CITY OF MELROSE
MELROSE, MINNESOTA

MANAGEMENT LETTER

FOR THE YEAR ENDED
DECEMBER 31, 2013

ABDO EICK & MEYERS LLP
Certified Public Accountants & Consultants

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FOR THE YEAR ENDED
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ABDO EICK & MEYERS LLP
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March 27, 2014

Management, Honorable Mayor and City Council
City of Melrose, Minnesota

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Melrose, Minnesota (the City), for the year ended December 31, 2013. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards and *Government Audit Standards* as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter dated November 6, 2013. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility Under Auditing Standards Generally Accepted in the United States of America and *Government Auditing Standards*

As stated in our engagement letter, our responsibility, as described by professional standards, is to express opinions about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve you or management of your responsibilities.

Our responsibility is to plan and perform the audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement. As part of our audit, we considered the internal control over financial reporting of the City. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control. We are responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures specifically to identify such matters.

Significant Audit Findings

In planning and performing our audit, we considered the City's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

A *deficiency in internal control* 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 and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We identified certain deficiencies in internal control, described on the following pages as findings 2013-001 and 2013-002 that we consider to be significant deficiencies.

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2013-001 Preparation of financial statements

Condition: As in prior years, we were requested to draft the audited financial statements and related footnote disclosures as part of our regular audit services. Recent auditing standards require auditors to communicate this situation to the City Council as an internal control deficiency. Ultimately, it is management's responsibility to provide for the preparation of your statements and footnotes, and the responsibility of the auditor to determine the fairness of presentation of those statements. It is our responsibility to inform you that this deficiency could result in a material misstatement to the financial statements that could have been prevented or detected by your management. Essentially, the auditors cannot be part of your internal control process.

Criteria: Internal controls should be in place to provide reasonable assurance over financial reporting.

Cause: From a practical standpoint we do both for you at the same time in connection with our audit. This is not unusual for us to do with an organization of your size.

Effect: The effectiveness of the internal control system relies on enforcement by management. The effect of deficiencies in internal controls can result in undetected errors in financial reporting.

Recommendation: It is your responsibility to make the ultimate decision to accept this degree of risk associated with this condition because of cost or other considerations. As in prior years, we have instructed management to review a draft of the auditor prepared financial statements in detail for their accuracy; we have answered any questions they might have, and have encouraged research of any accounting guidance in connection with the adequacy and appropriateness of classification of disclosure in your statements. We are satisfied that the appropriate steps have been taken to provide you with the completed financial statements. While the City is reviewing the financial statements we recommend that a disclosure checklist be utilized to ensure all required disclosures are presented and the City should agree its financial software to the numbers reported in the financial statements.

Management response:

For now, the City's management accepts the degree of risk associated with this condition and thoroughly reviews a draft of the financial statements.

2013-002 Reconciliation of investments

Condition: During our audit, we noted that although reconciliations were partially completed for the City's investment accounts, finance system entries are not always completed for each transaction.

Criteria: Timely reconciliations are an important control activity in the City's overall internal control structure.

Cause: An investment report derived from a complex tracking system is prepared monthly and from our review it appears to contain most of the data necessary to agree the investments to the finance system, however, due to staff turnover, it appears that there was not a procedure in place to ensure the report was agreed to the finance system.

Effect: As a result there was unrecorded activity including the market value adjustment at year end.

Recommendation: We recommend that the City put controls in place to ensure investments are reconciled to the finance system each month and that all investment activity is recorded. Implementing this recommendation will not result in any additional cost and will ensure that finance system data is complete.

Management response:

The City has developed streamlined tracking and reconciliation procedures and an investment schedule that will allow for complete reconciliation to the finance system. The City will complete procedures to ensure timely investment reconciliations are completed.

Compliance

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* or statutes set forth by the State of Minnesota.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing.

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the City are described in Note 1 to the financial statements. The application of existing policies was not changed during the year. We noted no transactions entered into by the City during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most significant estimates affecting the financial statements were capital asset basis, depreciation, compensated absences, other postemployment benefits, and allocation of payroll.

We evaluated the key factors and assumptions used to develop these accounting estimates in determining that it is reasonable in relation to the financial statements taken as a whole.

The disclosures in the financial statements are neutral, consistent, and clear. Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management.

We also assisted in preparing a number of year end accounting entries. These were necessary to adjust the City's records at year end to correct ending balances.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representations letter March 27, 2014**.**

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the City's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the City's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Other Matters

The City sold the Centracare facility to CentraCare Health Systems on July 1, 2013. The transaction consisted of the sale of two parcels of land to CentraCare as well as the issuance of a $1,329,500 non-negotiable note receivable. The note is receivable from Centracare with semi-annually payments scheduled starting January 1, 2014 through July 1, 2023 at 2 percent interest. The sale of the facility resulted in the recognition of $1,329,500 of revenue as noted as a special item in the financial statements.

With respect to the supplementary information accompanying the financial statements, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

Financial Position and Results of Operations

Our principal observations and recommendations are summarized on the following pages. These recommendations resulted from our observations made in connection with our audit of the City's financial statements for the year ended December 31, 2013.

General Fund

The General fund is used to account for resources traditionally associated with government, which are not required legally or by sound principal management to be accounted for in another fund. The General fund balance increased $56,252 from 2012. The fund balance of $1,361,134 is 63 percent of the 2013 expenditures and transfers out.

We recommend the fund balance be maintained at a level sufficient to fund operations until the major revenue sources are received in June. The City has formally adopted a fund balance policy for the General fund to maintain a minimum unrestricted fund balance of 35-50 percent of the next year's budgeted expenditures. The City's ending fund balance is above this target level.

The purposes and benefits of a fund balance are as follows:

- Expenditures are incurred somewhat evenly throughout the year. However, property tax and state aid revenues are not received until the second half of the year. An adequate fund balance will provide the cash flow required to finance the governmental fund expenditures.

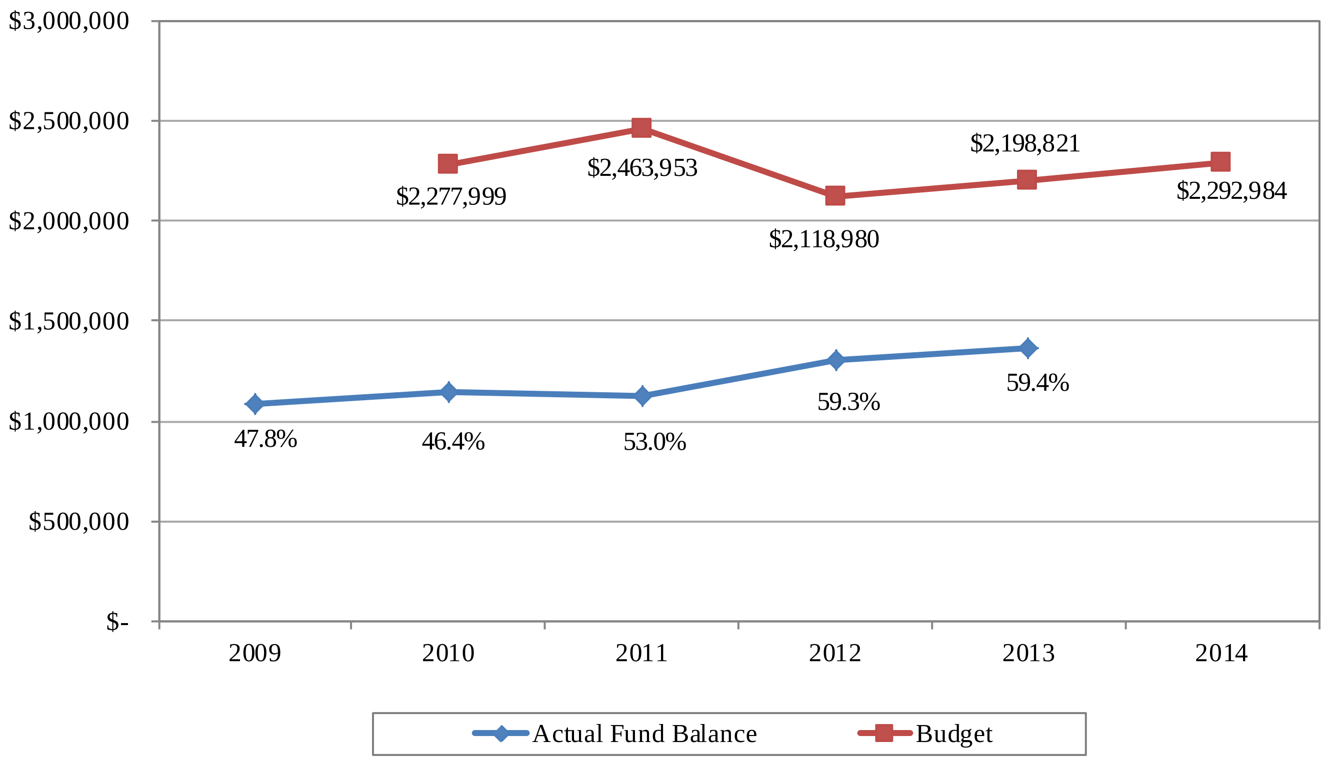
- Expenditures not anticipated at the time the annual budget was adopted may need immediate City Council action. These would include capital outlay, replacement, lawsuits and other items. An adequate fund balance will provide the financing needed for such expenditures.

- A strong fund balance will assist the City in maintaining, improving or obtaining its bond rating. The result will be better interest rates in future bond sales.

A table summarizing the General fund balance in relation to the following years' budget follows:

Year	Fund Balance December 31	Budget Year	General Fund Budget	Percent of Fund Balance to Budget
2009	$ 1,089,358	2010	$ 2,277,999	47.8 %
2010	1,143,622	2011	2,463,953	46.4
2011	1,122,806	2012	2,118,980	53.0
2012	1,304,882	2013	2,198,821	59.3
2013	1,361,134	2014	2,292,984	59.4

Fund Balance as a Percent of Next Year's Budget



We have compiled a peer group average derived from information we have requested from the Office of the State Auditor for Cities of the 4th class which have populations of 2,500-10,000. In 2011 and 2012, the average General fund balance as a percentage of expenditures was 69 percent and 76 percent, respectively.

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A summary of the 2013 operations are as follows:

	Final Budget Amounts	Actual Amounts	Variance with Final Budget
Revenues	$ 2,163,811	$ 2,229,863	$ 66,052
Expenditures	1,621,862	1,602,482	19,380
Excess of revenues over expenditures	541,949	627,381	85,432
Other financing sources (uses)			
Transfers in	40,000	-	(40,000)
Transfers out	(576,959)	(571,129)	5,830
Total other financing sources (uses)	(536,959)	(571,129)	(34,170)
Net change in fund balances	4,990	56,252	51,262
Fund balances, January 1	1,304,882	1,304,882	-
Fund balances, December 31	$ 1,309,872	$ 1,361,134	$ 51,262

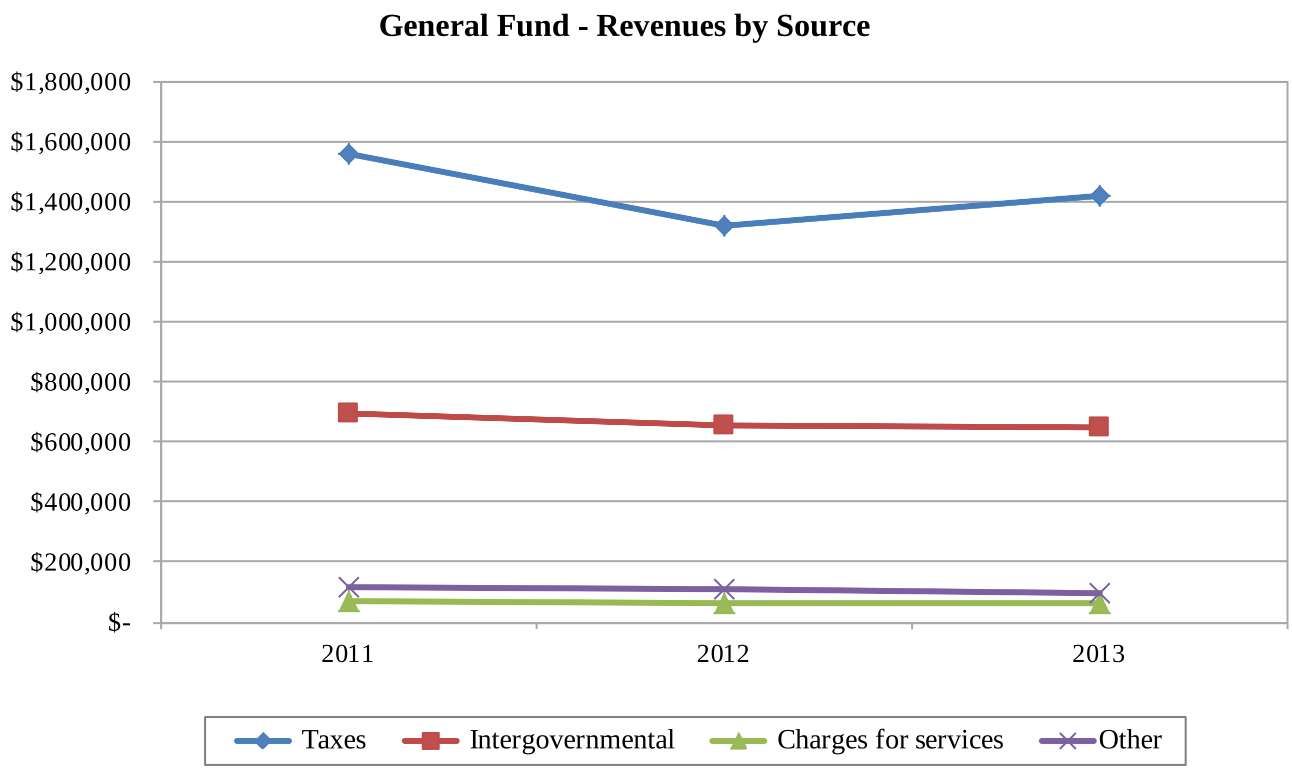
- The most significant revenue variances were in taxes and intergovernmental revenue which were over budget by $42,010 and $21,808, respectively. The taxes variance was mostly due to delinquent tax collections, and the majority of the intergovernmental increase related to local government aid coming in $23,735 higher than budget.

- The most significant expenditure variance was in the general government and streets and highways functions which were under budget by $42,710 and $15,695, respectively.

A comparison between 2011, 2012, and 2013 General fund revenues is presented below:

Revenue Source	2011	2012	2013	Percent of Total	Per Capita
Taxes	$ 1,561,902	$ 1,320,776	$ 1,418,010	63.5 %	$ 390
Licenses and permits	50,592	48,217	44,421	2.0	12
Intergovernmental	697,180	655,259	650,769	29.2	179
Charges for services	66,951	63,019	62,244	2.8	17
Fines and forfeitures	27,774	18,825	18,545	0.8	5
Interest on investments	23,980	29,544	19,203	0.9	5
Miscellaneous	11,555	13,253	16,671	0.8	5
Total revenues	$ 2,439,934	$ 2,148,893	$ 2,229,863	100.0 %	$ 613

A graphical presentation of 2011, 2012, and 2013 revenues follows:



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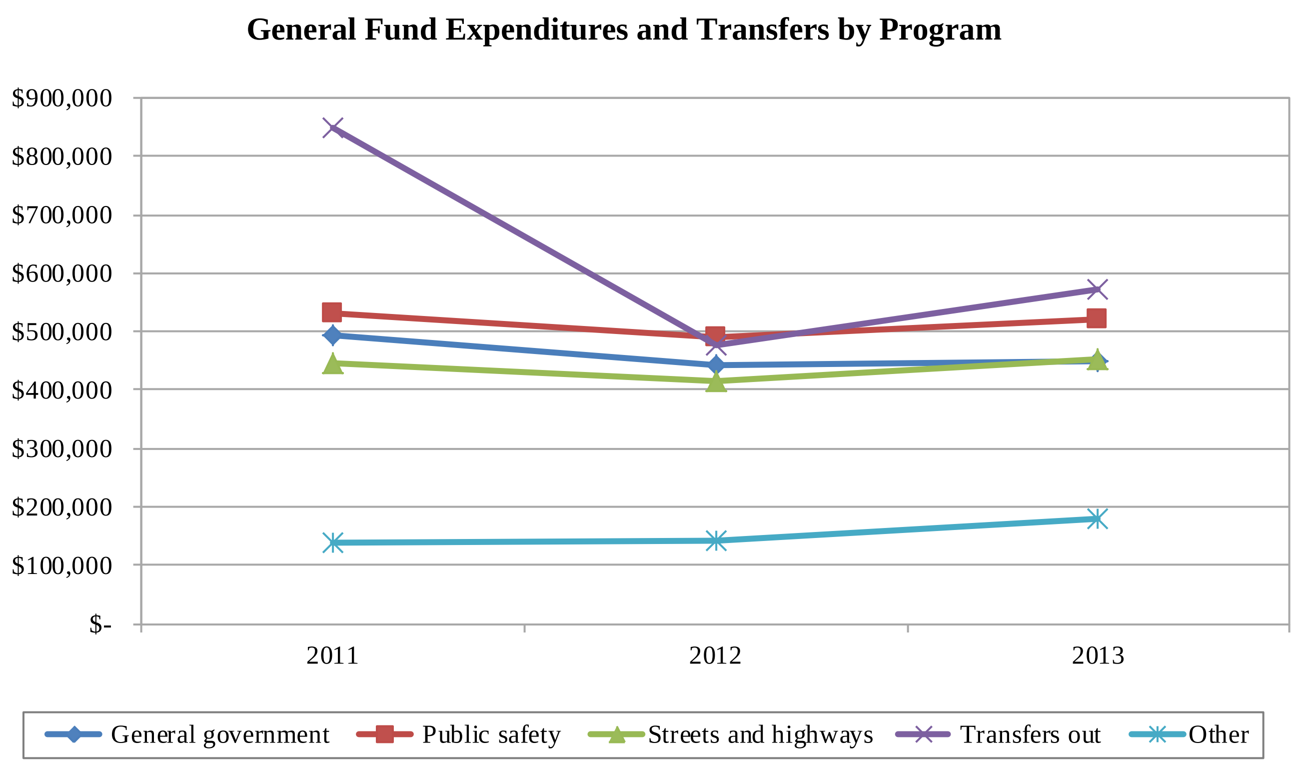
A comparison between 2011, 2012, and 2013 General fund expenditures and transfers is presented below:

Program	2011	2012	2013	Percent of Total	Per Capita	Peer Group Per Capita
Current						
General government	$ 494,674	$ 443,745	$ 448,253	20.6 %	$ 123	$ 125
Public safety	532,136	491,013	522,662	24.0	144	218
Streets and highways	445,912	414,043	453,118	20.8	125	106
Sanitation	4,515	5,255	4,119	0.2	1	-
Culture and recreation	49,628	51,285	59,284	2.7	16	54
Economic development	83,226	84,489	90,654	4.2	25	4
Total current	1,610,091	1,489,830	1,578,090	72.5	434	507
Capital outlay	-	-	23,174	1.1	6	34
Debt service	786	1,468	1,218	0.1	-	-
Transfers out	849,873	475,519 *	571,129	26.3	157	-
Total expenditures and transfers	$ 2,460,750	$ 1,966,817	$ 2,173,611	100.0 %	$ 597	$ 541

* Decrease in transfer out related to the issuance of the 2011A crossover refunding bonds. A transfer from the General fund to support the debt service payments was no longer necessary.

The above chart compares the amount the City spends per capita, in comparison to a peer group. The peer group average is compiled from information from approximately 120 fourth class cities (populations 2,500-10,000) and is derived from information available on the website of the Office of the State Auditor.

A graphical presentation of 2011, 2012, and 2013 expenditures and transfers totals by program follows:



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Special Revenue Funds

The nonmajor special revenue funds account for revenue sources that are restricted or committed to expenditure for specified purposes. The funds in this account group include:

Fund	Fund Balances December 31, 2013	Fund Balances December 31, 2012	Increase (Decrease)
Nonmajor			
Melrose Area Development Authority (MADA)	$ (16,816)	$ (17,536)	$ 720
MADA Revolving Loan	582,368	563,776	18,592
Senior Activity Center	2,875	3,064	(189)
PIA Asset Building	248	522	(274)
Tri-Cap Bus	5,838	3,741	2,097
Yellow Bike Program	1,899	-	1,899
Fire Department	221,405	163,922	57,483
Total	$ 797,817	$ 717,489	$ 80,328

All funds should have sufficient resources to provide for their operations but occasionally deficits will occur. MADA's deficit is expected to be funded with future revenue in excess of expenditures. In addition to the fund balance above, MADA Revolving Loan fund has approximately $399,000 in current loans receivable.

Capital Projects Funds

The capital projects funds account for the financial resources that are restricted, committed, or assigned to expenditure for capital outlays, including the acquisition or construction of capital facilities and other capital assets not being financed by proprietary funds. The funds in this group include:

Fund	Fund Balances December 31, 2013	Fund Balances December 31, 2012	Increase (Decrease)
Major			
Capital improvements	$ 3,701,460	$ 3,372,323	$ 329,137

In 1990, several of the designated funds within the General fund were transferred to establish the Capital Improvements fund. Other revenue sources, which were available, have been transferred to this fund. This fund gives the City the ability to finance its capital improvement projects internally rather than issuing bonds and incurring the related issuance costs. The City has also planned well for its use through a thorough fund balance policy.

Debt Service Funds

Debt Service funds are a type of governmental fund to account for the accumulation of resources for the payment of interest and principal on debt (other than enterprise fund debt).

Debt Service funds may have one or a combination of the following revenue sources pledged to retire debt as follows:

- Property taxes - Primarily for general City benefit projects such as streets and municipal buildings. Property taxes may also be used to fund special assessment bonds which are not fully assessed.
- Capitalized interest portion of bond proceeds - After the sale of bonds, the project may not produce revenue (tax increments or special assessments) for a period of one to two years. Bonds are issued with this timing difference considered in the form of capitalized interest.
- Special assessments - Charges to benefited properties for various improvements.

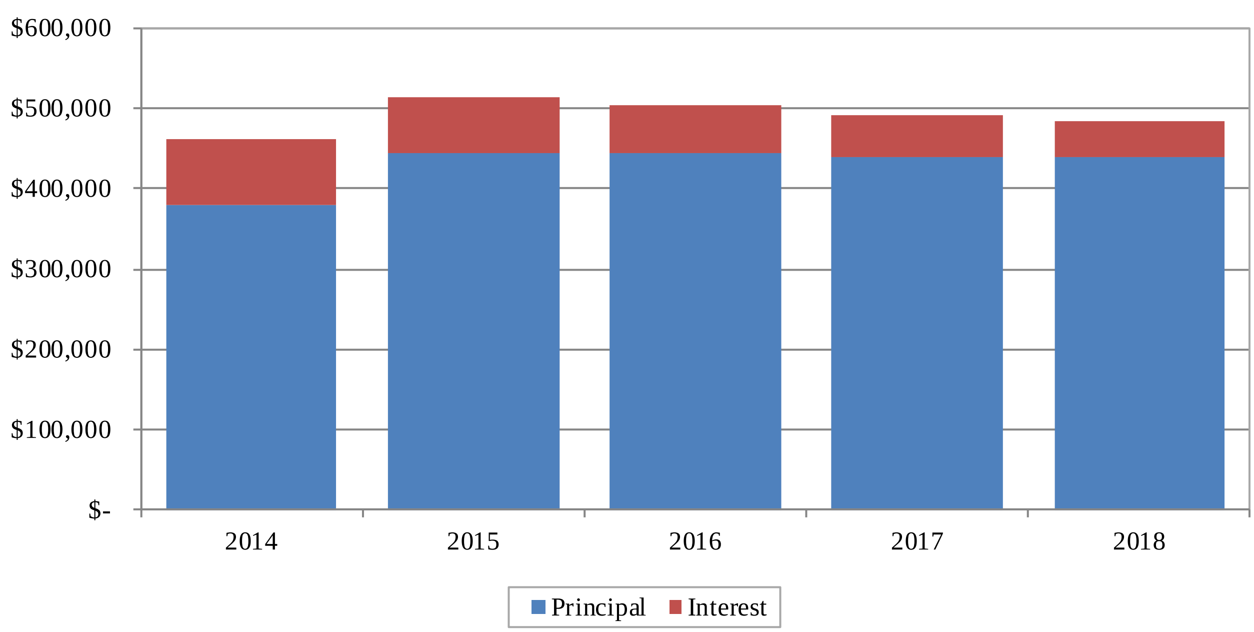
In addition to the above pledged assets, other funding sources may be received by Debt Service funds as follows:

- Residual project proceeds from the related capital projects fund
- Investment earnings
- Transfers from other funds

The following is a recap of the various Debt Service fund assets and the related bond principal outstanding:

Debt Description	Cash Balance	Total Assets	Bonds Outstanding	Year of Maturity
G.O. Improvement Refunding Bonds, Series 2011A	$ 404,780	$ 592,197	$ 2,065,000	02/01/20
G.O. Capital Improvement Plan Bonds, Series 2013A	148,311	148,311	1,965,000	02/01/28
Total	$ 553,091	$ 740,508	$ 4,030,000	
Total future scheduled interest payments			$ 461,965	

Debt Service Scheduled Principal and Interest for the Next 5 Years



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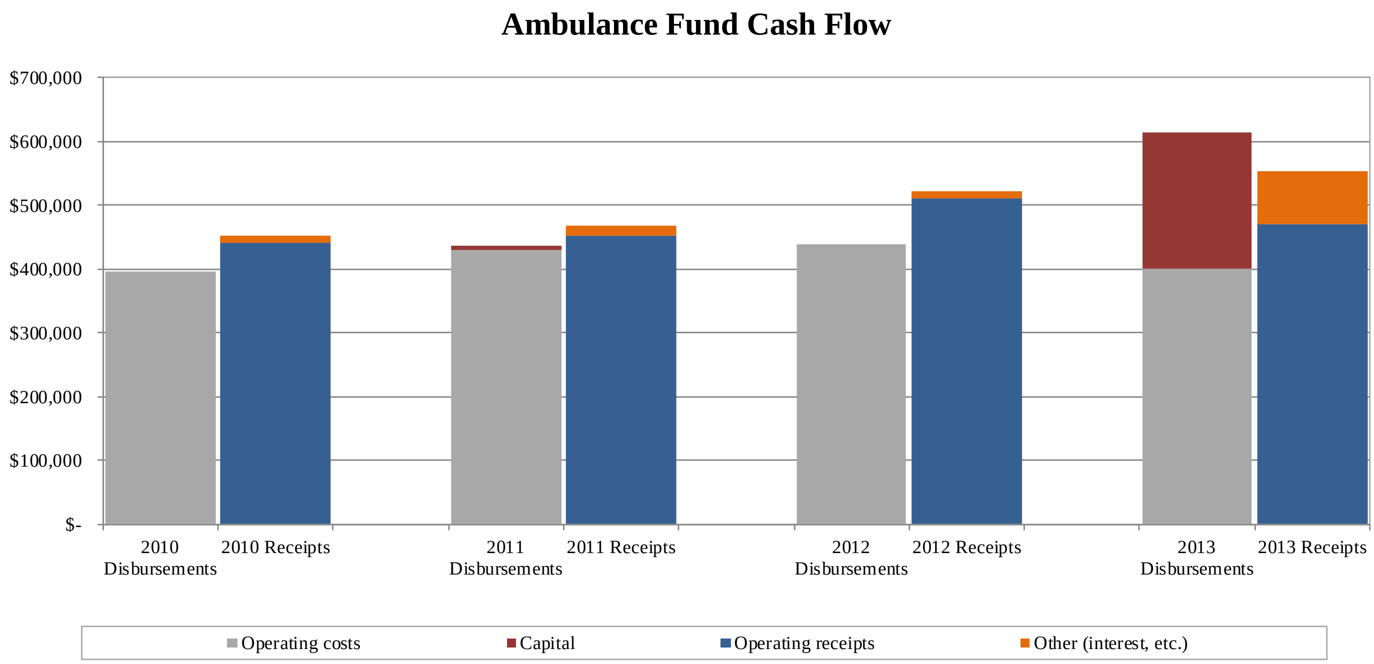
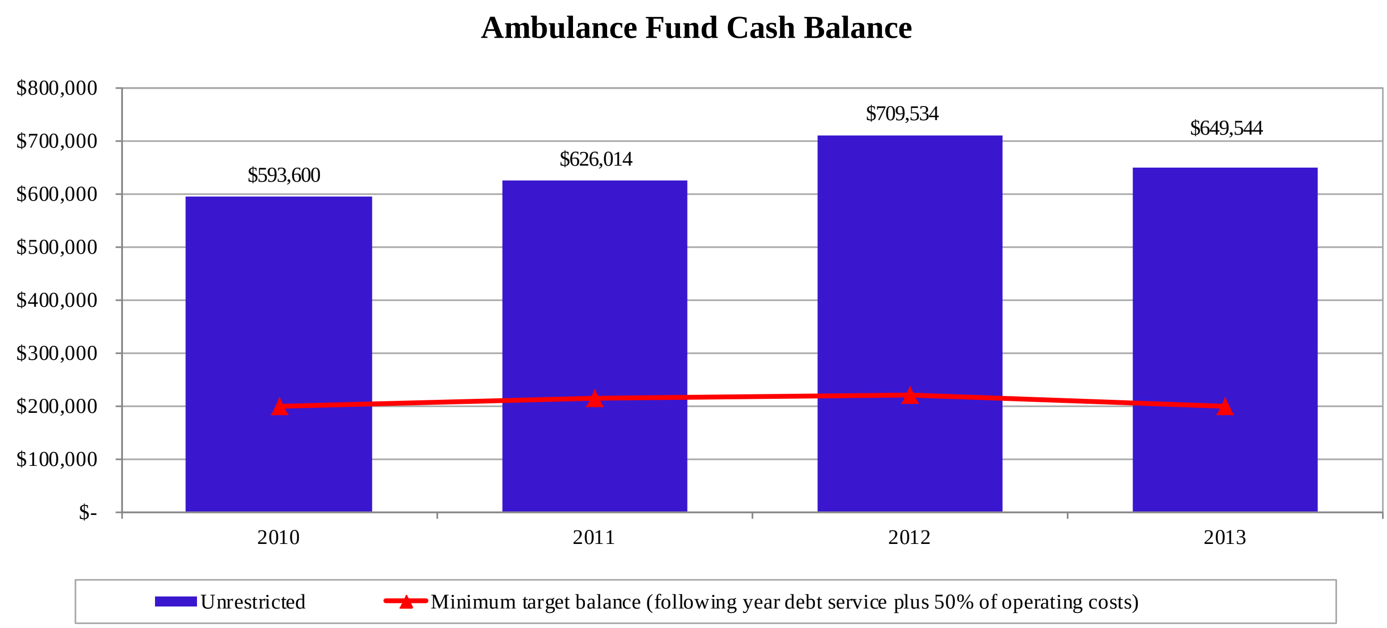
Enterprise Funds

Ambulance Fund

The results of the operations in terms of cash flow and the breakdown of the cash balances for the past four years are as follows:



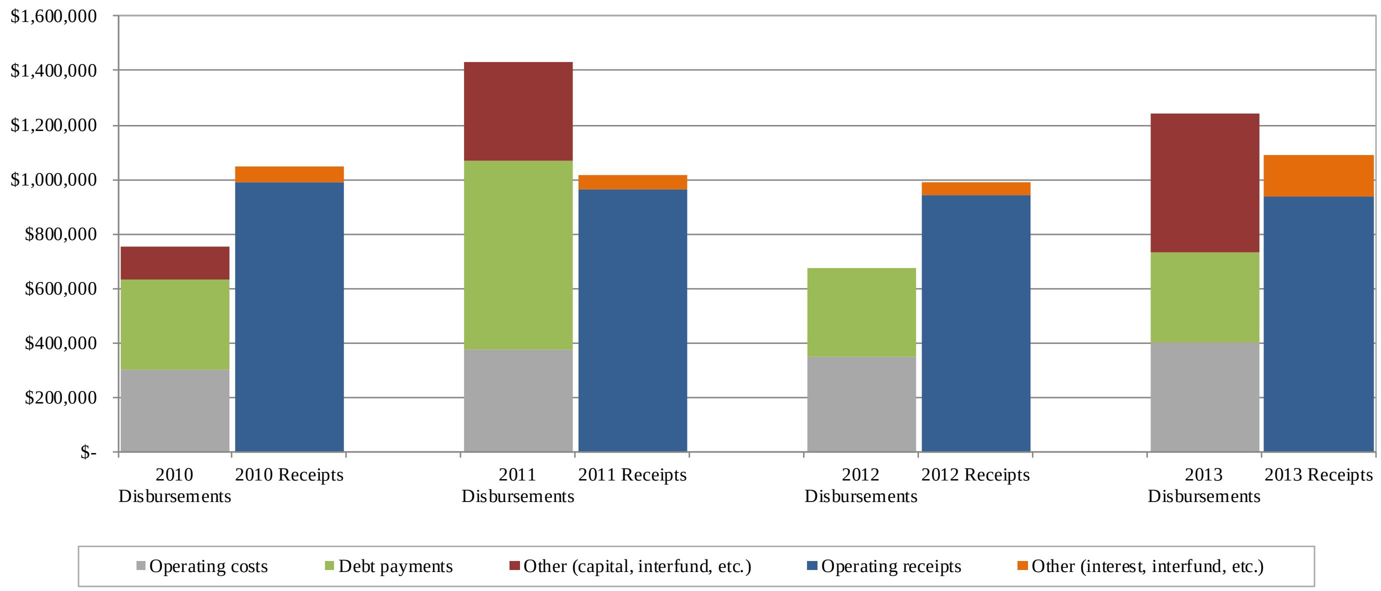


The cash balance decreased from the prior year; however, it is still at a level sufficient to provide for working capital and other needs. The decrease in cash balance was mostly due to collections from Medicare and Medicaid being behind due to new procedures with the Affordable Care Act, as well as the purchase of two ambulances. The change in net position was positive and the fund has healthy reserves relative to operations.

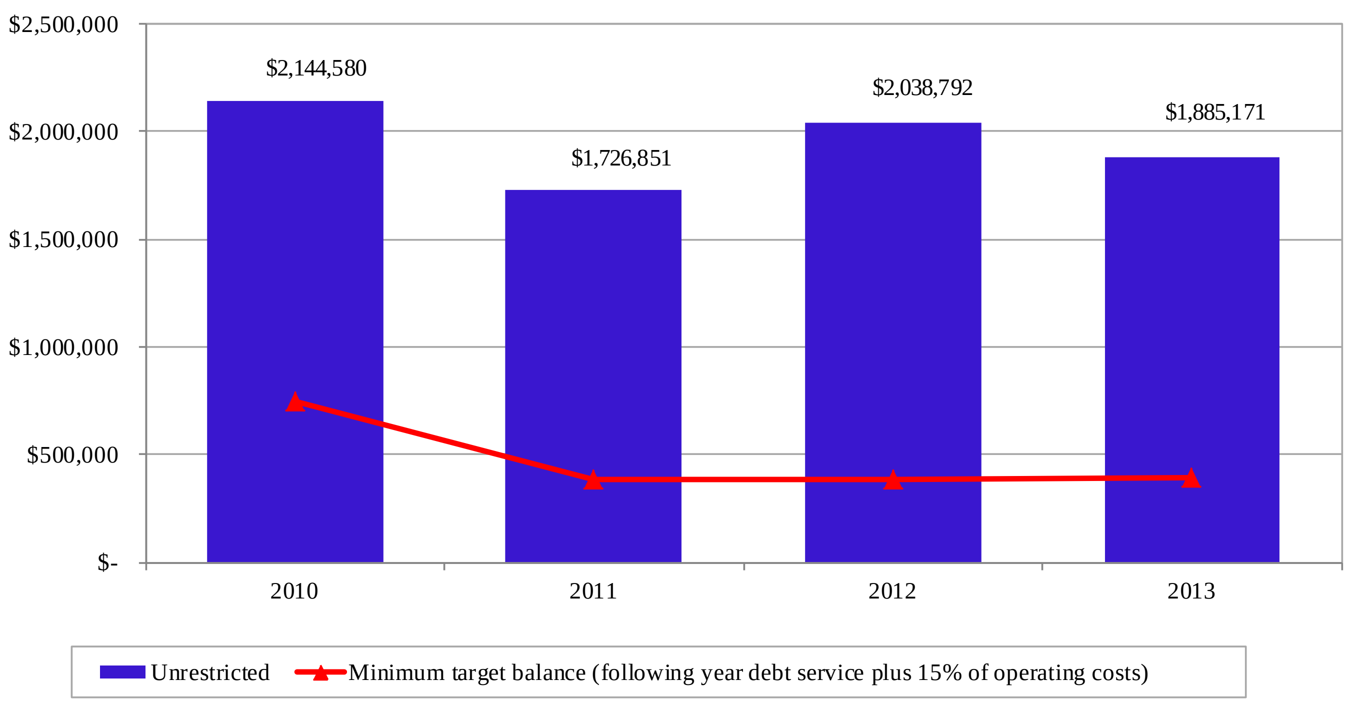
Water Fund

The results of the operations in terms of cash flow and the breakdown of the cash balances for the past four years are as follows:

Water Fund Cash Flow



Water Fund Cash Balance



The operating income has been adequate to support cash flow needs in the past and is expected to remain sufficient but it is always important to review cash flow each year to determine if rates are adequate to cover operations and debt service. The water fund paid $465,000 toward the cost of an AMI water meter reading system.

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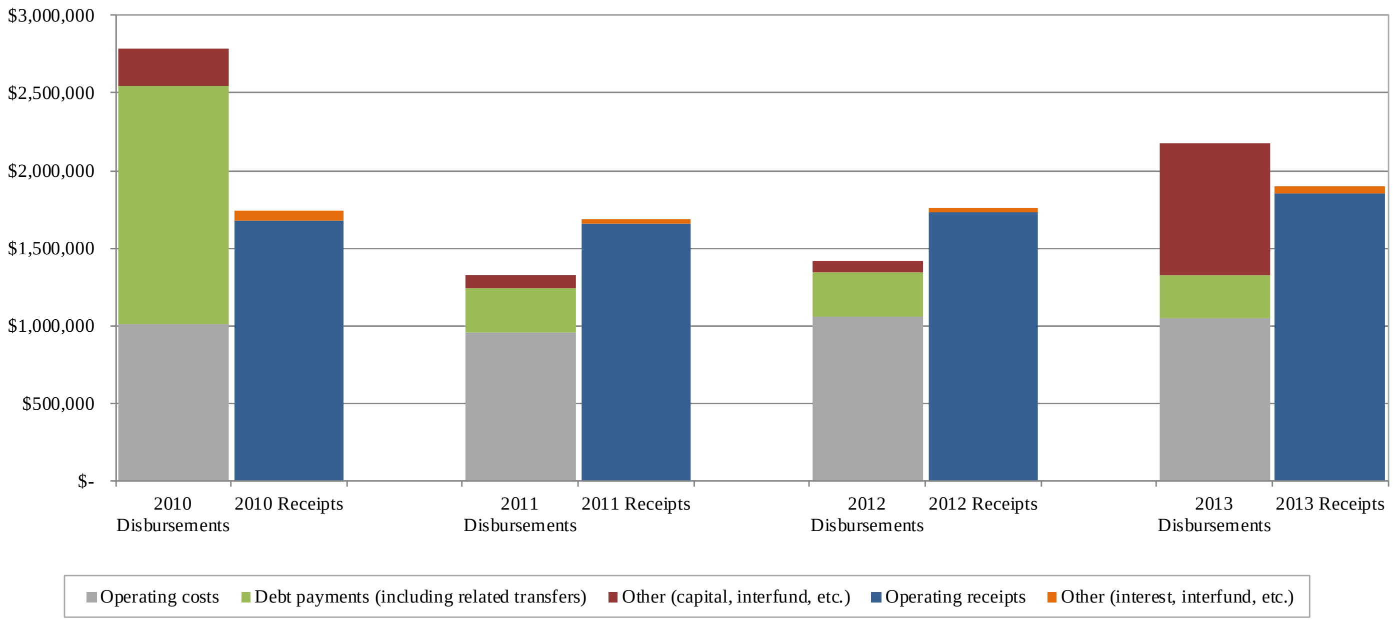
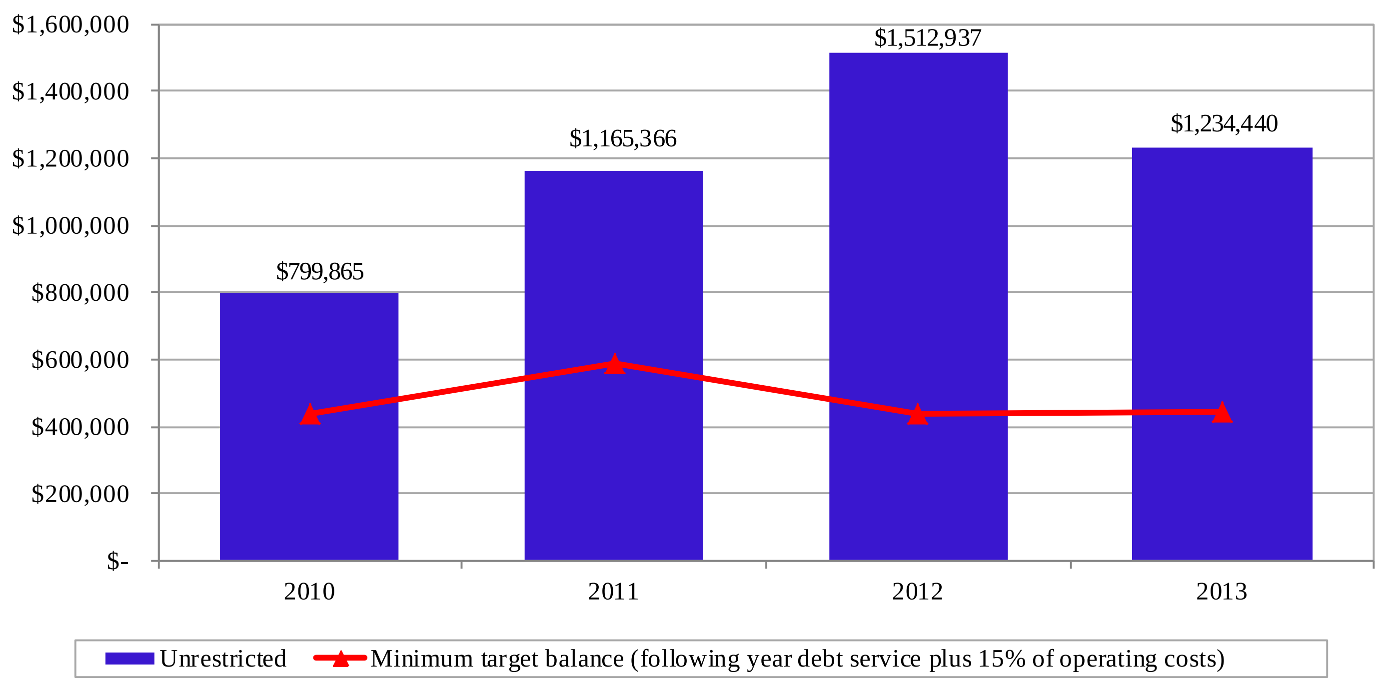
Wastewater Fund

The results of the operations in terms of cash flow and the breakdown of the cash balances for the past four years are as follows:

Wastewater Fund Cash Flow



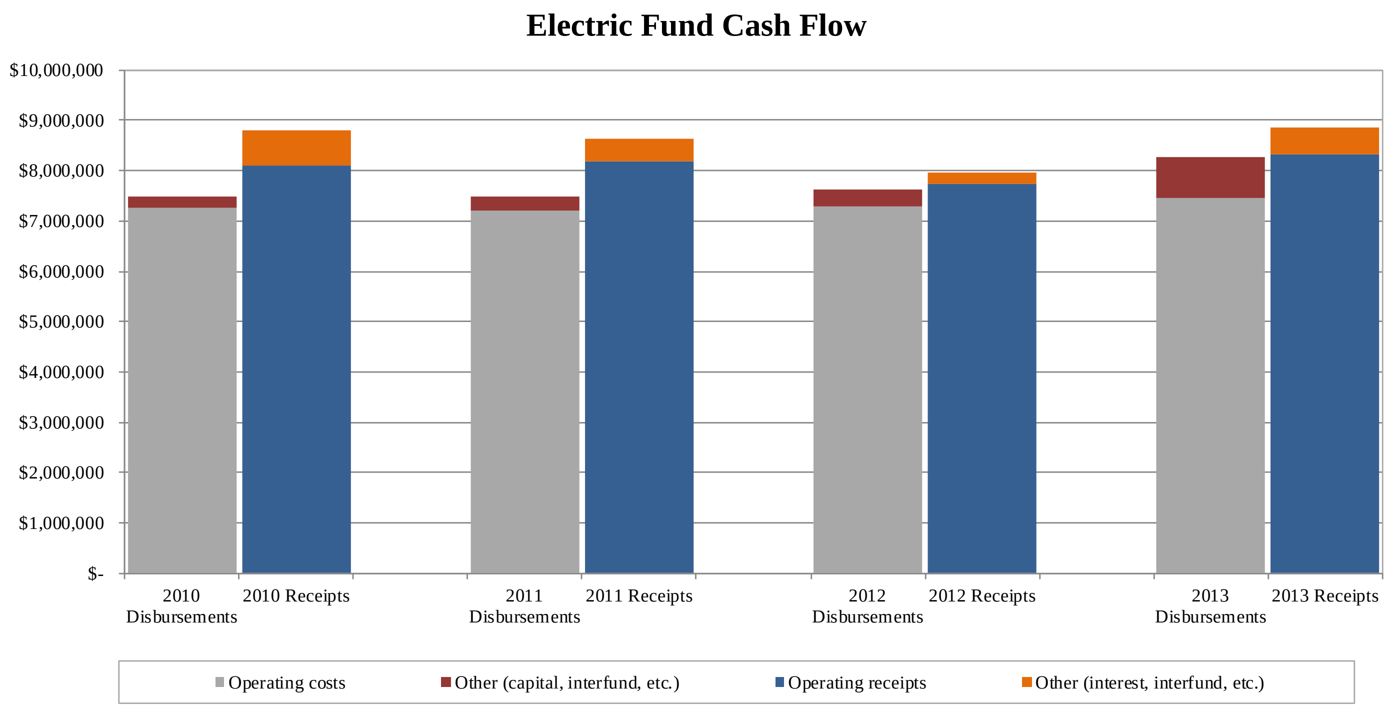
Wastewater Fund Cash Balance

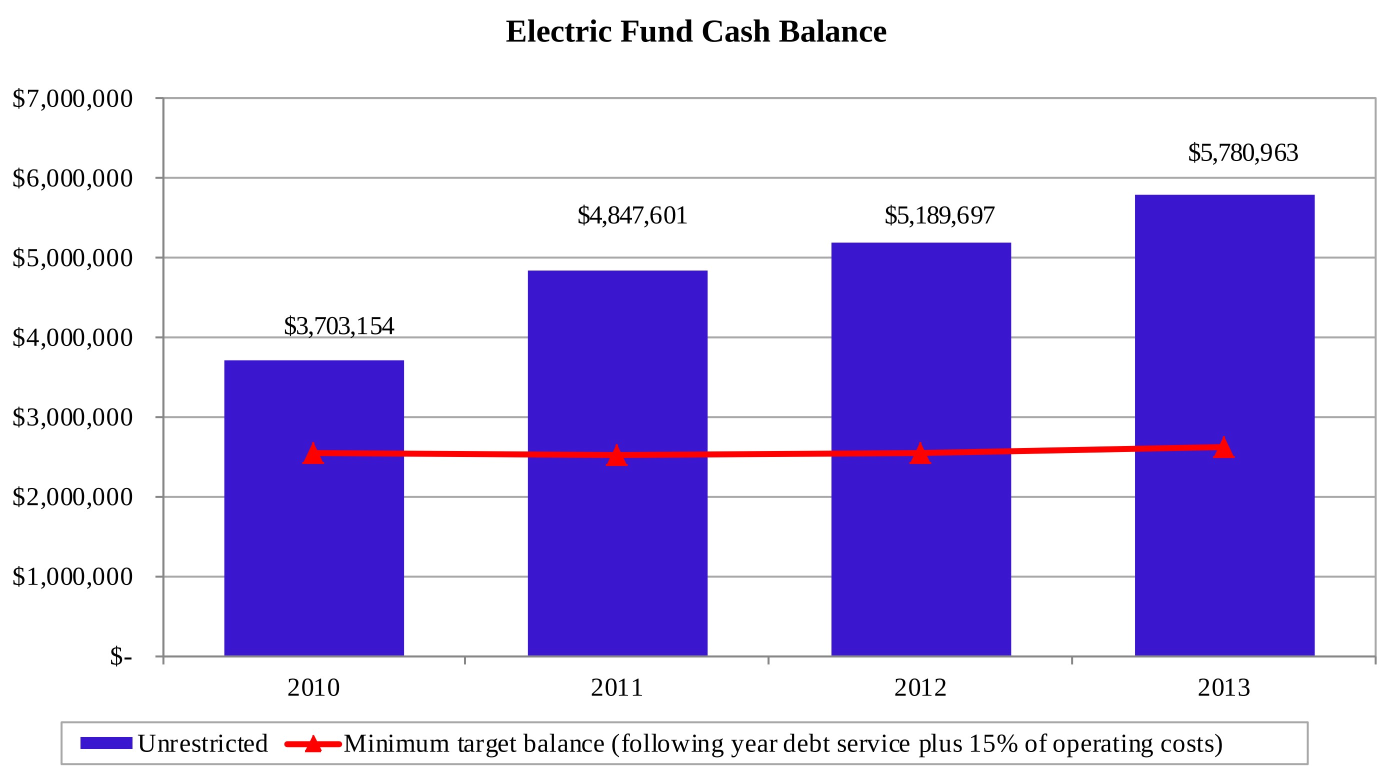


The cash balance remains strong in relation to operations but like the Water fund, it will be important to maintain cash flow to cover future debt service. In 2010, the City issued $1,415,000 of crossover refunding bonds, and transferred $1,250,000 to escrow to pay the $2,600,000 called Revenue Bonds of 2004 on December 1, 2012. Significant other expenses in 2013 were due to transfers to the Water and Electric funds as reimbursement for its portion of the AMI project costs and a transfer to the Electric fund for a generator, as well as other capital outlay expenditures.

Electric Fund

The results of the operations in terms of cash flow and the breakdown of the cash balances for the past four years are as follows:





In 2013, the operating income covered the operating and other costs of the fund allowing the cash balance to again increase. Significant other expenses in 2013 were mainly due to the Electric fund's portion of the AMI project costs and the purchase of a generator. Like the Water and Wastewater funds, it is always important to review cash flow each year to determine if rates are adequate to cover operations.

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Ratio Analysis

The following captures a few ratios from the City's financial statements that give some additional information for trend and peer group analysis. The peer group average is derived from information available on the website of the Office of the State Auditor for Cities of the 4th class (2,500-10,000). The majority of these ratios facilitate the use of economic resources focus and accrual basis of accounting at the government-wide level. A combination of liquidity (ability to pay its most immediate obligations), solvency (ability to pay its long-term obligations), funding (comparison of financial amounts and economic indicators to measure changes in financial capacity over time) and common-size (comparison of financial data with other cities) ratios are shown below.

Ratio	Calculation	Source	2010	2011	2012	2013
Debt to assets	Total liabilities/total assets	Government-wide	25% *37%*	26% *33%*	20% *33%*	15% *N/A*
Debt service coverage	Net cash provided by operations/ enterprise fund debt payments	Enterprise funds	219% *102%*	321% *106%*	206% *106%*	221% *N/A*
Debt per capita	Bonded debt/population	Government-wide	$ 3,555 *$ 3,125*	$ 3,659 *$ 2,826*	$ 2,519 *$ 2,626*	$ 1,814 *N/A*
Taxes per capita	Tax revenues/population	Government-wide	$ 489 *$ 407*	$ 462 *$ 500*	$ 470 *$ 480*	$ 489 *N/A*
Current expenditures per capita	Governmental fund current expenditures/population	Governmental funds	$ 599 *$ 624*	$ 539 *$ 640*	$ 483 *$ 649*	$ 499 *N/A*
Capital expenditures per capita	Governmental fund capital outlay/population	Governmental funds	$ 53 *$ 265*	$ 44 *$ 229*	$ 175 *$ 298*	$ 200 *N/A*
Capital assets % left to depreciate - Governmental	Net capital assets/ gross capital assets	Government-wide	73% *61%*	71% *64%*	69% *65%*	68% *N/A*
Capital assets % left to depreciate - Business-type	Net capital assets/ gross capital assets	Government-wide	59% *59%*	56% *65%*	54% *63%*	51% *N/A*

Represents the City of Melrose

Represents Peer Group Average

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Debt-to-Assets Leverage Ratio (Solvency Ratio)

The debt-to-assets leverage ratio is a comparison of a city's total liabilities to its total assets or the percentage of total assets that are provided by creditors. It indicates the degree to which the City's assets are financed through borrowings and other long-term obligations (i.e. a ratio of 50 percent would indicate half of the assets are financed with outstanding debt).

Debt Service Coverage Ratio (Solvency Ratio)

The debt coverage ratio is a comparison of cash generated by operations to total debt service payments (principal and interest) of enterprise funds. This ratio indicates if there are sufficient cash flows from operations to meet debt service obligations. Except in cases where other nonoperating revenues (i.e. taxes, assessments, transfers from other funds, etc.) are used to fund debt service payments, an acceptable ratio would be above 100 percent.

Bonded Debt per Capita (Funding Ratio)

This dollar amount is arrived at by dividing the total bonded debt by the population of the City and represents the amount of bonded debt obligation for each citizen of the City at the end of the year. The higher the amount, the more resources are needed in the future to retire these obligations through taxes, assessments or user fees.

Taxes per Capita (Funding Ratio)

This dollar amount is arrived at by dividing the total tax revenues by the population of the City and represents the amount of taxes for each citizen of the City for the year. The higher this amount is, the more reliant the City is on taxes to fund its operations.

Current Expenditures per Capita (Funding Ratio)

This dollar amount is arrived at by dividing the total current governmental expenditures by the population of the City and represents the amount of governmental expenditure for each citizen of the City during the year. Since this is generally based on ongoing expenditures, we would expect consistent annual per capita results.

Capital Expenditures per Capita (Funding Ratio)

This dollar amount is arrived at by dividing the total governmental capital outlay expenditures by the population of the City and represents the amount of capital expenditure for each citizen of the City during the year. Since projects are not always recurring, the per capita amount will fluctuate from year to year.

Capital Assets Percentage (Common-size Ratio)

This percentage represents the percent of governmental or business-type capital assets that are left to be depreciated. The lower this percentage, the older the City's capital assets are and may need major repairs or replacements in the near future. A higher percentage may indicate newer assets being constructed or purchased and may coincide with higher debt ratios or bonded debt per capita.

Future Accounting Standard Changes

The following Governmental Accounting Standards Board (GASB) Statements have been issued and may have an impact on future City financial statements: [(1)]

GASB Statement No. 67 - *The Financial Reporting for Pension Plans- an Amendment to GASB Statement No. 25*

Summary

The objective of this Statement is to improve financial reporting by state and local governmental pension plans. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency.

This Statement replaces the requirements of Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 50, *Pension Disclosures*, as they relate to pension plans that are

administered through trusts or equivalent arrangements (hereafter jointly referred to as trusts) that meet certain criteria.

The requirements of Statements No. 25 and No. 50 remain applicable to pension plans that are not administered through trusts covered by the scope of this Statement and to defined contribution plans that provide postemployment benefits other than pensions.

This Statement is effective for financial statements for fiscal years beginning after June 15, 2013. Earlier application is encouraged.

How the Changes in This Statement Will Improve Financial Reporting

The requirements of this Statement will improve financial reporting primarily through enhanced note disclosures and schedules of required supplementary information that will be presented by the pension plans that are within its scope. The new information will enhance the decision-usefulness of the financial reports of these pension plans, their value for assessing accountability, and their transparency by providing information about measures of net pension liabilities and explanations of how and why those liabilities changed from year to year. The net pension liability information, including ratios, will offer an up-to-date indication of the extent to which the total pension liability is covered by the fiduciary net position of the pension plan. The comparability of the reported information for similar types of pension plans will be improved by the changes related to the attribution method used to determine the total pension liability. The contribution schedule will provide measures to evaluate decisions related to the assessment of contribution rates in comparison to actuarially determined rates, when such rates are determined. In that circumstance, it also will provide information about whether employers and nonemployer contributing entities, if applicable, are keeping pace with actuarially determined contribution measures. In addition, new information about rates of return on pension plan investments will inform financial report users about the effects of market conditions on the pension plan's assets over time and provide information for users to assess the relative success of the pension plan's investment strategy and the relative contribution that investment earnings provide to the pension plan's ability to pay benefits to plan members when they come due.

Future Accounting Standard Changes - Continued

GASB Statement No. 68 - *The Accounting and Financial Reporting of Pensions- an Amendment of GASB Statement No. 27*

The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency.

This Statement replaces the requirements of Statement No. 27, Accounting for Pensions by State and Local Governmental Employers, as well as the requirements of Statement No. 50, Pension Disclosures, as they relate to pensions that are provided through pension plans administered as trusts or equivalent arrangements (hereafter jointly referred to as trusts) that meet certain criteria. The requirements of Statements 27 and 50 remain applicable for pensions that are not covered by the scope of this Statement.

This Statement is effective for fiscal years beginning after June 15, 2014. Earlier application is encouraged.

How the Changes in This Statement Will Improve Financial Reporting

The requirements of this Statement will improve the decision-usefulness of information in employer and governmental nonemployer contributing entity financial reports and will enhance its value for assessing accountability and interperiod equity by requiring recognition of the entire net pension liability and a more comprehensive measure of pension expense. Decision-usefulness and accountability also will be enhanced through new note disclosures and required supplementary information.

GASB Statement No. 69 - *Government Combinations and Disposals of Government Operations*

Summary

This Statement establishes accounting and financial reporting standards related to government combinations and disposals of government operations. As used in this Statement, the term government combinations include a variety of transactions referred to as mergers, acquisitions, and transfers of operations.

The distinction between a government merger and a government acquisition is based upon whether an exchange of significant consideration is present within the combination transaction. Government mergers include combinations of legally separate entities without the exchange of significant consideration. This Statement requires the use of carrying values to measure the assets and liabilities in a government merger. Conversely, government acquisitions are transactions in which a government acquires another entity, or its operations, in exchange for significant consideration. This Statement requires measurements of assets acquired and liabilities assumed generally to be based upon their acquisition values. This Statement also provides guidance for transfers of operations that do not constitute entire legally separate entities and in which no significant consideration is exchanged. This Statement defines the term operations for purposes of determining the applicability of this Statement and requires the use of carrying values to measure the assets and liabilities in a transfer of operations.

A disposal of a government's operations results in the removal of specific activities of a government. This Statement provides accounting and financial reporting guidance for disposals of government operations that have been transferred or sold.

This Statement requires disclosures to be made about government combinations and disposals of government operations to enable financial statement users to evaluate the nature and financial effects of those transactions.

The requirements of this Statement are effective for government combinations and disposals of government operations occurring in financial reporting periods beginning after December 15, 2013, and should be applied on a prospective basis. Earlier application is encouraged.

How the Changes in This Statement Will Improve Financial Reporting

Until now, governments have accounted for mergers, acquisitions, and transfers of operations by analogizing to accounting and financial reporting guidance intended for the business environment, generally APB Opinion No. 16, Business Combinations. This Statement provides specific accounting and financial reporting guidance for combinations in the governmental environment. This Statement also improves the decision usefulness of financial reporting by requiring that disclosures be made by governments about combination arrangements in which they engage and for disposals of government operations.

GASB Statement No. 70 - *Accounting and Financial Reporting for Nonexchnage Financial Guarantees*

Summary

Some governments extend financial guarantees for the obligations of another government, a not-for-profit organization, a private entity, or individual without directly receiving equal or approximately equal value in exchange (a nonexchange transaction). As a part of this nonexchange financial guarantee, a government commits to indemnify the holder of the obligation if the entity or individual that issued the obligation does not fulfill its payment requirements. Also, some governments issue obligations that are guaranteed by other entities in a nonexchange transaction. The objective of this Statement is to improve accounting and financial reporting by state and local governments that extend and receive nonexchange financial guarantees.

This Statement requires a government that extends a nonexchange financial guarantee to recognize a liability when qualitative factors and historical data, if any, indicate that it is more likely than not that the government will be required to make a payment on the guarantee. The amount of the liability to be recognized should be the discounted present value of the best estimate of the future outflows expected to be incurred as a result of the guarantee. When there is no best estimate but a range of the estimated future outflows can be established, the amount of the liability to be recognized should be the discounted present value of the minimum amount within the range.

This Statement requires a government that has issued an obligation guaranteed in a nonexchange transaction to report the obligation until legally released as an obligor. This Statement also requires a government that is required to repay a guarantor for making a payment on a guaranteed obligation or legally assuming the guaranteed obligation to continue to recognize a liability until legally released as an obligor. When a government is released as an obligor, the government should recognize revenue as a result of being relieved of the obligation. This Statement also provides additional guidance for intra-entity nonexchange financial guarantees involving blended component units.

This Statement specifies the information required to be disclosed by governments that extend nonexchange financial guarantees. In addition, this Statement requires new information to be disclosed by governments that receive nonexchange financial guarantees.

The provisions of this Statement are effective for reporting periods beginning after June 15, 2013. Earlier application is encouraged. Except for disclosures related to cumulative amounts paid or received in relation to a nonexchange financial guarantee, the provisions of this Statement are required to be applied retroactively. Disclosures related to cumulative amounts paid or received in relation to a nonexchange financial guarantee may be applied prospectively.

How the Changes in This Statement Will Improve Financial Reporting

The requirements of this Statement will enhance comparability of financial statements among governments by requiring consistent reporting by those governments that extend nonexchange financial guarantees and by those governments that receive nonexchange financial guarantees. This Statement also will enhance the information disclosed about a government's obligations and risk exposure from extending nonexchange financial guarantees. This Statement also will augment the ability of financial statement users to assess the probability that governments will repay obligation holders by requiring disclosures about obligations that are issued with this type of financial guarantee.

GASB Statement No. 71 - *Pension Transition for Contributions Made Subsequent to the Measure Date - an Amendment of GASB Statement No. 68*

Summary

The objective of this Statement is to address an issue regarding application of the transition provisions of Statement No. 68, Accounting and Financial Reporting for Pensions. The issue relates to amounts associated with contributions, if any, made by a state or local government employer or nonemployer contributing entity to a defined benefit pension plan after the measurement date of the government's beginning net pension liability.

Future Accounting Standard Changes - Continued

Statement No. 68 requires a state or local government employer (or nonemployer contributing entity in a special funding situation) to recognize a net pension liability measured as of a date (the measurement date) no earlier than the end of its prior fiscal year. If a state or local government employer or nonemployer contributing entity makes a contribution to a defined benefit pension plan between the measurement date of the reported net pension liability and the end of the government's reporting period, Statement No. 68 requires that the government recognize its contribution as a deferred outflow of resources. In addition, Statement No. 68 requires recognition of deferred outflows of resources and deferred inflows of resources for changes in the net pension liability of a state or local government employer or nonemployer contributing entity that arise from other types of events. At transition to Statement No. 68, if it is not practical for an employer or nonemployer contributing entity to determine the amounts of all deferred outflows of resources and deferred inflows of resources related to pensions, paragraph 137 of Statement No. 68 required that beginning balances for deferred outflows of resources and deferred inflows of resources not be reported.

Consequently, if it is not practical to determine the amounts of all deferred outflows of resources and deferred inflows of resources related to pensions, contributions made after the measurement date of the beginning net pension liability could not have been reported as deferred outflows of resources at transition. This could have resulted in a significant understatement of an employer or nonemployer contributing entity's beginning net position and expense in the initial period of implementation.

This Statement amends paragraph 137 of Statement No. 68 to require that, at transition, a government recognize a beginning deferred outflow of resources for its pension contributions, if any, made subsequent to the measurement date of the beginning net pension liability. Statement No. 68, as amended, continues to require that beginning balances for other deferred outflows of resources and deferred inflows of resources related to pensions be reported at transition only if it is practical to determine all such amounts.

The provisions of this Statement are required to be applied simultaneously with the provisions of Statement No. 68.

How the Changes in This Statement Will Improve Financial Reporting

The requirements of this Statement will eliminate the source of a potential significant understatement of restated beginning net position and expense in the first year of implementation of Statement No. 68 in the accrual-basis financial statements of employers and nonemployer contributing entities. This benefit will be achieved without the imposition of significant additional costs.

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

Our audit would not necessarily disclose all weaknesses in the system because it was based on selected tests of the accounting records and related data. The comments and recommendations in the report are purely constructive in nature, and should be read in this context.

If you have any questions or wish to discuss any of the items contained in this letter, please feel free to contact us at your convenience. We wish to thank you for the continued opportunity to be of service and for the courtesy and cooperation extended to us by your staff.

Abdo Eick & Meyers, LLP

ABDO, EICK & MEYERS, LLP
Minneapolis, Minnesota
March 27, 2014

People + Process. Going Beyond the Numbers