

MANAGEMENT LETTER
VILLAGE OF SISTER BAY, WISCONSIN
DECEMBER 31, 2004



To the Village Board
Village of Sister Bay, Wisconsin

We have completed our audit of the basic financial statements of the Village of Sister Bay for the year ended December 31, 2004. The Village's basic financial statements, including our report thereon, are presented in a separate audit report document. Included in the Village's audit report is the following additional auditors' report required by government auditing standards:

Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards

The above report states that our consideration of the internal control structure did not disclose any conditions that we believe to be material weaknesses and that nothing came to our attention to indicate that the Village was not in compliance with laws, regulations, contracts and grant agreements for which noncompliance with could have a material effect on the Village's basic financial statements.

Our responsibility under auditing standards, as prescribed by auditing standards generally accepted in the United States of America promulgated by the American Institute of Certified Public Accountants (AICPA) and *Government Auditing Standards* issued by the Comptroller General of the United States, is to plan and perform our audit to obtain reasonable assurance about whether the basic financial statements are free of material misstatement. An audit in accordance with auditing standards generally accepted in the United States of America and *Government Auditing Standards* does not provide absolute assurance or guarantee the accuracy of the financial statements and is subject to the inherent risk that errors, irregularities (or illegal acts), or noncompliance with the provisions of laws, regulations, contracts and grant agreements, if existing, have not been detected. Such standards require that we obtain a sufficient understanding of the Village's internal control structure to plan the audit. However, such understanding and any tests performed with respect to such internal controls, or as to compliance with laws, regulations, contracts and grant agreements, were for the purpose of expressing our opinion on the Village's basic financial statements and not to form an opinion or provide any assurance concerning such internal control structure or compliance. We could, however, as a separate engagement, be engaged to perform agreed-upon procedures or examine and report on management's assertion about the internal control structure or that management complied with specified laws and regulations. Such engagements would be conducted in accordance with AICPA standards for attestation engagements.

Presented on the following page is a table of contents for enclosed information and comments about financial and administrative matters that came to our attention during our audit of the Village's basic financial statements. The basic purpose of the enclosed is to provide recommendations for improving the internal control structure and to provide financial information to assist management in the decision making process.

Schenck SC

Certified Public Accountants
Green Bay, Wisconsin
March 3, 2005

VILLAGE OF SISTER BAY, WISCONSIN

December 31, 2004

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SUMMARY FINANCIAL INFORMATION

1. Governmental Fund Balances

Presented below is a summary of the Village's governmental fund balances on December 31, 2004, including a comparison to the prior year. This information is provided for assessing financial results for 2004 and for indicating financial resources available for 2005 and subsequent years.

	12/31/04	12/31/03
Governmental Funds		
General Fund		
Designated for subsequent years' expenditures		
Waterfront property	\$ -	\$ 40,000
Fire truck	-	50,000
Downtown engineering	-	89,901
Undesignated	243,285	364,813
Total General Fund	243,285	544,714
Special Revenue Fund		
Designated for subsequent year's expenditures		
Ice rink operations	9,301	25,284
Marina operations	171,157	189,332
Total Special Revenue Fund	180,458	214,616
Capital Projects Fund		
Designated for subsequent year's expenditures		
Fire station and sports complex	322,580	705,083
Storm sewer/watermain project	266,993	-
Mill road	109,915	-
Street resurfacing projects	20,000	-
Fire truck	60,000	-
Acquisition of waterfront property	60,000	-
Old fire station demolition	10,000	-
Moving of baseball field	20,000	-
Park maintenance building	110,000	-
Park sprinkler system	2,500	-
Park mower	8,000	-
Total Capital Projects Fund	989,988	705,083
Total Governmental Fund Balances	\$1,413,731	\$1,464,413

The Village's current undesignated fund balance of \$243,285 represents approximately 28% of the 2004 general fund operating (non-debt service) expenditures for 2003. A general consensus of what represents an adequate undesignated fund balance is to have an undesignated fund balance of between 10 to 25% of the general fund's budgeted operating (non-debt service) expenditures.

Additional information on the marina special revenue fund and the capital projects fund is presented in comments No. 2 and 3, respectively.

2. Marina Operations

A comparative analysis of the Marina operations for the years ended December 31, 2004 and 2003 follows:

	2004	2003
Revenues		
Public charges for services	\$260,073	\$260,640
Interest on investments	3,402	4,157
Total Revenues	<u>263,475</u>	<u>264,797</u>
Expenditures		
Operation and maintenance	134,811	143,911
Capital outlay	46,934	68,359
Debt service		
Principal of note	79,500	71,000
Interest on note	20,405	28,776
Total Expenditures	<u>281,650</u>	<u>312,046</u>
Excess of Revenues Over (Under) Expenditures	(18,175)	(47,249)
Other Financing Sources (Uses)		
Operating transfer out to capital project fund	<u>-</u>	<u>(50,000)</u>
Excess of Revenues and Other Financing Sources Over (Under) Expenditures and Other Uses	(18,175)	(97,249)
Fund Balance - January 1	<u>189,332</u>	<u>286,581</u>
Fund Balance - December 31	<u>\$171,157</u>	<u>\$189,332</u>

A total of \$503,500 of general obligation debt incurred for the marina project remained outstanding on December 31, 2004.

3. Capital Projects Fund

In the 2004 financial statements a capital projects fund was created to account for debt proceeds issued for various capital projects of the Village. A summary of the revenues, expenditures and changes in fund balance of the capital projects fund for 2004 and 2003 is presented below:

	2004	2003
Revenues		
Reimbursement from Door County	\$ 292,855	\$ 222,938
Reimbursement from NWTC	-	25,520
State aid - bike path	181,760	-
Total Revenues	474,615	248,458
Expenditures		
Purchase of land for sports complex	-	360,494
Purchase of waterfront property	-	800,000
Fire station/ambulance building	1,546,529	1,182,787
Sports complex development	483,809	-
Bayshore storm sewer and watermain	208,007	-
Bike path	210,177	-
Promissory note payment	50,000	-
Mill Road	34,045	-
Other	15,098	-
Total Expenditures	2,547,665	2,343,281
Excess of Revenues Over (Under) Expenditures	(2,073,050)	(2,094,823)
Other Financing Sources		
Transfer in from marina	-	50,000
Transfer in from general fund	532,976	163,000
Proceeds from bank loan	475,000	360,000
Proceeds from bank construction loans	100,000	650,000
Proceeds from state trust fund loan	1,249,979	826,907
Proceeds from promissory note	-	750,000
Total Other Financing Sources	2,357,955	2,799,907
Excess of Revenues and Other Financing Sources Over Expenditures	284,905	705,084
Fund Balance - January 1	705,083	-
Fund Balance - December 31	\$989,988	\$705,084

In 2003 and 2004 the above financial transactions were accounted for in the Village's general fund. Because of the significance of the long-term debt issued and the size of the projects, the financial transactions were separated out into a capital projects fund at year end. A separate capital projects fund on the Village's accounting software was created in 2005. This will give the Village increased ability to monitor financial transactions of the various projects.

4. Water Department Operations

Operating Results

A comparative analysis of the water department's income account for the years ended December 31, 2004 and 2003 follows:

	2004	2003
Operating Revenues		
General customers	\$164,888	\$160,374
Public fire protection	51,930	40,944
Miscellaneous	9,845	9,958
Total Operating Revenues	<u>226,663</u>	<u>211,276</u>
Operating Expenses		
Operation and maintenance	147,833	132,566
Depreciation	76,416	74,027
Taxes	4,021	27,027
Total Operating Expenses	<u>228,270</u>	<u>233,620</u>
Operating Income (Loss)	<u>(1,607)</u>	<u>(223,344)</u>
Nonoperating Revenues (Expenses)		
Interest income (estimated allocation)	7,464	11,173
Interest on long-term debt (estimated allocation)	(29,165)	(22,856)
Total Nonoperating Revenues (Expenses)	<u>(21,701)</u>	<u>(11,683)</u>
Net Income (Loss)	<u>\$(23,308)</u>	<u>\$(34,027)</u>

As shown above, the water utility incurred an operating loss of \$1,607 for the year. Although operations resulted in a loss, the utility did have a positive cash flow for the year. An operating loss indicates the utility did not entirely recover depreciation on its capital assets. Because of the operating loss, the Village is eligible for a rate increase.

5. Wastewater Department Operations

A comparative analysis of the wastewater department's income account for the years ended December 31, 2004 and 2003 follows:

	2004	2003
Operating Revenues		
General customers	\$221,512	\$192,877
Service to other systems	35,807	29,762
Other sewage service	41,937	40,314
Miscellaneous	2,668	2,599
Total Operating Revenues	<u>301,924</u>	<u>265,552</u>
Operating Expenses		
Operation and maintenance	266,882	301,894
Depreciation	296,178	274,771
Taxes	6,727	6,044
Total Operating Expenses	<u>569,787</u>	<u>582,709</u>
Operating Income (Loss)	<u>(267,863)</u>	<u>(317,157)</u>
Nonoperating Revenues (Expenses)		
Interest income (estimated allocation)	14,488	21,892
Contribution and subsidies for interest charges	61,155	68,975
Amortization of debt discount	(26,535)	(26,535)
Interest on long-term debt (estimated allocation)	(61,155)	(67,672)
Miscellaneous	18,996	5,608
Total Nonoperating Revenues (Expenses)	<u>6,949</u>	<u>2,268</u>
Net Income (Loss)	<u>\$(260,914)</u>	<u>\$(314,889)</u>

The above net losses result from the wastewater department not recovering sufficient revenues from customers to fund annual depreciation expense of \$296,178 and \$274,711 for 2004 and 2003, respectively. Because of the operating losses and additional funds needed for debt retirement, the Village is completing an analysis to determine increased rates.

6. Restricted Cash and Investments - Water and Wastewater Utility

Detail of restricted cash and investments of the Water and Wastewater Utility on December 31, 2004, follows:

<u>Fund</u>	<u>Amount</u>	<u>Description</u>
Water		
Plant replacement	\$162,113	To be used for the replacement of equipment and other assets of the water plant. (internally restricted by Village Board.)
Wastewater		
Revenue bond reserve	267,310	To reserve additional funds for debt retirement to be used if sufficient funds are not available in the Special Redemption Fund or otherwise available. (Required by the revenue bond ordinance.)
Plant replacement	444,314	To be used for the replacement of specific equipment and other assets of wastewater treatment plant. (Required by the DNR.)
Special Redemption Fund	77,160	To provide funds for the payment of principal and interest on the 1994 mortgage revenue bonds when due. (Required by the mortgage revenue bond ordinance.)
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Total Restricted Cash and Investments	<u>\$950,897</u>	

COMMENTS AND OBSERVATIONS

1. Implementation of GASB Statements No. 34, 37 and 38

The Village's 2004 financial statements are presented in accordance with the new financial reporting model for governmental entities as required by *Governmental Accounting Standards Board (GASB) Statements No. 34, 37 and 38*. Various restatements were made to the financial statements to conform to the new financial reporting model. Due to the significance of the restatement and changes to fund structure it was not practical to present comparative data for the 2003 calendar year in the basic financial statements.

While fund financial statements are still included in the Village's Annual Financial Report, the new reporting model offers many new features which we have summarized below:

- *Government-wide Financial Statements.* A "Statement of Net Assets" and a "Statement of Activities" have been added to the Village's basic financial statements on pages 3 and 4. These statements consolidate financial reporting for governmental activities of the Village. In addition, governmental activities in the government-wide financial statements are now accounted for in the same way as business-type activities (full accrual accounting) to provide financial statement users with a long-term financial perspective on these activities. Accordingly, capital assets of the Village are reported within the governmental activities. The new government-wide financial statements complement the Village's fund financial statements which continue to be reported on the short-term focus traditionally associated with these activities.

The statement of activities classifies expenses, including depreciation on capital assets, to functional areas. Revenues have been further classified into program revenues (those derived directly from a specific function) and general revenues (includes taxes, grants not relating to a specific program and interest income).

- *Major Fund Disclosures.* In the past, the Village's fund financial statements have aggregated all information for a fund type into one column. The new reporting model requires fund financial data to be included in the Village's basic financial statements for all major funds of the Village. The Village's major funds are the general fund, capital projects fund and water and sewer utility. This additional reporting of major fund information should be more useful to the Village's financial statement users.
- *Additional Budgetary Reporting.* In the past, comparisons of the Village's actual results were based on the final amended budget of the Village. Under the new reporting model, both the original and final amended budgets are presented for the general and any major special revenue funds.

GASB 34 also suggests that each government include in its annual financial report a Management's Discussion and Analysis (MDA). This discussion is prepared solely by the entity and briefly summarizes the financial positions and results of the current year. For the 2004 year the Village did not complete the MDA. This is something the Village may want to consider in the future.

2. Status of New Accounting System

Prior to the start of 2005 we assisted the Village in upgrading its financial software and accounting system. The Windows version of American Fundware was installed along with the automated payroll module. In addition, we assisted the Village in developing a new multi-fund chart of accounts to provide the framework for increased accountability of financial transactions. Also, capital projects were assigned unique numbers to track funds appropriated and spent over multiple years.

Although the account structure and software is in place, at the current time, the Village is not completely up-to-date with verifying transaction entries and utilizing the expanded features of the new accounting system. Because of the changes in procedures and the additional complexity of the system, it is our experience that it will take Village personnel a few months to become familiar with the new system. Also, additional assistance and review of recorded transactions by a professional accountant may be necessary to provide feedback over the most efficient method of recording and balancing transactions. We are available to assist Village personnel in learning the features of the new system.

3. Potential Enhancements to Village's Internal Control Structure

During 2005 the Village hired a new utility bookkeeper and moved the utility accounting office into the administration building. As a result both the Village Clerk and the utility bookkeeper work in the same building and provide the Village with increased opportunity to enhance the internal accounting control system in place. Specifically, the two employees can be cross-trained in each system to provide backup when needed. Also, consideration could be given to combining both the utility and the general accounting in one balance-fund system. With this setup, operating cash could be combined to provide additional efficiencies, along with a distribution of accounting duties among the two employees to increase internal control.

Without combining the accounting into one system, there are still additional control procedures that could be considered to increase the oversight and internal accounting controls. In our opinion, the following procedures could be considered:

- Require two signatures on all Village checks, along with having the Village President's signature stamp in the possession of the Village Administrator to be placed on checks for distribution.
- Review and approval of monthly bank reconciliations by the Village Administrator.
- Review and approval of accounting journal entries by someone other than the preparer.
- Development of a general Village invoice and accounts receivable system.

OTHER REQUIRED COMMUNICATION

In accordance with the requirements of government auditing standards generally accepted in the United States of America, the following disclosures are presented:

1. **Significant Accounting Policies**

The significant accounting policies used in the preparation of the financial statements are disclosed in Note A to the basic financial statements. There have been no material unusual transactions or controversial accounting issues.

2. **Accounting Estimates**

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's current judgments. We are not aware of any particularly sensitive accounting estimates used by management in the preparation of the financial statements.

3. **Significant Audit Adjustments**

The financial statements reflect all accounting adjustments proposed during our audit. None of the adjustments were considered significant to the financial condition or operating results of the Village. Copies of the audit adjustments are available from management.

4. **Other Information in Documents Containing Audited Financial Statements**

All the information included in the basic financial statements has been audited. Our responsibilities are addressed in the Independent Auditors' Report.

5. **Disagreements with Management**

We have had no material disagreements with management. For the purposes of this disclosure, professional accounting standards define a disagreement with management as a matter concerning a financial accounting, reporting, or auditing matter that could be significant to the financial statements or the auditors' report.

6. **Consultations with Other Auditors**

To the best of our knowledge, management has not consulted with or obtained opinions from other independent auditors on auditing and accounting matters during the past year.

7. **Issues Discussed Prior to the Current Audit**

We have discussed various accounting and financial issues, including the application of any new and changed accounting principles or auditing standards, with management prior to conducting the audit. These discussions occurred in the normal course of our professional relationship and our responses were not a condition to completing the services as your auditor.

8. **Difficulties Encountered in Performing the Audit**

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