal	Interest
2006	\$ 1,910,000	\$ 280,265
2007	2,025,000	183,500
2008	2,145,000	80,875
Totals	\$ 6,080,000	\$ 544,640

2. Revenue Bonds

The Sanitary District issues bonds to be paid by income derived from the acquired or constructed assets. Revenue bonds outstanding at year end are as follows:

Purpose	Interest Rates	Amount
2005 Refunding revenue bonds	3% to 3.85%	<u>\$ 7,685,000</u>

Revenue bonds debt service requirements to maturity are as follows:

SANITARY DISTRICT
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

Year Ended		
<u>December 31</u>	<u>Principal</u>	<u>Interest</u>
2006	\$ 665,000	\$ 250,840
2007	685,000	230,740
2008	705,000	210,040
2009	725,000	188,740
2010	750,000	166,655
2011-2015	<u>4,155,000</u>	<u>432,135</u>
Totals	<u>\$ 7,685,000</u>	<u>\$ 1,479,150</u>

On January 6, 2005, the Sanitary District issued \$8,000,000 in refunding revenue bonds with an average interest rate of 3.62% to advance refund \$7,845,000 of outstanding 1994 revenue bonds with an average interest rate of 5.39%. The net proceeds of \$7,868,576 (after payment of \$161,925 in issuance costs) were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the 1994 revenue bonds. As a result, these bonds are considered to be defeased and the liability for those bonds has been removed from the Statement of Net Assets. The refunding resulted in the accounting loss of \$210,613, which has been recognized on the Statement of Net Asset as a net of the unamortized deferred amount on refunding from revenue bonds payable and will be amortized using the straight-line method and charged to interest expense over the next ten years. The Sanitary District in effect reduced its aggregate debt service payment by \$763,342 over the next ten years and realized an economic gain (difference between the present values of the old and new debt service payments) of \$646,201.

3. Loan Payable

The Sanitary District has entered into a State Revolving Loan for the extension of sanitary sewer service to the Indian Springs Area. The loan is payable solely from special capital charges collected from Indian Springs residents, which is reported as a loan receivable on the statement of net assets. The \$990,000 loan will not bear interest and is to be repaid quarterly beginning April 1, 2005, and ending January 1, 2047. The term of the loan may be extended beyond 42 years if there are deficiencies in the special capital charges collected as a result of delinquent user charge fees that are not recovered in the due course of business. As of December 31, 2005, the full \$990,000 has been drawdown and \$25,010 has been collected and remitted to the State leaving a balance of \$964,990. Annual debt service requirements to maturity are based upon the monthly collections received from the Indian Springs area residents.

4. Advance Refunding

In prior years, the Sanitary District defeased certain revenue bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments of the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Sanitary District's financial statements. At December 31, 2005, \$290,000 of the 1994 revenue bonds outstanding were considered defeased.

SANITARY DISTRICT
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

5. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2005, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
General obligation bonds	\$ 7,890,000	\$ -	\$ 1,810,000	\$ 6,080,000	\$ 1,910,000
Less discount	(90,154)	-	(22,538)	(67,616)	-
Revenue bonds	8,130,000	8,000,000	8,445,000	7,685,000	665,000
Add premium	-	30,501	1,526	28,975	-
Less discount	(81,411)	-	(81,411)	-	-
Less deferred amount on refunding	-	(210,613)	(10,532)	(200,081)	-
Total bonds payable	15,848,435	7,819,888	10,142,045	13,526,278	2,575,000
Loan payable	869,519	120,481	25,010	964,990	23,580
Compensated absences	91,467	-	43,260	48,207	-
Total long-term liabilities	<u>\$ 16,809,421</u>	<u>\$ 7,940,369</u>	<u>\$ 10,210,315</u>	<u>\$ 14,539,475</u>	<u>\$ 2,598,580</u>

E. Restricted Assets

The balances of restricted asset accounts for debt repayment and improvements are as follows:

Bond and interest cash and cash equivalents	\$ 1,449,866
Improvement cash and cash equivalents	802,159
Excess Levy cash and cash equivalents	284,393
Loan receivable	964,990
Taxes receivable	173,674
Intergovernmental receivable	<u>66,459</u>
Total restricted assets	<u>\$ 3,741,541</u>

F. Restatements

For the year ended December 31, 2005, certain changes have been made to the financial statements to more appropriately reflect financial activity of the Sanitary District. Prior period adjustments represent continued adjustments to capital assets due to updated information.

SANITARY DISTRICT
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

Net Assets as Reported December 31, 2004	Prior Period Adjustments	Net Assets as Restated January 1, 2005
\$ 63,818,852	\$ 50,991	\$ 63,869,843

III. Other Information

A. Risk Management

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; job related illnesses or injuries to employees; medical benefits to employees, retirees, and dependents (excluding postemployment benefits); and natural disasters.

The risks of torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters are covered by commercial insurance from independent third parties. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years. There were no significant reductions in insurance by major category of risk.

Medical Benefits to Employees, Retirees, and Dependents

The City, including the Sanitary District, has chosen to establish a risk financing fund for risks associated with medical benefits to employees, retirees, and dependents. The risk financing fund is accounted for in the City's Employee Health and Life Insurance Fund, an internal service fund, where assets are set aside for claim settlements. An excess policy through commercial insurance covers individual claims in excess of \$100,000 per year. Settled claims resulting from this risk did not exceed commercial insurance coverage in the past three years. A premium is charged to each fund that accounts for employee payroll. The total charge allocated to each of the funds is calculated using trends in actual claims experience. Provisions are also made for unexpected and unusual claims.

Claim expenditures and liabilities of the fund are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported (IBNRs).

Information to segregate the assets and liabilities figures between the City, Utilities, and the Port Authority is not available and therefore considered an obligation of the City. Thus, claim liabilities cannot be reasonably estimated for the Sanitary District separate from the City.

Job Related Illnesses or Injuries to Employees

During 1992, the Sanitary District joined together with other governmental entities in the Indiana Public Employer's Plan, Inc. (IPEP), a public entity risk pool currently operating as a common risk management and insurance program for approximately 350 member governmental entities. This risk pool

SANITARY DISTRICT
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

was formed in 1990. The purpose of the risk pool is to provide a medium for the funding and administration of job related illnesses or injuries to employees. The Sanitary District pays an annual premium to the risk pool for its job related illnesses or injuries to employees coverage. The risk pool is considered a self-sustaining risk pool that will provide coverage for its members for up to \$1,000,000 per insured event.

B. Subsequent Events

On October 15, 2005, the Sanitary District approved an agreement with the Indiana Finance Authority for a \$90,000 loan, with an annual interest rate of 2.4%, to construct a sewer extension to an area near Trail Creek. The loan is drawn down on an as-needed basis upon presentation of accurate and complete claims to the Indiana Finance Authority. Drawdowns totaling \$78,427 were requested and received in February 2006. The loan is payable solely from special capital charges collected from users served by the sewer extension. The loan will mature quarterly over a period ending April 1, 2038.

On December 21, 2005, the Sanitary District Board of Commissioners approved to provide retiree health insurance to non-contract employees who have at least 20 years of service, are not yet age 65, are at a minimum of 55 years of age, or are eligible for PERF disability effective January 1, 2006. The retired employee shall contribute one-third (1/3) of the total health insurance premium cost and the City shall contribute two-thirds (2/3).

C. Rate Structure

The current rate structure was approved by the Board of Sanitary District Commissioners and the Michigan City Common Council on December 21, 2004. The Sanitary District has 11,376 customers.

D. Pension Plan

Public Employees' Retirement Fund

Plan Description

The City, including the Sanitary District, contributes to the Indiana Public Employees' Retirement Fund (PERF), a defined benefit pension plan. PERF is an agent multiple-employer public employee retirement system, which provides retirement benefits to plan members and beneficiaries. All full-time employees are eligible to participate in the defined benefit plan. State statutes (IC 5-10.2 and 5-10.3) govern, through the PERF Board, most requirements of the system and give the City, including the Sanitary District, authority to contribute to the plan. The PERF retirement benefit consists of the pension provided by employer contributions plus an annuity provided by the member's annuity savings account. The annuity savings account consists of member's contributions, set by state statute at 3% of compensation, plus the interest credited to the member's account. The employer may elect to make the contributions on behalf of the member.

PERF administers the plan and issues a publicly available financial report that includes financial statements and required supplementary information for the plan as a whole and for its participants. The report may be obtained by contacting:

SANITARY DISTRICT
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

Public Employees' Retirement Fund
Harrison Building, Room 800
143 West Market Street
Indianapolis, IN 46204
Ph. (317) 233-4162

Funding Policy and Annual Pension Cost

The contribution requirements of plan members for PERF are established by the Board of Trustees of PERF. The City's (including the Sanitary District's) annual pension cost and related information, as provided by the actuary, is presented in this note. Information to segregate the assets/liabilities and the actuarial study figures between the City and the Sanitary District is not available. Therefore, the liability for Net Pension Obligation (NPO) is considered an obligation of the City as a whole.

Actuarial Information for the Above Plan

	PERF
Annual required contribution	\$ 559,453
Interest on net pension obligation	(12,969)
Adjustment to annual required contribution	14,779
Annual pension cost	561,263
Contributions made	542,191
Increase in net pension obligation	19,072
Net pension obligation, beginning of year	(178,881)
Net pension obligation, end of year	\$ (159,809)
Contribution rates:	
Sanitary District	6.5%
Plan members	3%
Actuarial valuation date	07-01-05
Actuarial cost method	Entry age
Amortization method	Level percentage of projected payroll, closed
Amortization period	40 years
Amortization period (from date)	07-01-97
Asset valuation method	4 year smoothed market

SANITARY DISTRICT
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

Actuarial Assumptions	PERF
Investment rate of return	7.25%
Projected future salary increases:	
Total	5%
Attributed to inflation	4%
Attributed to merit/seniority	1%
Cost-of-living adjustments	2%

Three Year Trend Information

	Year Ending	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation
PERF	06-30-03	\$ 520,680	84%	\$ (145,792)
	06-30-04	467,021	107%	(178,881)
	06-30-05	561,263	116%	(159,809)

SANITARY DISTRICT
CITY OF MICHIGAN CITY
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF FUNDING PROGRESS

Public Employees' Retirement Fund

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (a-b)	Funded Ratio (a/b)	Covered Payroll (c)	Unfunded AAL as a Percentage of Covered Payroll ((a-b)/c)
07-01-03	\$ 6,864,219	\$ 8,392,364	\$ (1,528,145)	82%	\$ 7,622,749	(20%)
07-01-04	7,084,173	9,396,394	(2,312,221)	75%	8,118,274	(28%)
07-01-05	7,513,688	10,997,902	(3,484,214)	68%	8,063,595	(43%)

SANITARY DISTRICT
CITY OF MICHIGAN CITY
AUDIT RESULTS AND COMMENTS

CAPITAL ASSET RECORDS

The construction in progress accounts did not accurately reflect the balance of the projects at December 31, 2005. Upon review of contract payments made to contractors, it was determined that at least \$6,406,123 of payments made from City funds for the Sanitary District projects were not posted to the Sanitary District's general ledger as contributed capital. Upon further review by officials, it was determined that an adjustment to construction work in progress as of December 31, 2005, totaling \$7,582,925 was needed which was posted to the general ledger and incorporated into the annual report.

Additionally, the Indian Springs project was completed as of December 31, 2005; however, the project was not transferred from construction work in progress to capital assets. The officials determined an adjustment of \$1,202,249 to transfer the completed project was needed which was posted to the general ledger and incorporated into the annual report.

Furthermore, the detail capital asset records agreed in total to the control accounts on the trial balance; however, it was determined that the individual asset classification balances did not agree. It was noted that deletions or disposals of capital assets are recorded in total; however, they are not always taken out of the individual asset classification totals.

Every governmental unit should have a complete inventory of all capital assets owned which reflect their acquisition value. Such inventory should be recorded in the Capital Assets Ledger form. A complete inventory should be taken at least every two years for good internal control and for verifying account balances carried in the accounting records. (Accounting and Uniform Compliance Guidelines Manual for Special Districts, Chapter 10)

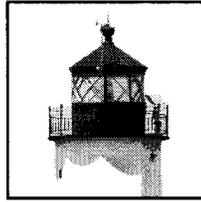
OVERDRAWN CASH BALANCE

The cash balance of the Sanitary District Refuse Operating Fund was overdrawn \$266,306.75 as of December 31, 2005.

The cash balance of any fund may not be reduced below zero. Routinely overdrawn funds could be an indicator of serious financial problems which should be investigated by the governmental unit. (Accounting and Uniform Compliance Guidelines Manual for Special Districts, Chapter 10)

SANITARY DISTRICT
CITY OF MICHIGAN CITY
EXIT CONFERENCE

The contents of this report were discussed on July 27, 2006, with Alan J. Walus, General Manager; Jeffrey Jones, Vice-President of the Board of Sanitary District Commissioners; Charles E. Oberlie, Mayor; John J. Schaefer, City Controller; Judith Paul, Sanitary District Commissioner; Doretha M. Sanders, Office Manager; and Cheryl Bates, Bookkeeper. The official response has been made a part of this report and may be found on pages 21 and 22.



M I C H I G A N C I T Y

the place is here, the time is now!

Office of City Controller – John J. Schaefer, CPA – Phone: 219.873.1404 – Fax: 219.873.1542 – e-mail: jschaefer@emichigancity.com

August 1, 2006

Mr. Bruce Hartman
State Examiner
Indiana State Board of Accounts
302 W. Washington Street
Indianapolis, IN 46204

Dear Mr. Hartman:

Your examiners have completed the audit of the Michigan City Sanitary District for the year 2005. The audit report contains two comments to which we wish to respond.

Capital Asset Records. The audit comment correctly states that some District assets were not included in the general ledger. Specifically, construction-in-progress was understated by approximately \$7.5 million and a completed project was not transferred from construction-in-progress to fixed assets.

The omission was related to those construction projects funded by the City through gaming revenues; expenditures for these projects were not paid by the District.

The District and the City have agreed to have all fixed asset accounting done by the Controller's office. The Controller's office has a staff person assigned to track City fixed assets and her duties will now also include District fixed assets.

Overdrawn Cash Balance. The audit comment correctly states that the Refuse Operating Fund was overdrawn at December 31, 2005.

The situation was caused by errors in planning the 2005 budget.

We discovered the errors when preparing the 2006 budget and we immediately implemented measures to correct them. Unfortunately, we were not able to completely erase the deficit by the

-21-
CHUCK OBERLIE – MAYOR

end of 2005. We project that, by the end of 2006, the Refuse Operating Fund will have a cash balance in excess of \$400,000.

We are pleased to note that this audit confirms that substantial improvement has been made in the District's accounting system since 2003 when new financial software was implemented. After two years of working with the vendor and an outside consultant, we have resolved our software issues and the problems noted in our audit reports from 2003 and 2004 no longer exist.

As usual, your auditors were a pleasure to work with and I appreciate their assistance and advice.

Sincerely,

A handwritten signature in black ink, appearing to read "John J. Schaefer". The signature is written in a cursive style with a large initial "J".

John J. Schaefer
City Controller