



CITY OF WOODLAND
WOODLAND, MINNESOTA

MANAGEMENT LETTER

YEAR ENDED
DECEMBER 31, 2010

 **ABDO
EICK &
MEYERS** LLP
Certified Public Accountants & Consultants

5201 Eden Avenue
Suite 370
Edina, MN 55436

Management, Honorable Mayor and Council
City of Woodland, Minnesota

We have audited each major fund of the governmental and proprietary funds of the City of Woodland, Minnesota (the City), for year ended December 31, 2010. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing 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 October 15, 2010. In our report, our opinion was modified because the City prepared its financial statements on the regulatory basis, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. 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

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 the regulatory basis of accounting prescribed by the Minnesota Office of the State Auditor. 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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all such deficiencies have been identified. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A deficiency in internal control over financial reporting 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 combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the City's financial statements will not be prevented, or detected and corrected on a timely basis. We did not identify any deficiencies in internal control that we consider to be material weaknesses.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider finding 2010-1 to be significant deficiency in internal control over financial reporting.



2010-1 Preparation of Financial Statements (Finding Since 2007)

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. 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 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. As in prior years, we have instructed management to review a draft of the auditor prepared financials in detail for accuracy; we have answered any questions that management 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.

Recommendation: Under these circumstances, the most effective controls lie in management's knowledge of the City's financial operations. It is the responsibility of management and those charged with governance to make the decision to accept the degree of risk associated with this condition because of cost or other considerations. Regarding the specific situations listed above, we would offer the following recommendations: 1) Utilize a disclosure checklist to ensure that all required disclosures are present and agree to work papers, and 2) Agree your accounting information from your financial software to the amounts 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.

Compliance and Other Matters

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. However, the objective of our tests was not to provide an opinion on compliance with such provisions. We noted no instances of noncompliance with Minnesota statutes.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you.

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. No new accounting policies were adopted and the application of existing policies was not changed during the year. We noted no transactions entered into by the governmental unit 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 sensitive estimates affecting the financial statements were depreciation on capital assets.

Management's estimate of depreciation is based on estimated useful lives of the assets. We evaluated the key factors and assumptions used to develop depreciation 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. Management has corrected all such misstatements. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to each opinion unit's financial statements taken as a whole.

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 representation letter dated February 23, 2011.

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.

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, 2010.

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 fund balance increased \$16,670 to \$227,906 at December 31, 2010. The total fund balance represents 73 percent of the 2011 budgeted expenditures and transfers out. We recommend that the fund balance be maintained at a level sufficient to fund operations until the major revenue sources are received in June. We feel a reserve of approximately 50 percent of planned expenditures and transfers out is adequate to meet working capital and small emergency needs.

Minnesota cities must maintain substantial amounts of fund balance in order to meet their liquidity and working capital needs as an operating entity. That is because a substantial portion of your revenue sources (taxes and intergovernmental revenues) are received in the last two months of each six-month cycle.

The Office of the State Auditor (the OSA) has issued a Statement of Position relating to fund balance stating “a local government should identify fund balance separately between reserved and unreserved fund balance. The local government may assign and report some or all of the fund balance as designated and undesignated.” We recommend local governments adopt a formal policy on the level of unreserved fund balance that should be maintained in the general and special revenue funds. This helps address citizen concerns as to the use of fund balance and tax levels.

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

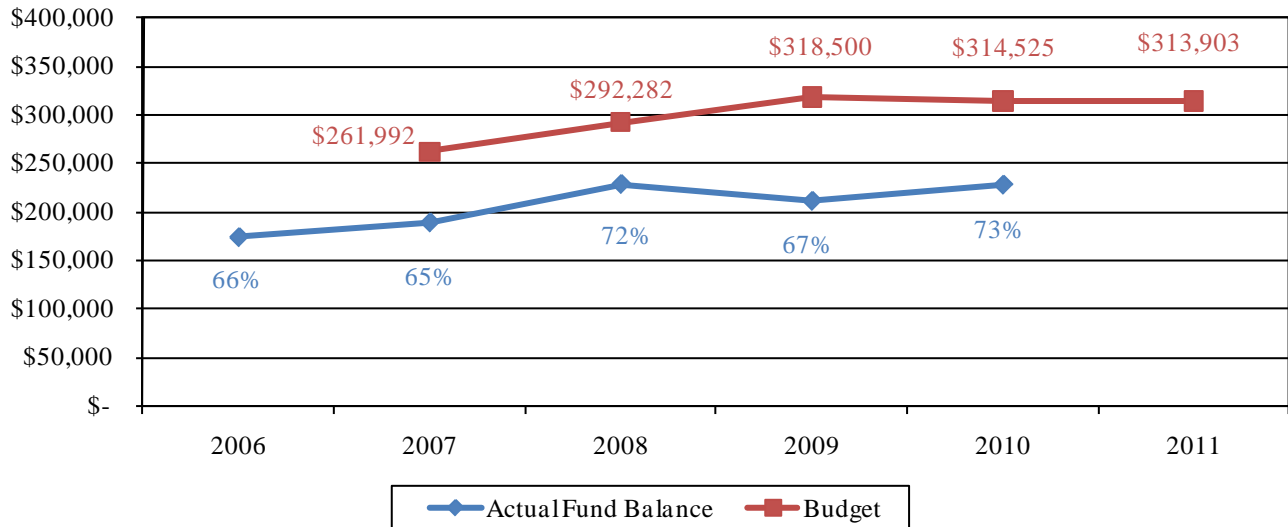
<u>Year</u>	<u>Fund Balance December 31</u>	<u>Budget Year</u>	<u>General Fund Budget</u>	<u>Percent of Fund Balance to Budget</u>
2006	\$ 173,887	2007	\$ 261,992	66 %
2007	189,050	2008	292,282	65
2008	228,624	2009	318,500	72
2009	211,236	2010	314,525	67
2010	227,906	2011	313,903	73

We have compiled peer group average fund balance information from the Regulatory Cities we audit. In 2008 and 2009, the average General fund balance as a percentage of expenditures was 70 percent and 83 percent, respectively. Based on comparison to the peer groups, the City’s General fund balance is lower than average.

The City has a Street Improvement capital project fund with an ending fund balance of \$30,844. If this is factored into the general fund balance, the City is in line with the peer group average mentioned above.



Fund Balances as a Percent of Next Year's Budget



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

Purposes and Benefits

- Disbursements 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 General fund disbursements.
- The City is vulnerable to legislative actions at the State and Federal level. The State imposed reductions of market value credit aid and local government aid for some cities at the end of 2010 and more reductions are anticipated for 2011. Levy limits have also been implemented for municipalities in past legislative sessions. An adequate fund balance will provide a temporary buffer against those aid adjustments and levy limits.
- Disbursements not anticipated at the time the annual budget was adopted may need immediate Council action. These would include capital outlay replacement, lawsuits and other items. An adequate fund balance will provide the financing needed for such disbursements.
- A strong fund balance will assist the City in maintaining, improving or obtaining a bond rating. The result will be better interest rates in future bond sales.



The 2010 operations are summarized as follows:

	Final Budgeted Amounts	Actual Amounts	Variance with Final Budget
Receipts	\$ 314,525	\$ 334,554	\$ 20,029
Disbursements	<u>274,525</u>	<u>277,884</u>	<u>(3,359)</u>
Excess of receipts over disbursements	40,000	56,670	16,670
Transfers out	<u>(40,000)</u>	<u>(40,000)</u>	<u>-</u>
Net change in fund balances	-	16,670	16,670
Fund balances, January 1,	<u>211,236</u>	<u>211,236</u>	<u>-</u>
Fund balances, December 31,	<u>\$ 211,236</u>	<u>\$ 227,906</u>	<u>\$ 16,670</u>

Some of the line items with significant variances are highlighted below:

- The two largest receipt variances were in licenses and permits and fines and forfeitures which were over budget by \$7,411 and \$7,026, respectively.
- Significant expenditure variances included legal fees \$5,086 under budget and snow and ice removal \$5,744 over budget.

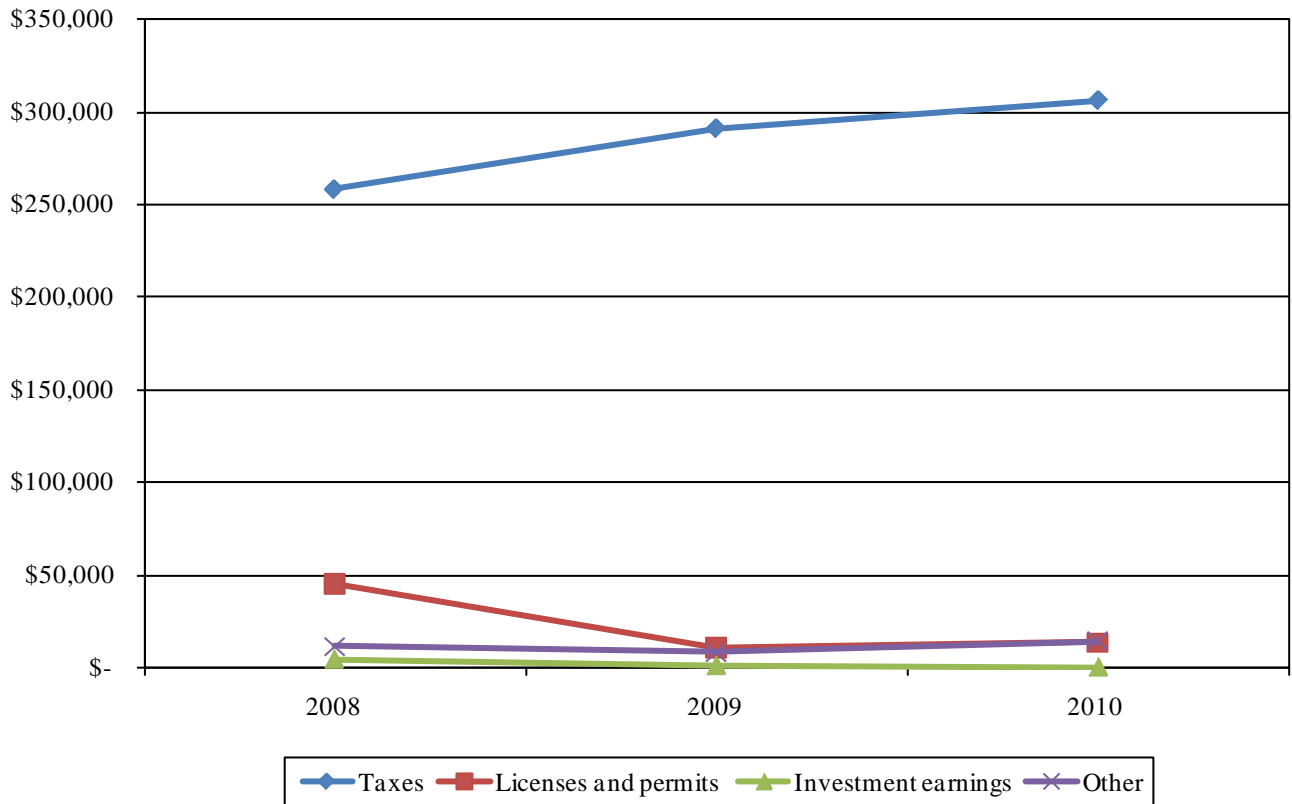


A comparison between 2010, 2009 and 2008 receipts is presented below:

Source	2008	2009	2010	Percent of	
				Total	Per Capita
Taxes	\$ 258,198	\$ 291,081	\$ 306,216	91.5 %	\$ 609
Licenses and permits	45,333	10,739	13,661	4.1	27
Intergovernmental	5,107	1,578	1,618	0.5	3
Charges for services	2,050	3,375	2,750	0.8	5
Fines and forfeitures	1,995	1,490	8,026	2.4	16
Investment earnings	4,622	1,064	252	0.1	1
Miscellaneous	2,161	1,842	2,031	0.6	4
Total receipts	\$ 319,466	\$ 311,169	\$ 334,554	100.0 %	\$ 665

A graphical presentation of the last three years receipts follows:

Receipts



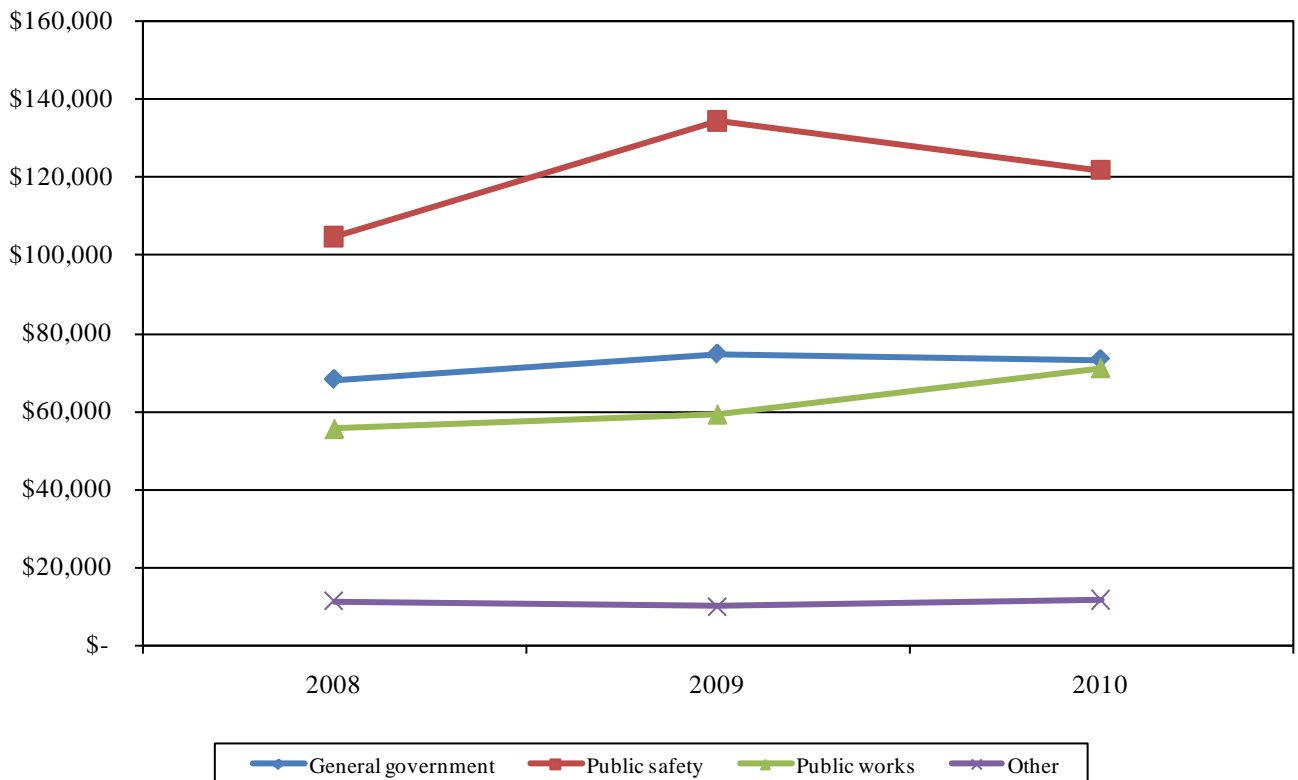


A comparison between 2010, 2009 and 2008 disbursements is presented below:

Program	2008	2009	2010	Percent of Total	Per Capita
General government	\$ 68,158	\$ 74,693	\$ 73,283	23.1 %	\$ 146
Public safety	104,776	134,516	121,878	38.3	242
Public works	55,683	59,335	71,047	22.3	141
Miscellaneous	11,275	10,013	11,676	3.7	23
Transfers out	40,000	50,000	40,000	12.6	80
Total disbursements	\$ 279,892	\$ 328,557	\$ 317,884	100.0 %	\$ 632

A graphical presentation of the last three years disbursements follows:

Disbursements





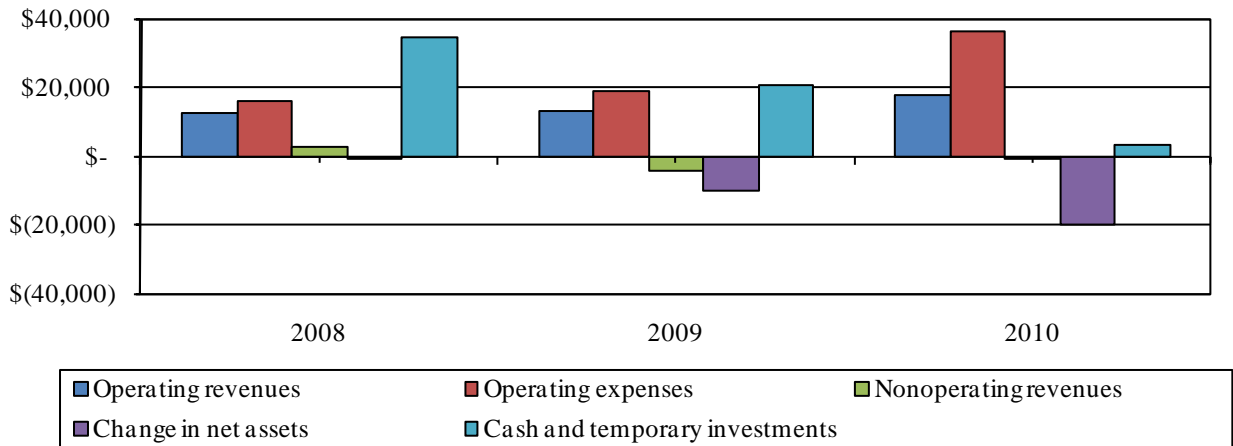
Enterprise Funds

The City operates two enterprise funds. Enterprise funds are used to account for those operations that are financed and operated in a manner similar to private business or where the Council has decided that the determination of revenues earned, costs incurred and/or net income is necessary for management accountability. A summary of their operations and cash position follows:

Water Fund

	2008		2009		2010	
	Total	Percent	Total	Percent	Total	Percent
Operating revenues	\$ 12,973	100.0 %	\$ 13,334	100.0 %	\$ 17,671	100.0 %
Operating expenses	16,346	126.0	19,172	143.8	36,625	207.3
Operating loss	(3,373)	(26.0)	(5,838)	(43.8)	(18,954)	(107.3)
Nonoperating revenues (expenses)	2,630	20.3	(4,309)	(32.3)	(902)	(5.1)
Transfers in	-	-	-	-	54,230	306.9
Change in net assets	\$ (743)	(5.7) %	\$ (10,147)	(76.1) %	\$ 34,374	194.5 %
Cash and temporary investments	\$ 34,957		\$ 20,618		\$ 3,476	
Bonds payable	\$ 125,000		\$ 112,500		\$ 100,000	

Water Fund Operations Summary



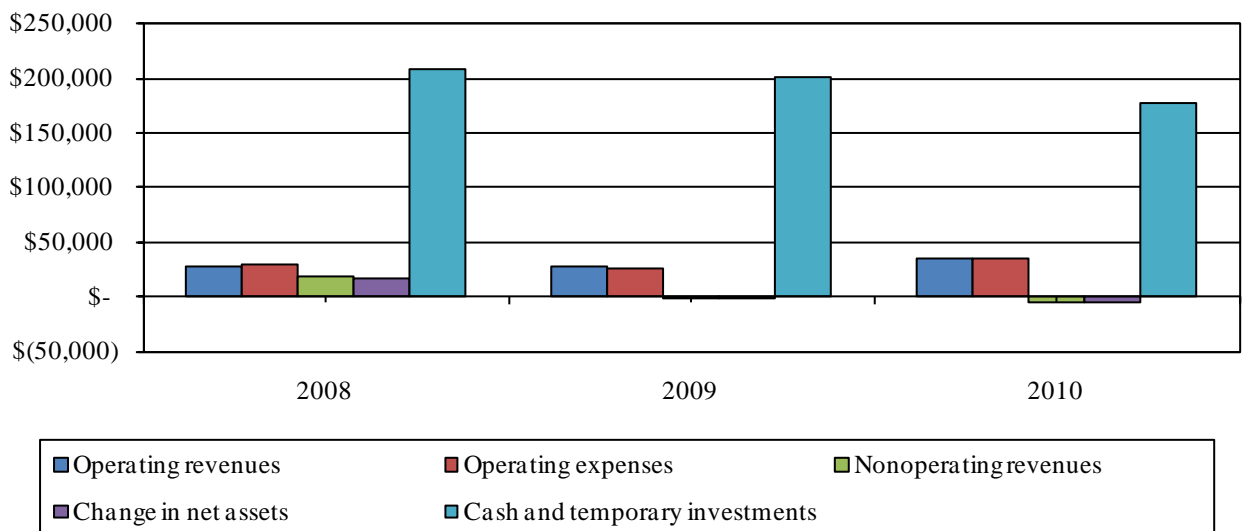
The Council had a rate study/cash flow projection completed in 2010. As a result, Council approved a resolution to allocate 75 percent of assessment revenue to the Water fund, as opposed to 25 percent in the past. It is the Council's expectation that this change in allocation, along with slight changes in utility fees, will help ensure that the Water fund is able to cover operating expenses, debt service payments, and future repairs. We recommend the City review rates annually and evaluate future cash flows to maintain appropriate resources.



Sewer Fund

	2008		2009		2010	
	Total	Percent	Total	Percent	Total	Percent
Operating revenues	\$ 27,149	100.0 %	\$ 27,860	100.0 %	\$ 34,687	100.0 %
Operating expenses	28,785	106.0	26,266	94.3	34,358	99.1
Operating income (loss)	(1,636)	(6.0)	1,594	5.7	329	0.9
Nonoperating revenues (expenses)	18,632	68.6	(1,736)	(6.2)	(5,870)	(16.9)
Transfers out	-	-	-	-	(54,230)	(156.3)
Change in net assets	<u>\$ 16,996</u>	<u>62.6 %</u>	<u>\$ (142)</u>	<u>(0.5) %</u>	<u>\$ (59,771)</u>	<u>(172.3) %</u>
Cash and temporary investments	<u>\$ 207,430</u>		<u>\$ 200,411</u>		<u>\$ 178,159</u>	
Bonds payable	<u>\$ 344,346</u>		<u>\$ 313,223</u>		<u>\$ 278,142</u>	

Sewer Fund Operations Summary



The Sewer fund continues to have a good cash balance relative to operations. A rate study/cash flow projection was completed in 2010 and Council approved a resolution to allocate 25 percent of assessment revenue to the Sewer fund, as opposed to 75 percent in the past. It is the Council's expectation that this change in allocation will help build adequate cash and reserve amounts in the Water fund as well as allow the Sewer fund to continue to cover operating expenses, debt service payments, and future repairs. We recommend the City review rates annually and evaluate future cash flows to maintain appropriate resources.



Future Statute and Accounting Standard Changes

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

GASB Statement No. 54 – *Fund Balance*

This statement was issued in March of 2009 and is effective for periods beginning after June 15, 2010.

This new standard is intended to improve the usefulness of information provided to financial report users about fund balance by providing clearer, more structured fund balance classifications, and clarifying the definitions of existing governmental fund types.

GASB No. 54 distinguishes fund balance between amounts that are considered non-spendable, such as fund balance associated with inventories, and other amounts that are classified based on the relative strength of the constraints that control the purposes for which specific amounts can be spent. The following classifications and definitions will be used:

- *Restricted* - amounts constrained by external parties, constitutional provision, or enabling legislation
- *Committed* - amounts constrained by a government using its highest level of decision-making authority
- *Assigned* - amounts a government intends to use for a particular purpose
- *Unassigned* - amounts that are not constrained at all will be reported in the general fund.

In addition to the classifications of fund balance, the standard clarified the definitions of individual governmental fund types, for example, special revenue funds, debt service funds, and capital project funds.

GASB Statement No. 59 – *Financial Instruments Omnibus*

Summary

The objective of this Statement is to update and improve existing standards regarding financial reporting and disclosure requirements of certain financial instruments and external investment pools for which significant issues have been identified in practice. This Statement provides for the following amendments:

- Statement 31 is clarified to indicate that a 2a7-like pool, as described in Statement 31, is an external investment pool that operates in conformity with the Securities and Exchange Commission's (SEC) Rule 2a7 as promulgated under the Investment Company Act of 1940, as amended.
- Statement No. 40, Deposit and Investment Risk Disclosures, is amended to indicate that interest rate risk information should be disclosed only for debt investment pools—such as bond mutual funds and external bond investment pools—that do not meet the requirements to be reported as a 2a7-like pool.

The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2010. Earlier application is encouraged.

How the Changes in This Statement Will Improve Financial Reporting

The requirements of this Statement will improve financial reporting by providing more complete information, by improving consistency of measurements, and by providing clarifications of existing standards. Emphasizing the applicability of SEC requirements to 2a7-like external investment pools provides practitioners with improved guidance. Finally, limiting interest rate risk disclosures for investments in mutual funds, external investment pools, and other pooled investments to debt investment pools provides better guidance regarding the applicability of interest rate risk disclosures.



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

Our audit does 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 opportunity to be of service and for the courtesy and cooperation extended to us by your staff.

February 23, 2011
Minneapolis, Minnesota

ABDO, EICK & MEYERS, LLP
Certified Public Accountants