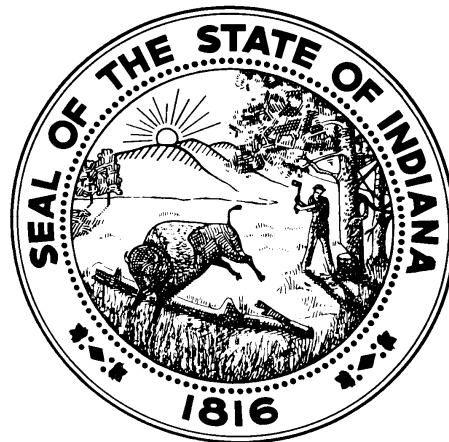


STATE BOARD OF ACCOUNTS
302 West Washington Street
Room E418
INDIANAPOLIS, INDIANA 46204-2769

EXAMINATION REPORT
OF
WATER UTILITY
CITY OF MICHIGAN CITY
LAPORTE COUNTY, INDIANA

January 1, 2008 to December 31, 2008



FILED
02/12/2010

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OFFICIALS

<u>Office</u>	<u>Official</u>	<u>Term</u>
Controller	John J. Schaefer	01-01-08 to 12-31-09
Mayor	Charles E. Oberlie	01-01-08 to 12-31-11
President of the Utility Board Of Directors	Larry J. Jordan III	01-01-08 to 12-31-09
Office Manager	Ronald Plamowski	01-01-08 to 12-31-09
Superintendent of Water Utility	Randall E. Russell	01-01-08 to 12-31-09



STATE OF INDIANA
AN EQUAL OPPORTUNITY EMPLOYER

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INDEPENDENT ACCOUNTANT'S REPORT

TO: THE OFFICIALS OF THE WATER UTILITY, CITY
OF MICHIGAN CITY, LAPORTE COUNTY, INDIANA

We have examined the accompanying financial statements of the business-type activities of the Water Utility (Utility), a department of the City of Michigan City, as of and for the year ended December 31, 2008. The Utility's management is responsible for the financial statements presented herein. Our responsibility is to express an opinion based on our examination.

Our examination was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants and, accordingly, included examining, on a test basis, evidence supporting the financial statement presented herein and performing such other procedures as we considered necessary in the circumstances. We believe that our examination provides a reasonable basis for our opinion.

As discussed in Note I, the financial statements of the Water Utility, 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 Utility. They do not purport to, and do not, present fairly the financial position of the City of Michigan City as of December 31, 2008, 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 for the Water Utility, as of December 31, 2008, and the respective changes in financial position and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

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 examine the information and express no opinion on it.

The Water Utility has not presented Management's Discussion and Analysis that accounting principles generally accepted in the United States of America has determined is necessary to supplement, although not required to be part of, the basic financial statements.

STATE BOARD OF ACCOUNTS

December 22, 2009

WATER UTILITY
CITY OF MICHIGAN CITY
STATEMENT OF NET ASSETS
December 31, 2008

Assets

Current assets:	
Cash and cash equivalents	\$ 1,523,880
Accounts receivable (net of allowance)	477,502
Inventories	<u>300,458</u>
 Total current assets	 <u>2,301,840</u>
Noncurrent assets:	
Restricted cash, cash equivalents and investments:	
Improvement cash and investments	3,943,049
Bond and interest cash and investments	404,890
Retainage cash and investments	26,095
Customer deposits cash and investments	505,813
Pension asset	<u>142,977</u>
 Total restricted assets:	 <u>5,022,824</u>
 Deferred charges	 <u>229,191</u>
Capital assets:	
Land, improvements to land and construction in progress	886,691
Other capital assets (net of accumulated depreciation)	<u>43,529,034</u>
 Total capital assets	 <u>44,415,725</u>
 Total noncurrent assets	 <u>49,667,740</u>
 Total assets	 <u>51,969,580</u>

Liabilities

Current liabilities:	
Accounts payable	100,134
Accrued wages payable	63,049
Contracts and retainage payable	196,059
Taxes payable	20,797
Unearned revenue	135,255
Current liabilities payable from restricted assets:	
Customer deposits	501,379
Revenue bonds payable	735,000
Loan payable	50,000
Accrued interest payable	<u>143,735</u>
 Total current liabilities	 <u>1,945,408</u>
Noncurrent liabilities:	
Revenue bonds payable (net of unamortized discounts and deferred amount on refunding)	6,135,428
Loan payable	6,084,916
Advances for construction	<u>76,641</u>
 Total noncurrent liabilities	 <u>12,296,985</u>
 Total liabilities	 <u>14,242,393</u>

Net Assets

Invested in capital assets, net of related debt	31,170,809
Restricted for debt service	548,626
Restricted for capital outlay	3,838,003
Restricted for other purposes	648,790
Unrestricted	<u>1,520,959</u>
 Total net assets	 <u>\$ 37,727,187</u>

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

WATER UTILITY
CITY OF MICHIGAN CITY
STATEMENT OF REVENUES, EXPENSES, AND OTHER CHANGES IN FUND NET ASSETS
As Of And For The Year Ended December 31, 2008

Operating revenues:	
Metered water revenue:	
Residential and commercial	\$ 3,502,240
Industrial and governmental	1,202,605
Fire protection revenue	1,133,894
Penalties	33,490
Sales for resale	471,117
Other water revenue	<u>230,464</u>
 Total operating revenues	 <u>6,573,810</u>
Operating expenses:	
Source of supply and expense - operations and maintenance	556,752
Water treatment expense - operations and maintenance	694,289
Transmission and distribution	992,148
Customer accounts	332,505
Administration and general	894,333
In lieu of tax	441,844
Depreciation	1,122,001
Taxes	<u>196,443</u>
 Total operating expenses	 <u>5,230,315</u>
 Operating income	 <u>1,343,495</u>
Nonoperating revenues (expenses):	
Interest and investment revenue	128,115
Interest expense	(470,120)
Amortization expense	<u>(24,032)</u>
 Total nonoperating revenues (expenses)	 <u>(366,037)</u>
 Income before contributions	 977,458
 Capital contributions	 <u>1,209,141</u>
 Change in net assets	 2,186,599
Total net assets - beginning	<u>35,540,588</u>
Total net assets - ending	<u>\$ 37,727,187</u>

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

WATER UTILITY
CITY OF MICHIGAN CITY
STATEMENT OF CASH FLOWS
As Of And For The Year Ended December 31, 2008

Cash flows from operating activities:	
Receipts from customers and users	\$ 6,673,706
Payments to suppliers and contractors	(1,847,629)
Payments to employees	(1,800,095)
Interfund services provided	90,903
Interfund services used	<u>(468,380)</u>
Net cash provided by operating activities	<u>2,648,505</u>
Cash flows from noncapital financing activities:	
Payments received on loan	<u>31,211</u>
Cash flows from capital and related financing activities:	
Capital contributions	1,209,141
Acquisition and construction of capital assets	(1,568,189)
Principal paid on revenue bonds	(715,000)
Principal paid on state revolving loan	(50,000)
Interest paid on revenue bonds	(269,419)
Interest paid on state revolving loan	(179,000)
Refunds of customer advances for construction	<u>(54,786)</u>
Net cash used by capital and related financing activities	<u>(1,627,253)</u>
Cash flows from investing activities:	
Interest received	<u>129,950</u>
Net increase in cash and cash equivalents	1,182,413
Cash and cash equivalents, January 1	<u>5,221,314</u>
Cash and cash equivalents, December 31	<u>\$ 6,403,727</u>
Reconciliation of operating income to net cash provided by operating activities:	
Operating income	<u>\$ 1,343,495</u>
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation expense	1,122,001
Bad debt expense	9,600
(Increase) decrease in assets:	
Accounts receivable	73,303
Inventories	(8,377)
Increase (decrease) in liabilities:	
Accounts payable	(17,883)
Accrued wages payable	16,945
Taxes payable	1,525
Unearned revenue	109,720
Customer deposits	<u>(1,824)</u>
Total adjustments	<u>1,305,010</u>
Net cash provided by operating activities	<u>\$ 2,648,505</u>
Noncash investing, capital and financing activities:	
Purchase of equipment on account	\$ 214,466
Disposal of fixed assets	517,377
Decrease in pension asset	1,835

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

WATER UTILITY
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 Utility 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 Utility, whose operations are controlled by the Utility Board of Directors, per Indiana Code 8-1.5-4-1.5(b), 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 Utility'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 Utility 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.

2. Inventories and Prepaid Items

All inventories are valued at cost using the first in/first out (FIFO) method.

WATER UTILITY
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

3. 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 Statement of Net Assets balance sheet because they are maintained in separate bank accounts and their use is limited by applicable bond covenants.

4. 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:

	<u>Capitalization Threshold</u>	<u>Depreciation Method</u>	<u>Estimated Useful Life</u>
Improvements other than buildings	\$ 500	Composite rate	2%
Buildings	500	Composite rate	2%
Machinery and equipment	500	Composite rate	2%

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.

5. Compensated Absences

- a. Sick Leave – Utility employees earn sick leave at the rate of 1.5 days per month. Unused sick leave may be accumulated to a maximum of 180 days. Accumulated sick leave is not paid to employees upon termination.
- b. Vacation Leave – Utility employees earn vacation leave at rates from 5 days to 20 days per year based upon the number of years of service. Vacation leave does not accumulate from year to year.
- c. Personal Leave – Utility employees earn personal leave at the rate of 2 days per year. Personal leave does not accumulate from year to year.

No liability is reported for vacation, sick and personal leave.

WATER UTILITY
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

6. Long-Term Obligations

Long-term debt and other long-term obligations are reported as liabilities in the Statement of Net Assets. Bond issuance costs, and deferred loss on refunding, are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable deferred 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

Deposits, made in accordance with Indiana Code 5-13, with financial institutions in the State of Indiana at year end were entirely insured by the Federal Depository Insurance Corporation or by the Indiana Public Deposit Insurance Fund. This includes any deposit accounts issued or offered by a qualifying financial institution.

B. Capital Assets

Capital asset activity for the year ended December 31, 2008, was as follows:

	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, not being depreciated:				
Land	\$ 91,291	\$ -	\$ -	\$ 91,291
Construction in progress	78,018	1,316,650	599,268	795,400
 Total capital assets, not being depreciated	 169,309	 1,316,650	 599,268	 886,691
Capital assets, being depreciated:				
Improvements other than buildings	30,181,594	567,118	-	30,748,712
Buildings	20,298,456	173,423	250,000	20,221,879
Machinery and equipment	5,644,515	324,732	267,377	5,701,870
 Totals	 56,124,565	 1,065,273	 517,377	 56,672,461
Less accumulated depreciation for:				
Improvements other than buildings	7,229,817	603,632		7,833,449
Buildings	4,323,849	405,969	250,000	4,479,818
Machinery and equipment	985,137	112,400	267,377	830,160
 Totals	 12,538,803	 1,122,001	 517,377	 13,143,427
 Total capital assets, being depreciated, net	 43,585,762	 (56,728)	 -	 43,529,034
 Total capital assets, net	 \$ 43,755,071	 \$ 1,259,922	 \$ 599,268	 \$ 44,415,725

WATER UTILITY
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

C. Construction Commitments

Construction work in progress is composed of the following:

Project	Total Project Authorized	Expended to December 31, 2008	Committed	Required Future Funding
Pine School Water Main	\$ 631,105	\$ 164,502	\$ 466,603	\$ -
Highway 20 Main Extension	124,679	21,599	103,080	-
Water Intake Shorewell	<u>1,308,244</u>	<u>609,299</u>	<u>698,945</u>	-
Totals	<u>\$ 2,064,028</u>	<u>\$ 795,400</u>	<u>\$ 1,268,628</u>	<u>\$ -</u>

D. Lease

Operating Lease

The Utility has entered into an operating lease having initial or remaining noncancelable term exceeding one year for a folder inserter machine. Rental expenditures for this lease were \$3,767. The following is a schedule by years of future minimum rental payments as of December 31, 2008:

2009	<u>\$ 2,197</u>
------	-----------------

E. Long-Term Liabilities

1. Revenue Bonds

The Utility 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
2004 Waterworks refunding revenue bond	3% to 3.75%	<u>\$ 7,110,000</u>

WATER UTILITY
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

Revenue bonds debt service requirements to maturity are as follows:

Year Ended December 31	Principal	Interest
2009	\$ 735,000	\$ 247,363
2010	775,000	222,669
2011	800,000	195,369
2012	830,000	167,106
2013	870,000	137,706
2014-2017	<u>3,100,000</u>	<u>223,325</u>
Totals	<u>\$ 7,110,000</u>	<u>\$ 1,193,538</u>

2. Loan Payable

The Utility has entered into a State Revolving Fund Loan. Annual debt service requirements to maturity for the loan are as follows:

Year Ended December 31	Principal	Interest
2009	\$ 50,000	\$ 177,550
2010	40,000	176,173
2011	40,000	175,013
2012	40,000	173,853
2013	30,000	172,765
2014-2018	1,920,000	819,455
2019-2022	<u>4,014,916</u>	<u>236,341</u>
Totals	<u>\$ 6,134,916</u>	<u>\$ 1,931,150</u>

3. Advance Refunding

In 2004, the Utility defeased revenue bonds of 1995, 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 Utility's financial statements. At December 31, 2008, \$7,055,000 of the 1995 revenue bonds were considered defeased.

WATER UTILITY
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

4. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2008, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Revenue bonds payable	\$ 7,825,000	\$ -	\$ 715,000	\$ 7,110,000	\$ 735,000
Less deferred amount on refunding	<u>268,907</u>	<u>-</u>	<u>29,335</u>	<u>239,572</u>	<u>-</u>
Total revenue bonds payable	7,556,093	-	685,665	6,870,428	735,000
Loan payable	6,184,916	-	50,000	6,134,916	50,000
Advances for construction	<u>131,427</u>	<u>-</u>	<u>54,786</u>	<u>76,641</u>	<u>-</u>
Total long-term liabilities	<u>\$ 13,872,436</u>	<u>\$ -</u>	<u>\$ 790,451</u>	<u>\$ 13,081,985</u>	<u>\$ 785,000</u>

III. Other Information

A. Risk Management

The Utility 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; job related illnesses or injuries to employees; 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 and Dependents

The Utility has chosen to participate in a risk financing fund of the City of Michigan City for risks associated with medical benefits to employees and dependents. The risk financing fund is accounted for in the City's Health and Health Insurance Funds, internal service funds, where assets are set aside for claim settlements. An excess policy through commercial insurance covers individual claims in excess of \$150,000 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 payroll expenditures. 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).

WATER UTILITY
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

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 Utility, separate from the City.

B. Rate Structure

The current rate structure was approved by the Indiana Utility Regulatory Commission on March 31, 2004. The Utility has 12,489 customers.

C. Pension Plan

Plan Description

The Utility has a defined contribution pension plan administered by McKready and Keene, Inc., as authorized by Indiana Code 8-1.5-3-7. The plan provides retirement, disability, and death benefits to plan members and beneficiaries. The plan was established by written agreement between the governing board of the Utility and the Plan Administrator. The Plan Administrator issues a publicly available financial report that includes financial statements and required supplementary information of the plan. That report may be obtained by contacting:

McKready and Keene, Inc.
7941 Castleway Drive
P.O. Box 50460
Indianapolis, IN 46250-0460
Ph. 317-849-4333

Funding Policy and Annual Pension Cost

The contribution requirements of plan members are established by the written agreement between the governing board of the Utility and the Plan Administrator. Plan members are required to contribute 3% of the annual covered salary. The Utility is required to contribute at an actuarially determined rate. The current rate is 0% of annual covered payroll. Employer and employee contributions to the plan were \$0 and \$50,609, respectively.

Actuarial Information for the Above Plan

Decrease in net pension obligation	\$ 1,835
Net pension obligation, beginning of year	<u>(144,812)</u>
Net pension obligation, end of year	<u><u>\$ (142,977)</u></u>

WATER UTILITY
CITY OF MICHIGAN CITY
NOTES TO FINANCIAL STATEMENTS
(Continued)

Contribution rates:

Utility	0%
Plan members	3%
Actuarial valuation date	01-01-09
Actuarial cost method	Entry age
Amortization method	Ten year level funding
Amortization period	30 years
Asset valuation method	Market value

Actuarial Assumptions

Investment rate of return	6%
Projected future salary increases:	4%

Three Year Trend Information

<u>Year Ending</u>	<u>Annual Pension Cost (APC)</u>	<u>Percentage of APC Contributed</u>	<u>Net Pension Obligation</u>
12-31-06	\$ 1,934	0%	\$ (156,540)
12-31-07	2,002	0%	(144,812)
12-31-08	1,835	0%	(142,977)

WATER UTILITY
CITY OF MICHIGAN CITY
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF FUNDING PROGRESS

Water Utility Pension Plan

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Excess of Assets Over AAL (a-b)	Funded Ratio (a/b)	Covered Payroll (c)	Excess AAL as a Percentage of Covered Payroll ((a-b)/c)
01-01-06	\$ 7,897,062	\$ 3,353,155	\$ 4,543,907	236%	\$ 1,489,584	305%
01-01-07	8,341,097	3,640,098	4,700,999	229%	1,651,726	285%
01-01-08	8,923,668	5,910,351	3,013,317	151%	1,664,817	181%
01-01-09	7,534,128	6,174,000	1,360,128	122%	1,687,915	81%

WATER UTILITY
CITY OF MICHIGAN CITY
EXIT CONFERENCE

The contents of this report were discussed on December 22, 2009, with John J. Schaefer, Controller. Randall E. Russell, Superintendent of Water Utility was informed of the contents of this report on December 23, 2009. Our examination disclosed no material items that warrant comment at this time.