

# STATE OF MINNESOTA

## Office of the State Auditor



**Patricia Anderson**  
**State Auditor**

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**SPIRIT MOUNTAIN RECREATION  
AREA AUTHORITY  
(COMPONENT UNIT OF THE CITY OF DULUTH)  
DULUTH, MINNESOTA**

**FOR THE YEARS ENDED APRIL 30, 2006 AND 2005**

## **Description of the Office of the State Auditor**

The Office of the State Auditor serves as a watchdog for Minnesota taxpayers by helping to ensure financial integrity, accountability, and cost-effectiveness in local governments throughout the state.

Through financial, compliance, and special audits, the State Auditor oversees and ensures that local government funds are used for the purposes intended by law and that local governments hold themselves to the highest standards of financial accountability.

The State Auditor performs approximately 250 financial and compliance audits per year and has oversight responsibilities for over 4,300 local units of government throughout the state. The office currently maintains five divisions:

**Audit Practice** - conducts financial and legal compliance audits for local governments;

**Government Information** - collects and analyzes financial information for cities, towns, counties, and special districts;

**Legal/Special Investigations** - provides legal analysis and counsel to the Office and responds to outside inquiries about Minnesota local government law; as well as investigates allegations of misfeasance, malfeasance, and nonfeasance in local government;

**Pension** - monitors investment, financial, and actuarial reporting for over 700 public pension funds; and

**Tax Increment Financing, Investment and Finance** - promotes compliance and accountability in local governments' use of tax increment financing through financial and compliance audits.

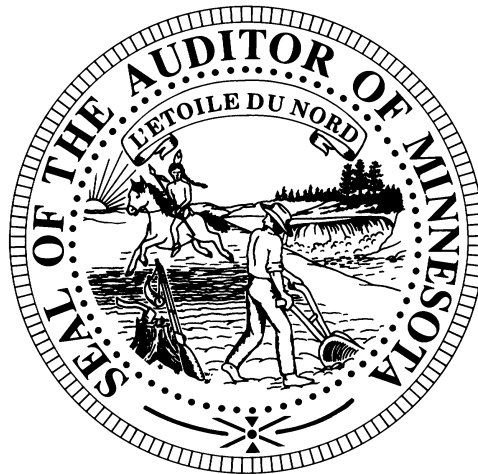
The State Auditor serves on the State Executive Council, State Board of Investment, Land Exchange Board, Public Employee's Retirement Association Board, Minnesota Housing Finance Agency, and the Rural Finance Authority Board.

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**SPIRIT MOUNTAIN RECREATION  
AREA AUTHORITY  
(COMPONENT UNIT OF THE CITY OF DULUTH)  
DULUTH, MINNESOTA**

**For the Years Ended April 30, 2006 and 2005**



**Audit Practice Division  
Office of the State Auditor  
State of Minnesota**

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**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

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**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

ORGANIZATION  
APRIL 30, 2006

|                        | <u>Term Ending</u> |
|------------------------|--------------------|
| Directors              |                    |
| C. J. Bird             | June 30, 2008      |
| Ken Buehler            | June 30, 2006      |
| John Goldfine          | June 30, 2006      |
| Alan Johnson           | June 30, 2008      |
| Eric Kaiser            | June 30, 2006      |
| Nancy Nelson           | June 30, 2006      |
| Pauline Olsen          | June 30, 2006      |
| <br>Executive Director |                    |
| Renee Mattson          |                    |
| <br>Officers           |                    |
| Chair                  |                    |
| Pauline Olsen          |                    |
| Vice Chair             |                    |
| Ken Buehler            |                    |
| Secretary              |                    |
| Nancy Nelson           |                    |

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PATRICIA ANDERSON  
STATE AUDITOR

# STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

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## INDEPENDENT AUDITOR'S REPORT

Mayor and City Council  
City of Duluth

Board of Directors  
Spirit Mountain Recreation Area Authority

We have audited the accompanying basic financial statements of the Spirit Mountain Recreation Area Authority, a component unit of the City of Duluth, as of and for the years ended April 30, 2006 and 2005. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Spirit Mountain Recreation Area Authority as of April 30, 2006 and 2005, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying financial information listed as supplementary information in the table of contents is presented for additional analysis and is not a required part of the basic financial statements of the Spirit Mountain Recreation Area Authority. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented in all material respects in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated July 31, 2006, on our consideration of the Spirit Mountain Recreation Area Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

*/s/Pat Anderson*

PATRICIA ANDERSON  
STATE AUDITOR

*/s/Greg Hierlinger*

GREG HIERLINGER, CPA  
DEPUTY STATE AUDITOR

End of Fieldwork: July 31, 2006

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

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**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
APRIL 30, 2006  
(Unaudited)**

This section presents management's analysis of the Spirit Mounting Recreation Area Authority's financial condition and activities for the fiscal year ended April 30, 2006. This information should be read in conjunction with the financial statements.

**FINANCIAL HIGHLIGHTS**

- Total net assets increased \$340,710, or 10 percent, compared to fiscal year 2005. The increase was due to total assets increasing 2 percent, while total liabilities decreased 8 percent.
- Operating income increased \$82,377, or 99 percent, compared to fiscal year 2005. The considerable increase was due primarily to an increase in sales, charges for services, and miscellaneous operating revenues.
- The City of Duluth issued a \$1.647 million Gross Revenue Recreational Facility Bond in 2003 to refinance existing Authority debt. The bond is not a general obligation of the City and is payable from the Authority's gross revenues. The City pledged tourism taxes in the amount of \$225,000 per year, effective January 1, 2004, as part of the gross revenues of the project. The tourism tax pledge by the City will allow the Authority to invest a minimum of \$225,000 in capital improvements on an annual basis over the life of the bond.

**OVERVIEW OF ANNUAL FINANCIAL REPORT**

The Management's Discussion and Analysis (MD&A) serves as an introduction to the financial statements. The MD&A represents management's examination and analysis of the Authority's financial condition and performance. Summary financial statement data; key financial and operational indicators used in the Authority's strategic plan, budget, and bond resolutions; and other management tools were used for this analysis.

The financial statements report information about the Authority using full accrual accounting methods as utilized by similar business activities in the private sector.

The financial statements include a statement of net assets; a statement of revenues, expenses, and changes in net assets; a statement of cash flows; and notes to the financial statements. The statement of net assets presents the financial position of the Authority on a full accrual historical

cost basis. While the statement of net assets provides information about the nature and amount of resources and obligations at year-end, the statement of revenues, expenses, and changes in net assets presents the results of the business activities over the course of the fiscal year and information as to how the net assets changed during the year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. This statement also provides certain information about the Authority's recovery of its costs.

The statement of cash flows present changes in cash and cash equivalents resulting from operational, financing, and investing activities. This statement presents cash receipts and cash disbursement information without consideration of the earnings event, when an obligation arises, or depreciation of capital assets.

The notes to the financial statements provide required disclosures and other information essential to a full understanding of material data provided in the statements. The notes present information about the Authority's accounting policies, significant account balances and activities, material risks, obligations, commitments, contingencies, and subsequent events, if any.

The financial statements were prepared by the Authority's staff from the detailed books and records of the Authority. The financial statements were audited and adjusted, if material, during the independent external audit process.

## **SUMMARY OF ORGANIZATION AND BUSINESS**

On May 18, 1973, the Minnesota State Legislature enacted the Laws, 1973, Chapter 327 (the "Act") creating the Spirit Mountain Recreation Area Authority. The mission of the Authority as defined in section one of the Act is as follows: The purpose of this Act is to facilitate the development of a land area with the following objectives: (1) the development of wide-range recreational facilities available to both local residents and tourists, (2) the aiding of the economy of northeastern Minnesota by encouraging private enterprise efforts in conjunction with the recreational facilities, and (3) the preservation of the environment in the area by a timely and intelligent plan of development. The Authority was created to have the power and duty to manage the property made up of the area. The State Legislature itself conferred upon the Authority the power and responsibility for the operation and management of the area. The Mayor of Duluth appoints seven community members to serve on the Board of Directors that oversees the Authority.

The main form of recreation provided to both local residents and visitors is skiing; alpine, nordic, and snowboarding. The Authority also hosts the world's largest Snocross race. Summertime activities include special events, mountain bike races, banquets, meetings, camping, and a Supper Club.

The Authority does not have taxing power. Operations are funded from customer revenues. Customer revenues, together with City tourism taxes, fund the acquisition and construction of capital assets.

## FINANCIAL ANALYSIS

The following comparative condensed financial statements and other selected information serve as the key financial data and indicators for management, monitoring, and planning. Comments regarding budget-to-actual variances and year-to-year variances are included in each section by the name of the statement or account.

### Condensed Statement of Net Assets

|                          | Fiscal Year<br>2006 | Fiscal Year<br>2005 | Change from 2005 to 2006 |                | Fiscal Year<br>2004 |
|--------------------------|---------------------|---------------------|--------------------------|----------------|---------------------|
|                          |                     |                     | Dollar                   | Percent<br>(%) |                     |
| Current and other assets | \$ 1,279,463        | \$ 1,166,708        | \$ 112,755               | 10             | \$ 999,259          |
| Capital assets           | 4,822,217           | 4,787,844           | 34,373                   | 1              | 4,915,661           |
| <b>Total Assets</b>      | <b>\$ 6,101,680</b> | <b>\$ 5,954,552</b> | <b>\$ 147,128</b>        | <b>2</b>       | <b>\$ 5,914,920</b> |
| Current liabilities      | \$ 766,216          | \$ 788,947          | \$ (22,731)              | (3)            | \$ 870,627          |
| Long-term liabilities    | 1,590,139           | 1,760,990           | (170,851)                | (10)           | 1,851,878           |
| <b>Total Liabilities</b> | <b>\$ 2,356,355</b> | <b>\$ 2,549,937</b> | <b>\$ (193,582)</b>      | <b>(8)</b>     | <b>\$ 2,722,505</b> |
| Net Assets               |                     |                     |                          |                |                     |
| Invested                 | \$ 3,107,869        | \$ 2,963,292        | \$ 144,577               | 5              | \$ 2,774,302        |
| Restricted               | 330,714             | 279,480             | 51,234                   | 18             | 250,000             |
| Unrestricted             | 306,742             | 161,843             | 144,899                  | 90             | 168,113             |
| <b>Total Net Assets</b>  | <b>\$ 3,745,325</b> | <b>\$ 3,404,615</b> | <b>\$ 340,710</b>        | <b>10</b>      | <b>\$ 3,192,415</b> |

As can be seen from the table, net assets increased \$340,710 to \$3,745,325 in 2006; up from \$3,404,615 in 2005. Unrestricted net assets increased \$144,899, or 90 percent, from 2005. The increase in net assets is due primarily to the increase in current assets and the decrease in total liabilities.

### Condensed Statements of Revenues, Expenses, and Changes in Net Assets (Comparative Amounts)

|                           | Actual              |                     | Change            |                | Fiscal Year<br>2004 |
|---------------------------|---------------------|---------------------|-------------------|----------------|---------------------|
|                           | Fiscal Year<br>2006 | Fiscal Year<br>2005 | Dollar            | Percent<br>(%) |                     |
| Operating revenues        | \$ 3,925,609        | \$ 3,494,563        | \$ 431,046        | 12             | \$ 3,317,737        |
| Nonoperating revenues     | 246,181             | 231,626             | 14,555            | 6              | 10,294              |
| <b>Total Revenues</b>     | <b>\$ 4,171,790</b> | <b>\$ 3,726,189</b> | <b>\$ 445,601</b> | <b>12</b>      | <b>\$ 3,328,031</b> |
| Operating expenses        | \$ 3,343,801        | \$ 2,955,350        | \$ 388,451        | 13             | \$ 2,854,678        |
| Nonoperating expenses     | 70,943              | 102,521             | (31,578)          | (31)           | 132,205             |
| Depreciation/amortization | 416,336             | 456,118             | (39,782)          | (9)            | 452,707             |
| <b>Total Expenses</b>     | <b>\$ 3,831,080</b> | <b>\$ 3,513,989</b> | <b>\$ 317,091</b> | <b>9</b>       | <b>\$ 3,439,590</b> |

(Unaudited)

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|                       | Actual              |                     | Change     |                | Fiscal Year<br>2004 |
|-----------------------|---------------------|---------------------|------------|----------------|---------------------|
|                       | Fiscal Year<br>2006 | Fiscal Year<br>2005 | Dollar     | Percent<br>(%) |                     |
| Changes in Net Assets | \$ 340,710          | \$ 212,200          | \$ 128,510 | 61             | \$ (111,559)        |
| Beginning Net Assets  | 3,404,615           | 3,192,415           | 212,200    | 7              | 3,303,974           |
| Ending Net Assets     | \$ 3,745,325        | \$ 3,404,615        | \$ 340,710 | 10             | \$ 3,192,415        |

**Condensed Statements of Revenues, Expenses, and Changes in Net Assets  
(2006 Budget and Actual)**

|                           | Actual       | Budget       | Budget<br>to Actual<br>Variance | Budget<br>Percent<br>(%)<br>Variance |
|---------------------------|--------------|--------------|---------------------------------|--------------------------------------|
| Operating revenues        | \$ 3,925,609 | \$ 3,549,286 | \$ 376,323                      | 11                                   |
| Nonoperating revenues     | 246,181      | 230,440      | 15,741                          | 7                                    |
| Total Revenues            | \$ 4,171,790 | \$ 3,779,726 | \$ 392,064                      | 10                                   |
| Operating expenses        | \$ 3,343,801 | \$ 3,007,692 | \$ 336,109                      | 11                                   |
| Nonoperating expenses     | 70,943       | 82,410       | (11,467)                        | (14)                                 |
| Depreciation/amortization | 416,336      | 440,982      | (24,646)                        | (6)                                  |
| Total Expenses            | \$ 3,831,080 | \$ 3,531,084 | \$ 299,996                      | 8                                    |
| Changes in Net Assets     | \$ 340,710   | \$ 248,642   | \$ 92,068                       | 37                                   |
| Beginning Net Assets      | 3,404,615    | 3,404,615    | -                               | -                                    |
| Ending Net Assets         | \$ 3,745,325 | \$ 3,653,257 | \$ 92,068                       | 3                                    |

## Revenues

The Authority earns operating revenues in both winter and summer. Operating revenues increased to \$3.926 million in 2006, up \$431,046 from 2005. Nonoperating revenues increased six percent in 2006, up \$14,555 over 2005.

## Expenses

The Authority's operating expenses increased 13 percent over 2005, due primarily to the increase in personnel costs as well as gas and utility costs. Nonoperating expenses decreased 31 percent from 2005 due primarily to a 12 percent decrease in interest expense.

## Budgetary Highlights

The Authority creates an annual operating budget, which includes proposed expenses and the means of financing them. Once management and the Board of Directors approve the budget, it is presented to the Duluth City Council for final approval. The Authority's operating budget remains in effect the entire year and is not revised. Management and the Board of Directors are presented detailed monthly financial statements. However, they are not reported on nor shown in the financial statement section of this report.

Operating revenues exceeded budgeted revenues by \$96,493. The additional revenue was due to the strength of performance in season pass sales, daily ticket sales, strong numbers in the rental department, enhanced food and beverage operations, and the campground.

Operating expenses exceeded budgeted operating expenses by 11 percent, due primarily to personnel costs. Nonoperating expenses were 14 percent below budget. The decrease is due primarily to a reduction in interest expense.

## CAPITAL ASSETS AND DEBT ADMINISTRATION

### Capital Assets

|                               | Fiscal Year<br>2006 | Fiscal Year<br>2005 | Change       |                |
|-------------------------------|---------------------|---------------------|--------------|----------------|
|                               |                     |                     | Dollar       | Percent<br>(%) |
| Land                          | \$ 2,429,118        | \$ 2,429,118        | \$ -         | -              |
| Equipment                     | 6,202,926           | 6,744,963           | (542,037)    | (8)            |
| Plant equipment               | 193,874             | 153,791             | 40,083       | 26             |
| Building and improvements     | 3,574,120           | 3,465,395           | 108,725      | 3              |
| Furniture and fixtures        | 194,928             | 197,013             | (2,085)      | (1)            |
| Other capital assets          | 351,861             | 378,298             | (26,437)     | (7)            |
| Work in progress              | 117,607             | 100,746             | 16,861       | 17             |
| Subtotal                      | \$ 13,064,434       | \$ 13,469,324       | \$ (404,890) | (3)            |
| Less: accumulated depreciated | (8,242,217)         | (8,681,480)         | 439,263      | 5              |
| Net Property and Equipment    | \$ 4,822,217        | \$ 4,787,844        | \$ 34,373    | 1              |

By the end of fiscal year 2006, the Authority had invested \$13.064 million in capital assets. The increase of \$34,373 in net property and equipment is due primarily to investments made to building and improvements.

The Authority's ongoing capital plan improvements include: continual upgrades to the snowmaking system, improvements within the chalet to better serve summer meeting and banquet business, remodeling of the Moosehead Saloon for use in the summer months as a Supper Club, and continued upgrades to the computer sales system.

## Debt Administration

|                                 | Fiscal Year<br>2006 | Fiscal Year<br>2005 | Change              |                |
|---------------------------------|---------------------|---------------------|---------------------|----------------|
|                                 |                     |                     | Dollar              | Percent<br>(%) |
| Gas lease                       | \$ 74,614           | \$ 97,046           | \$ (22,432)         | (23)           |
| Groomer lease                   | 305,116             | 213,083             | 92,033              | 43             |
| Rental equipment lease          | -                   | 61,848              | (61,848)            | -              |
| Lease/leaseback (revenue bonds) | 1,334,618           | 1,479,901           | (145,283)           | (10)           |
| Total Debt                      | <u>\$ 1,714,348</u> | <u>\$ 1,851,878</u> | <u>\$ (137,530)</u> | (7)            |

At the end of fiscal year 2006, the Authority's outstanding debt decreased \$137,530 to \$1.714 million, down from \$1.852 million at the end of fiscal year 2005. The decrease in outstanding debt is due primarily to the payoff of the rental equipment lease.

## ECONOMIC AND OTHER FACTORS

The Authority considers many factors when setting the fiscal year 2006 budget, rates, and services. We continue to aggressively target the Twin Cities market for both season pass holders and day skiers. In 2006, we partnered with Welch Village Ski Area to offer a joint season pass, an initiative that was both innovative and unmatched in the Midwest. Out-of-area skiers provide a benefit to Spirit Mountain as well as the Duluth area hospitality industry, as they spend nights in hotels, dine in restaurants, shop, visit attractions, and purchase other services benefiting the local economy. It is imperative we continue to set rates that enable us to be competitive in our region and provide affordable recreation to local winter enthusiasts. The Authority's Board of Directors made the decision to retain the lower price structure enacted for the 2004-2005 ski season to continue to keep Spirit Mountain affordable and competitive in the marketplace. We added new food and beverage outlets to provide guests with more choices and easier access, additions that proved successful in increased revenue. We continue to actively promote and sell Spirit Mountain as a year-round venue, partnering with other entities to bring activities and special events to the facility. Our banquet and meeting business continues to grow through our assertive sales efforts. The campground continues to flourish with another season of record revenues.

## FINANCIAL CONTACT

This financial report is designed to provide our customers and creditors with a general overview of the Authority's finances and to demonstrate the Authority's accountability for the money it receives. If you have any questions about this report, or need additional financial information, contact the Finance Department, Spirit Mountain Recreation Area Authority, 9500 Spirit Mountain Place, Duluth, Minnesota 55810.

## **BASIC FINANCIAL STATEMENTS**

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**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

**EXHIBIT A**

**COMPARATIVE STATEMENT OF NET ASSETS  
APRIL 30, 2006 AND 2005**

|  | <b>2006</b>         | <b>2005</b>         |
|--|---------------------|---------------------|
| <b>Assets</b>  |                     |                     |
| <b>Current assets</b>  |                     |                     |
| Cash and cash equivalents  | \$ 833,480          | \$ 722,629          |
| Accounts receivable  | 18,757              | 63,408              |
| Inventory  | 40,275              | 44,992              |
| Prepaid items  | 34,112              | 21,593              |
|  | <b>\$ 926,624</b>   | <b>\$ 852,622</b>   |
| <b>Noncurrent assets</b>   |                     |                     |
| Cash and cash equivalents - restricted for capital improvements  | \$ 299,764          | \$ 254,480          |
| Planning and development costs - net of accumulated amortization | 47,624              | 53,179              |
| Debt issuance costs - net of accumulated amortization            | 5,451               | 6,427               |
|  | <b>\$ 352,839</b>   | <b>\$ 314,086</b>   |
| Capital assets   | \$ 13,064,434       | \$ 13,469,325       |
| Less: allowance for depreciation                                 | (8,242,217)         | (8,681,481)         |
|  | <b>\$ 4,822,217</b> | <b>\$ 4,787,844</b> |
| <b>Total noncurrent assets - net of accumulated depreciation</b> | <b>\$ 4,822,217</b> | <b>\$ 4,787,844</b> |
| <b>Total noncurrent assets</b>                                   | <b>\$ 5,175,056</b> | <b>\$ 5,101,930</b> |
| <b>Total Assets</b>  | <b>\$ 6,101,680</b> | <b>\$ 5,954,552</b> |
| <b>Liabilities</b>   |                     |                     |
| <b>Current liabilities</b>                                       |                     |                     |
| Accounts payable   | \$ 90,315           | \$ 93,642           |
| Due to City of Duluth  | 137,333             | 136,420             |
| Due to other governments   | 4,073               | 2,853               |
| Accrued salaries payable   | 10,730              | 17,528              |
| Accrued vacation payable   | 51,576              | 51,271              |
| Accrued interest payable   | 26,849              | 31,022              |
| Leases payable   | 93,426              | 152,117             |
| Revenue bonds payable  | 166,798             | 145,283             |
| Deferred revenue   | 185,116             | 158,811             |
|  | <b>\$ 766,216</b>   | <b>\$ 788,947</b>   |
| <b>Noncurrent liabilities</b>                                    |                     |                     |
| Due to City of Duluth  | \$ 136,015          | \$ 206,512          |
| Leases payable   | 286,304             | 219,860             |
| Revenue bonds payable  | 1,167,820           | 1,334,618           |
|  | <b>\$ 1,590,139</b> | <b>\$ 1,760,990</b> |
| <b>Total noncurrent liabilities</b>                              | <b>\$ 1,590,139</b> | <b>\$ 1,760,990</b> |
| <b>Total Liabilities</b>   | <b>\$ 2,356,355</b> | <b>\$ 2,549,937</b> |
| <b>Net Assets</b>  |                     |                     |
| Invested in capital assets - net of related debt                 | \$ 3,107,869        | \$ 2,963,292        |
| Restricted for capital improvements                              | 299,764             | 254,480             |
| Restricted for workers' compensation claims                      | 25,000              | 25,000              |
| Restricted for special projects                                  | 5,950               | -                   |
| Unrestricted   | 306,742             | 161,843             |
|  | <b>\$ 3,745,325</b> | <b>\$ 3,404,615</b> |
| <b>Total Net Assets</b>  | <b>\$ 3,745,325</b> | <b>\$ 3,404,615</b> |

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

**EXHIBIT B**

**COMPARATIVE STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS  
YEARS ENDED APRIL 30, 2006 AND 2005**

|  | <b>2006</b>         | <b>2005</b>         |
|--|---------------------|---------------------|
| <b>Operating Revenues</b>                                  |                     |                     |
| Sales  | \$ 825,540          | \$ 759,393          |
| Less: cost of goods sold                                   | (341,411)           | (278,458)           |
| <b>Gross profit on sales</b>                               | <b>\$ 484,129</b>   | <b>\$ 480,935</b>   |
| Charges for services                                       | 3,389,628           | 2,998,252           |
| Miscellaneous  | 51,852              | 15,376              |
| <b>Total Operating Revenues</b>                            | <b>\$ 3,925,609</b> | <b>\$ 3,494,563</b> |
| <b>Operating Expenses</b>                                  |                     |                     |
| Personal services  | \$ 1,937,680        | \$ 1,625,417        |
| Supplies   | 238,890             | 220,120             |
| Utilities  | 322,901             | 327,488             |
| Other services and charges                                 | 844,330             | 782,325             |
| Amortization   | 20,787              | 24,410              |
| Depreciation   | 395,549             | 431,708             |
| <b>Total Operating Expenses</b>                            | <b>\$ 3,760,137</b> | <b>\$ 3,411,468</b> |
| <b>Operating Income (Loss)</b>                             | <b>\$ 165,472</b>   | <b>\$ 83,095</b>    |
| <b>Nonoperating Revenues (Expenses)</b>                    |                     |                     |
| Earnings on investments                                    | \$ 12,467           | \$ 6,626            |
| Tourism tax  | 225,000             | 225,000             |
| Gain (loss) on sale or disposition of capital assets - net | 8,714               | (5,531)             |
| Claims and judgments                                       | -                   | (3,218)             |
| Interest expense   | (70,943)            | (93,772)            |
| <b>Total Nonoperating Revenues (Expenses)</b>              | <b>\$ 175,238</b>   | <b>\$ 129,105</b>   |
| <b>Change in Net Assets</b>                                | <b>\$ 340,710</b>   | <b>\$ 212,200</b>   |
| <b>Net Assets - May 1</b>                                  | <b>3,404,615</b>    | <b>3,192,415</b>    |
| <b>Net Assets - April 30</b>                               | <b>\$ 3,745,325</b> | <b>\$ 3,404,615</b> |

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

**EXHIBIT C**

**COMPARATIVE STATEMENT OF CASH FLOWS  
YEARS ENDED APRIL 30, 2006 AND 2005**

|  | <b>2006</b>         | <b>2005</b>         |
|--|---------------------|---------------------|
| <b>Cash Flows from Operating Activities</b>  |                     |                     |
| Cash received from customers   | \$ 4,234,795        | \$ 3,716,880        |
| Cash paid to suppliers   | (1,763,470)         | (1,464,760)         |
| Cash paid to employees   | (1,944,173)         | (1,641,913)         |
| Cash paid for claims and judgments   | -                   | (3,218)             |
| Other cash received  | 51,852              | 15,376              |
|  | <b>\$ 579,004</b>   | <b>\$ 622,365</b>   |
| <b>Cash Flows from Capital and Related Financing Activities</b>  |                     |                     |
| Capital lease payments   | \$ (146,189)        | \$ (157,879)        |
| Acquisition and construction of capital assets   | (289,147)           | (318,981)           |
|  | <b>\$ (435,336)</b> | <b>\$ (476,860)</b> |
| <b>Cash Flows from Investing Activities</b>  |                     |                     |
| Interest on investments  | \$ 12,467           | \$ 6,626            |
|  | <b>\$ 156,135</b>   | <b>\$ 152,131</b>   |
| <b>Net Increase (Decrease) in Cash and Cash Equivalents</b>  | <b>\$ 156,135</b>   | <b>\$ 152,131</b>   |
| <b>Cash and Cash Equivalents - May 1</b>   | <b>977,109</b>      | <b>824,978</b>      |
| <b>Cash and Cash Equivalents - April 30</b>  | <b>\$ 1,133,244</b> | <b>\$ 977,109</b>   |
| <b>Reconciliation of operating income (loss) to net cash provided by (used in) operating activities</b>            |                     |                     |
| <b>Net operating income (loss)</b>   | <b>\$ 165,472</b>   | <b>\$ 83,095</b>    |
| <b>Adjustments to reconcile net operating income (loss) to net cash provided by (used in) operating activities</b> |                     |                     |
| Depreciation   | 395,549             | 431,708             |
| Amortization   | 20,787              | 24,410              |
| Claims and judgments   | -                   | (3,218)             |
| Change in assets and liabilities   |                     |                     |
| Decrease (increase) in receivables   | 44,651              | (22,843)            |
| Decrease (increase) in inventory   | 4,717               | 4,575               |
| Decrease (increase) in prepaid items   | (12,519)            | 8,818               |
| Increase (decrease) in accounts payable  | (59,465)            | 69,661              |
| Increase (decrease) in salaries payable  | (6,798)             | 1,155               |
| Increase (decrease) in vacations payable   | 305                 | (17,651)            |
| Increase (decrease) in deferred revenue  | 26,305              | 42,655              |
|  | <b>\$ 579,004</b>   | <b>\$ 622,365</b>   |

**Noncash Investing, Capital, and Financing Activities  
Fiscal Year Ended April 30, 2006**

The City of Duluth directly makes revenue bond payments for the Spirit Mountain Recreation Area Authority. The revenue bonds are secured by the Authority, but tourism tax is actually used to fund the bond payments. The Authority is to withhold \$225,000 in revenue to use for capital improvements. A capital improvement budget is submitted and approved by the City.

The Authority refinanced the 2003 Groomer Lease. In the current lease, the Authority retained the BR 350 2004 Grooming Tractor, acquired the BR 350 2006 Groomer Tractor, and disposed of the BR 275 2002 Groomer Tractor.

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**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

NOTES TO THE FINANCIAL STATEMENTS  
AS OF AND FOR THE YEARS ENDED APRIL 30, 2006 AND 2005

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1. Summary of Significant Accounting Policies

Organization

The Spirit Mountain Recreation Area Authority was created by Minn. Laws 1973, ch. 327, for the purpose of developing and operating wide-range recreational facilities in the Spirit Mountain area within and adjacent to the City of Duluth, Minnesota. The management of the Authority is vested in seven directors appointed by the Mayor of Duluth and approved by resolution of the City Council.

The accounting policies of the Spirit Mountain Recreation Area Authority conform to generally accepted accounting principles.

A. Financial Reporting Entity

The Authority is a component unit of the City of Duluth reporting entity and, therefore, is included in the City's Comprehensive Annual Financial Report.

B. Fund Accounting

The Authority is accounted for as an enterprise fund. Enterprise funds account for operations financed and operated in a manner similar to private business enterprises-- where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

The principal operating revenues of the Authority are charges to customers for sales and services for recreational activities offered within the Spirit Mountain area. All revenues not meeting this definition are reported as nonoperating revenues.

When both restricted and unrestricted resources are available for use, it is the Authority's policy to use restricted resources first, then unrestricted resources as they are needed.

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

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1. Summary of Significant Accounting Policies (Continued)

C. Basis of Accounting

The Authority uses the accrual basis of accounting. Revenues are recognized when they are earned, and expenses are recognized when they are incurred. Pursuant to Governmental Accounting Standards Board (GASB) Statement 20, the Authority has elected not to apply accounting standards issued after November 30, 1989, by the Financial Accounting Standards Board.

D. Assets

For purposes of the statement of cash flows, all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased are considered to be cash equivalents.

Inventories of supplies and merchandise for resale are priced at the lower of cost or market value on a first-in, first-out basis.

Development costs, consisting of engineering, feasibility study, and interest costs during construction, have been recorded at cost and are being amortized over 40 years.

Monies with external restrictions are accounted for as restricted assets.

Capital assets are stated at cost. Interest costs incurred during construction are not capitalized unless determined to be significant.

Depreciation of capital assets is determined using the straight-line method. The estimated useful lives of the assets are:

| <u>Classification</u>    | <u>Range</u>  |
|--------------------------|---------------|
| Buildings and structures | 5 to 40 years |
| Equipment                | 3 to 40 years |
| Furniture and fixtures   | 5 to 20 years |
| Other fixed assets       | 2 to 40 years |

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

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1. Summary of Significant Accounting Policies (Continued)

E. Trade-Offs

The Authority issues ski lift passes, rentals, lessons, etc., in exchange for other non-monetary assets or services, such as advertising and other promotional services. The value of the lift passes, rentals, or lessons is credited to the appropriate revenue account and debited to the appropriate expense account.

F. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. Detailed Notes

A. Budget

The Authority adopts an annual budget which is approved by the Duluth City Council. A comparison of budget to actual for the years ended April 30, 2006 and 2005, follows:

|                          | 2006         |              | Variance<br>Favorable<br>(Unfavorable) |
|--------------------------|--------------|--------------|--|
|                          | Budget       | Actual       |  |
| Operating Revenues       |              |              |  |
| Sales                    | \$ 748,249   | \$ 825,540   | \$ 77,291                              |
| Less: cost of goods sold | (279,830)    | (341,411)    | (61,581)                               |
| Gross profit on sales    | \$ 468,419   | \$ 484,129   | \$ 15,710                              |
| Charges for services     | 3,069,767    | 3,389,628    | 319,861                                |
| Miscellaneous            | 11,100       | 51,852       | 40,752                                 |
| Total Operating Revenues | \$ 3,549,286 | \$ 3,925,609 | \$ 376,323                             |



**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

2. Detailed Notes

A. Budget (Continued)

|   | 2005                |                     | Variance<br>Favorable<br>(Unfavorable) |
|---|---------------------|---------------------|--|
|   | Budget              | Actual              |  |
| Operating Expenses                                    |                     |                     |  |
| Personal services                                     | \$ 1,509,576        | \$ 1,625,417        | \$ (115,841)                           |
| Supplies  | 196,698             | 220,120             | (23,422)                               |
| Utilities   | 333,470             | 327,488             | 5,982                                  |
| Other services and charges                            | 839,340             | 782,325             | 57,015                                 |
| Amortization  | 23,000              | 24,410              | (1,410)                                |
| Depreciation  | 410,000             | 431,708             | (21,708)                               |
| Total Operating Expenses                              | <u>\$ 3,312,084</u> | <u>\$ 3,411,468</u> | <u>\$ (99,384)</u>                     |
| Operating Income (Loss)                               | <u>\$ 177,627</u>   | <u>\$ 83,095</u>    | <u>\$ (94,532)</u>                     |
| Nonoperating Revenues<br>(Expenses)                   |                     |                     |  |
| Earnings on investments                               | \$ -                | \$ 6,626            | \$ 6,626                               |
| City of Duluth hotel-motel,<br>food, and beverage tax | 225,000             | 225,000             | -                                      |
| Gain (loss) on disposal of assets                     | -                   | (5,531)             | (5,531)                                |
| Claims and judgments                                  | (30,000)            | (3,218)             | 26,782                                 |
| Interest expense                                      | (97,593)            | (91,427)            | 6,166                                  |
| Other nonoperating expenses                           | -                   | (2,345)             | (2,345)                                |
| Total Nonoperating<br>Revenues (Expenses)             | <u>\$ 97,407</u>    | <u>\$ 129,105</u>   | <u>\$ 31,698</u>                       |
| Change in Net Assets                                  | <u>\$ 275,034</u>   | <u>\$ 212,200</u>   | <u>\$ (62,834)</u>                     |

B. Deposits

Minn. Laws 1973, ch. 327, designates the Treasurer of the City of Duluth as Treasurer of the Authority. Authority deposits are pooled with all other City deposits. Minn. Stat. §§ 118A.02 and 118A.04 authorize the City Treasurer to deposit cash and to invest in certificates of deposit in financial institutions designated by the Duluth City Council. Minnesota statutes require that all Authority deposits be covered by insurance, surety bond, or collateral.

Minn. Stat. §§ 118A.04 and 118A.05 authorize the types of investments available to the City Treasurer. Investments are stated at fair value.

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

2. Detailed Notes

B. Deposits (Continued)

Additional disclosures required by GASB Statement No. 40, *Deposits and Investment Risk Disclosures*, are disclosed on an entity-wide basis in the City of Duluth's Comprehensive Annual Financial Report. The Authority is a component unit of the City of Duluth.

Following is a summary of the Authority's cash:

|                                 | April 30     |            |
|---------------------------------|--------------|------------|
|                                 | 2006         | 2005       |
| City Treasurer                  | \$ 681,687   | \$ 711,262 |
| Money market savings            | 444,268      | 257,347    |
| Petty cash and change funds     | 7,289        | 8,500      |
| Total Cash and Cash Equivalents | \$ 1,133,244 | \$ 977,109 |

C. Capital Assets

A summary of the changes in capital assets for the years ended April 30, 2006 and 2005, follows:

|                                      | Balance<br>May 1, 2005 | Additions  | Deductions | Reclassification | Balance<br>April 30, 2006 |
|--------------------------------------|------------------------|------------|------------|------------------|---------------------------|
| Capital assets not depreciated       |                        |            |            |                  |                           |
| Land and land improvements           | \$ 2,429,118           | \$ -       | \$ -       | \$ -             | \$ 2,429,118              |
| Construction in progress             | 100,746                | 242,190    | -          | (225,329)        | 117,607                   |
| Total capital assets not depreciated | \$ 2,529,864           | \$ 242,190 | \$ -       | \$ (225,329)     | \$ 2,546,725              |
| Capital assets depreciated           |                        |            |            |                  |                           |
| Buildings and structures             | \$ 3,465,395           | \$ -       | \$ 68,012  | \$ 176,737       | \$ 3,574,120              |
| Equipment                            | 6,898,754              | 239,019    | 789,565    | 48,592           | 6,396,800                 |
| Furniture and fixtures               | 197,013                | 4,999      | 7,084      | -                | 194,928                   |
| Other capital assets                 | 378,298                | -          | 26,437     | -                | 351,861                   |
| Total capital assets depreciated     | \$ 10,939,460          | \$ 244,018 | \$ 891,098 | \$ 225,329       | \$ 10,517,709             |

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

2. Detailed Notes

C. Capital Assets (Continued)

|                                       | Balance<br>May 1, 2005 | Additions    | Deductions | Reclassification | Balance<br>April 30, 2006 |
|---------------------------------------|------------------------|--------------|------------|------------------|---------------------------|
| Less: accumulated depreciation for    |                        |              |            |                  |                           |
| Buildings and structures              | \$ 2,055,135           | \$ 140,325   | \$ 60,358  | \$ -             | \$ 2,135,102              |
| Equipment                             | 6,191,325              | 234,883      | 741,432    | -                | 5,684,776                 |
| Furniture and fixtures                | 176,552                | 6,292        | 7,084      | -                | 175,760                   |
| Other capital assets                  | 258,468                | 14,049       | 25,938     | -                | 246,579                   |
| Total accumulated depreciation        | \$ 8,681,480           | \$ 395,549   | \$ 834,812 | \$ -             | \$ 8,242,217              |
| Total capital assets depreciated, net | \$ 2,257,980           | \$ (151,531) | \$ 56,286  | \$ 225,329       | \$ 2,275,492              |
| Capital Assets, Net                   | \$ 4,787,844           | \$ 90,659    | \$ 56,286  | \$ -             | \$ 4,822,217              |
|                                       |                        |              |            |                  |                           |
|                                       | Balance<br>May 1, 2004 | Additions    | Deductions | Reclassification | Balance<br>April 30, 2005 |
| Capital assets not depreciated        |                        |              |            |                  |                           |
| Land and land improvements            | \$ 2,391,330           | \$ -         | \$ -       | \$ 37,788        | \$ 2,429,118              |
| Construction in progress              | 30,007                 | 296,769      | 7,400      | (218,630)        | 100,746                   |
| Total capital assets not depreciated  | \$ 2,421,337           | \$ 296,769   | \$ 7,400   | \$ (180,842)     | \$ 2,529,864              |
| Capital assets depreciated            |                        |              |            |                  |                           |
| Buildings and structures              | \$ 3,216,639           | \$ 29,612    | \$ -       | \$ 219,144       | \$ 3,465,395              |
| Equipment                             | 6,911,572              | -            | 30,122     | 17,304           | 6,898,754                 |
| Furniture and fixtures                | 236,891                | -            | -          | (39,878)         | 197,013                   |
| Other capital assets                  | 394,026                | -            | -          | (15,728)         | 378,298                   |
| Total capital assets depreciated      | \$ 10,759,128          | \$ 29,612    | \$ 30,122  | \$ 180,842       | \$ 10,939,460             |
| Less: accumulated depreciation for    |                        |              |            |                  |                           |
| Buildings and structures              | \$ 1,932,706           | \$ 126,229   | \$ -       | \$ (3,800)       | \$ 2,055,135              |
| Equipment                             | 5,918,455              | 285,402      | 15,032     | 2,500            | 6,191,325                 |
| Furniture and fixtures                | 170,723                | 5,829        | -          | -                | 176,552                   |
| Other capital assets                  | 242,920                | 14,248       | -          | 1,300            | 258,468                   |
| Total accumulated depreciation        | \$ 8,264,804           | \$ 431,708   | \$ 15,032  | \$ -             | \$ 8,681,480              |
| Total capital assets depreciated, net | \$ 2,494,324           | \$ (402,096) | \$ 15,090  | \$ 180,842       | \$ 2,257,980              |
| Capital Assets, Net                   | \$ 4,915,661           | \$ (105,327) | \$ 22,490  | \$ -             | \$ 4,787,844              |

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

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2. Detailed Notes (Continued)

D. Vacation, Sick Leave, and Compensatory Time

Full-time employees are granted from 10 to 20 days of vacation per year depending on their years of service. Maximum amounts of vacation time that can be accumulated depend on which union bargaining unit is representing the employee. Sick leave is accumulated at the rate of 30 days per year up to a maximum of 120 days for those employees covered by the Minnesota Arrowhead District Council 96.

Staff personnel are granted from one to four weeks of vacation per year depending on their years of service. Staff may carry forward no more than the amount that was earned in the year. Staff personnel are granted 30 days of sick leave per year.

Unpaid vacation pay earned as of April 30, 2006 and 2005, is \$51,576 and \$51,272, respectively, and is recognized as a liability in the financial statements.

Sick leave is recorded as an expense when paid. The contingent liability for unused sick leave is not recognized in the financial statements.

E. Due to City of Duluth

The amounts due to the City at April 30, 2006 and 2005, follows:

|  | <u>2006</u>       | <u>2005</u>       |
|--|-------------------|-------------------|
| General Fund - cost allocation plan      | \$ 54,665         | \$ 143,967        |
| General Fund - sales tax                 | 1,282             | 734               |
| Self-Insurance Fund - insurance premiums | <u>217,401</u>    | <u>198,231</u>    |
| Total                                    | <u>\$ 273,348</u> | <u>\$ 342,932</u> |

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

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2. Detailed Notes

E. Due to City of Duluth (Continued)

In 2005, the City of Duluth and Spirit Mountain agreed on a repayment schedule. Of the \$273,348 owed to the City, \$137,333 is expected to be repaid within the next year. Payments will be made through 2010. A summary of the noncurrent payments by year due follows:

| Year<br>Ended<br>April 30 |    |         |
|---------------------------|----|---------|
| 2008                      | \$ | 45,500  |
| 2009                      |    | 45,500  |
| 2010                      |    | 45,015  |
| Total                     | \$ | 136,015 |

F. Long-Term Debt

The following is a summary of the long-term bonded debt transactions of the Authority.

|   |                |
|---|----------------|
|   | 2006           |
| Bonds Payable - May 1   | \$ 1,479,901   |
| Issued  | -              |
| Payments  | (159,538)      |
| Add: current year amount of unamortized refinancing deferred loss | 14,255         |
| Bonds Payable - April 30  | \$ 1,334,618   |
| <br>Amount Due Within One Year                                    | <br>\$ 166,798 |

Bonds payable comprise the following issue:

A \$1,646,750 City of Duluth Gross Revenue Recreational Facility Bond dated March 28, 2003, with interest at 4.50 percent, due in semi-annual installments on June 1 and December 1, through 2012. The bonds are not general obligations of the City and are payable from Authority gross revenues. The City has pledged tourism taxes in the amount of \$225,000 per year as part of the gross revenues of

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

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2. Detailed Notes

F. Long-Term Debt (Continued)

the project. The Authority is required to deposit \$75,000 on each November 15, December 15, and January 15 to the Repair and Replacement Account each year until 2012. The monies in this account can then be expended by the Authority for repairs and replacements made to the facilities. The bonds were issued to refinance existing debt. The refinancing resulted in a \$53,850 deferred loss, which is amortized over the life of the old debt.

The annual requirements to service the debt follow:

| <u>Fiscal Year<br/>Ended April 30</u> | <u>Principal</u>    | <u>Interest</u>   |
|---------------------------------------|---------------------|-------------------|
| 2007                                  | \$ 166,798          | \$ 58,202         |
| 2008                                  | 174,388             | 50,612            |
| 2009                                  | 182,324             | 42,676            |
| 2010                                  | 190,620             | 34,379            |
| 2011                                  | 199,295             | 25,705            |
| 2012                                  | 208,365             | 16,636            |
| 2013                                  | 212,828             | 7,154             |
| Total                                 | <u>\$ 1,334,618</u> | <u>\$ 235,364</u> |

G. Capitalized Lease Obligations

Capitalized lease obligations consist of the following at April 30, 2006:

| <u>Type of Property</u>        |                   |
|--------------------------------|-------------------|
| Building improvements          | \$ 210,021        |
| Equipment                      | 661,588           |
| Less: accumulated amortization | <u>(476,358)</u>  |
| Net Capital Lease Property     | <u>\$ 395,251</u> |

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

2. Detailed Notes

G. Capitalized Lease Obligations (Continued)

Minimum future lease payments follow:

| Fiscal Year<br>Ended April 30 | Principal  | Interest  |
|-------------------------------|------------|-----------|
| 2007                          | \$ 94,862  | \$ 17,985 |
| 2008                          | 99,560     | 13,288    |
| 2009                          | 104,488    | 8,359     |
| 2010                          | 80,820     | 3,185     |
| Total                         | \$ 379,730 | \$ 42,817 |

Capitalized lease obligations at April 30, 2006, consist of the following leases:

|  |            |
|--|------------|
| A \$210,000 lease purchase for gas conversion equipment, dated April 30, 1999; due in variable semi-annual installments through February 2009, with interest at 5.25 percent.  | \$ 74,614  |
| A \$381,410 lease purchase to refinance the 2003 lease, to replace one groomer and retain the other groomer, dated August 1, 2005, due in periodic installments during the ski season through April 2010, with interest at 4.78 percent. | 305,116    |
| Total  | \$ 379,730 |
| Current portion  | \$ 93,426  |
| Long-term portion  | 286,304    |
| Total  | \$ 379,730 |

H. Operating Lease

The Authority is obligated under an operating lease for office equipment. Lease expense for fiscal year 2006 and 2005 is \$2,040 for each year. The future minimum rental payments, which are not reported as liabilities in the financial statements at April 30, 2006, are \$4,252 due in fiscal year 2007.

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

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2. Detailed Notes (Continued)

I. Mountain Villas Agreements

In November 1979, the Authority entered into an agreement with the Mountain Villas Owner's Association, Inc., for the rental of property associated with 15 rental housing units sold by the Authority to the Association. The agreement provides for an annual base rental payment of \$15,000 by the Association and features an annual inflation adjustment clause equal to the change in the consumer price index. This clause was not invoked by the Authority until 1989.

In October 1989, the Authority entered into another agreement with the Mountain Villas Owner's Association, Inc., to manage the 15 rental housing units owned by the Association. The agreement provides payment to the Authority of an annual base management fee of \$24,000 plus 10 percent of gross sales.

3. Risk Management

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; employee health and dental; and natural disasters. The Authority participates in the City of Duluth Internal Service Funds to insure against its obligation to provide benefits to employees pursuant to the Minnesota Workers' Compensation Act and to insure against general liability claims, except the liability claims arising by reason of selling, serving, or furnishing alcoholic beverages. The Authority purchases commercial insurance for all other risks of loss. There were no significant reductions in insurance coverage from the previous year. There were no settlements in excess of insurance for any of the past three fiscal years.

For claims arising from the Workers' Compensation Act, insured through the City of Duluth Self-Insurance Internal Service Fund, the Authority retains responsibility for attorney fees on contested claims. In addition, the Authority is required to escrow \$25,000 as a reserve fund to pay excess workers' compensation claims and costs that exceed the agreed-upon value of plan participation with the City. No liability has been recognized in the financial statements for excess workers' compensation claims and costs.

For general liability claims, insured through the City of Duluth Self-Insurance Internal Service Fund, the Authority retains responsibility for paying the first \$50,000 of each loss resulting from each occurrence. The maximum coverage provided by the City was \$300,000 per claimant; \$1,000,000 per occurrence. The estimated liability of the Authority for general liability claims, where coverage is not provided by the City, is accrued if the

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

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3. Risk Management (Continued)

Authority's attorney determines settlement is probable, based on a case-by-case evaluation. The attorney has indicated there are \$17,500 in claims that may become losses to the Authority.

4. Defeased Debt

On March 31, 2003, the City of Duluth issued a Gross Revenue Recreational Facility Bond, with an interest rate of 4.5 percent, to refund the Authority's refinancing lease, having an interest rate of 4.85 percent. The \$1,646,750 Gross Revenue Recreation Facility Bond was issued at par. The proceeds, together with Authority funds of \$53,527, were used to refund a \$1,646,750 refinancing lease with accrued interest of \$53,527.

As a result of the refunding, the Authority increased its total debt service requirement by \$312,471, which resulted in an economic loss (difference between the present value of the debt service payments on the old and new debt) of \$106,360.

As part of the agreement to issue the Gross Revenue Recreational Facility Bond, the City of Duluth pledged tourism taxes in the amount of \$225,000 per year to pay principal and interest on the bonds.

5. Pension Plans

A. Plan Description

All full-time and certain part-time employees of the Spirit Mountain Recreation Area Authority are covered by defined benefit plans administered by the Public Employees Retirement Association of Minnesota (PERA). The PERA administers the Public Employees Retirement Fund, which is a cost-sharing, multiple-employer retirement plan. The plan is established and administered in accordance with Minn. Stat. chs. 353 and 356.

Public Employees Retirement Fund members belong to either the Coordinated Plan or the Basic Plan. Coordinated Plan members are covered by Social Security, and Basic Plan members are not. All new members must participate in the Coordinated Plan.

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

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5. Pension Plans

A. Plan Description (Continued)

The PERA provides retirement benefits as well as disability benefits to members and benefits to survivors upon death of eligible members. Benefits are established by state statute and vest after three years of credited service. The retirement benefits are based on a member's highest average salary for any five successive years of allowable service, age, and years of credit at termination of service.

Two methods are used to compute benefits for Coordinated and Basic Plan members. The retiring member receives the higher of a step-rate benefit accrual formula (Method 1) or a level accrual formula (Method 2). Under Method 1, the annuity accrual rate for a Basic Plan member is 2.2 percent of average salary for each of the first ten years of service and 2.7 percent for each year thereafter. For a Coordinated Plan member, the annuity accrual rate is 1.2 percent of average salary for each of the first ten years and 1.7 percent for each successive year. Using Method 2, the annuity accrual rate is 2.7 percent of average salary for Basic Plan members and 1.7 percent for Coordinated Plan members for each year of service.

For Public Employees Retirement Fund members whose annuity is calculated using Method 1, a full annuity is available when age plus years of service equal 90. A reduced retirement annuity is also available to eligible members seeking early retirement.

The benefit provisions stated in the previous paragraphs of this section are current provisions and apply to active plan participants. Vested, terminated employees who are entitled to benefits but are not yet receiving them are bound by the provisions in effect at the time they last terminated public service.

The PERA issues a publicly available financial report that includes financial statements and required supplementary information for the Public Employees Retirement Fund. That report may be obtained on the Internet at [www.mnpera.org](http://www.mnpera.org); by writing to PERA at 60 Empire Drive, Suite 200, Saint Paul, Minnesota 55103-2088; or by calling 651-296-7460 or 1-800-652-9026.

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

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5. Pension Plans (Continued)

B. Funding Policy

Pension benefits are funded from member and employer contributions and income from the investment of fund assets. Minn. Stat. ch. 353 sets the rates for employer and employee contributions. These statutes are established and amended by the State Legislature. The Authority makes annual contributions to the pension plans equal to the amount required by state statutes. Public Employees Retirement Fund Basic Plan members and Coordinated Plan members were required to contribute 9.10 and 5.10 percent, respectively, of their annual covered salary in 2005. Contribution rates in the Coordinated Plan increased in 2006 to 5.50 percent. The Authority is required to contribute the following percentages of annual covered payroll:

|                                  |        |
|----------------------------------|--------|
| In 2005                          |        |
| Public Employees Retirement Fund |        |
| Basic Plan members               | 11.78% |
| Coordinated Plan members         | 5.53   |
| In 2006                          |        |
| Public Employees Retirement Fund |        |
| Basic Plan members               | 11.78% |
| Coordinated Plan members         | 6.00   |

The Authority's contributions for the years ending April 30, 2006, 2005, and 2004, were \$53,925, \$46,307, and \$45,380, respectively, equal to the contractually required contributions for each year as set by state statute.

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**SUPPLEMENTARY INFORMATION**

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**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

**Schedule 1**

**COMPARATIVE STATEMENT OF OPERATING REVENUES  
YEARS ENDED APRIL 30, 2006 AND 2005**

|                                   | <b>2006</b>         | <b>2005</b>         |
|-----------------------------------|---------------------|---------------------|
| <b>Sales</b>                      |                     |                     |
| Food                              | \$ 472,968          | \$ 449,650          |
| Liquor                            | 205,412             | 189,953             |
| Ski shop                          | 147,160             | 119,790             |
| Less: cost of goods sold          | (341,411)           | (278,458)           |
| <b>Net sales</b>                  | <b>\$ 484,129</b>   | <b>\$ 480,935</b>   |
| <b>Charges for Services</b>       |                     |                     |
| Season pass                       | \$ 1,229,236        | \$ 1,142,692        |
| Daily lift tickets                | 1,303,552           | 1,112,886           |
| Ski school and snow sports        | 128,918             | 109,478             |
| Ski rental                        | 287,735             | 248,975             |
| Snowboard rental                  | 103,983             | 75,496              |
| Locker rental                     | 29,077              | 26,823              |
| Nordic tickets and rental         | 18,693              | 21,394              |
| Paintball admissions              | -                   | 1,851               |
| Snocross                          | 67,605              | 69,606              |
| Campground                        | 82,361              | 66,069              |
| Summer events                     | 19,649              | 22,962              |
| Mountain villa management fee     | 90,663              | 80,741              |
| Marketing revenue                 | 28,156              | 19,279              |
| <b>Total charges for services</b> | <b>\$ 3,389,628</b> | <b>\$ 2,998,252</b> |
| <b>Miscellaneous</b>              |                     |                     |
| Other revenues                    | <b>\$ 51,852</b>    | <b>\$ 15,376</b>    |
| <b>Total Operating Revenues</b>   | <b>\$ 3,925,609</b> | <b>\$ 3,494,563</b> |

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

**Schedule 2**

**COMPARATIVE STATEMENT OF OPERATING EXPENSES  
YEARS ENDED APRIL 30, 2006 AND 2005**

|                                   | <b>2006</b>         | <b>2005</b>         |
|-----------------------------------|---------------------|---------------------|
| <b>Department</b>                 |                     |                     |
| Food and beverage                 | \$ 217,082          | \$ 221,105          |
| Housekeeping                      | 65,314              | 51,794              |
| Rental                            | 75,500              | 78,776              |
| Ski shop                          | 30,226              | 23,807              |
| Campground                        | 56,804              | 86,077              |
| Parking and lockers               | 31,090              | 6,200               |
| Building and grounds              | 207,863             | 168,744             |
| Snocross                          | 96,342              | 82,260              |
| Summer events                     | 41,419              | 28,387              |
| Ski school and snow sports center | 135,452             | 95,047              |
| Outside mountain operations       | 968,879             | 870,458             |
| Nordic                            | 22,582              | 17,129              |
| Ski patrol                        | 9,899               | 5,886               |
| Sales and marketing               | 473,350             | 448,507             |
| Office administration             | 871,812             | 732,091             |
| Mountain villas                   | 40,187              | 39,082              |
| <b>Total departmental costs</b>   | <b>\$ 3,343,801</b> | <b>\$ 2,955,350</b> |
| Amortization                      | 20,787              | 24,410              |
| Depreciation                      | 395,549             | 431,708             |
| <b>Total Operating Expenses</b>   | <b>\$ 3,760,137</b> | <b>\$ 3,411,468</b> |

**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

Schedule 3

**STATEMENT OF CAPITAL IMPROVEMENTS  
YEAR ENDED APRIL 30, 2006**

|                                       | <b>Repair and<br/>Replacement<br/>Account<br/>Capital<br/>Improvements</b> | <b>Non-Repair and<br/>Replacement<br/>Account<br/>Capital<br/>Improvements</b> | <b>Total</b>      |
|---------------------------------------|--|--|-------------------|
| <b>Construction in Progress</b>       |  |  |                   |
| Computer upgrades                     | \$ 5,000   | \$ -   | \$ 5,000          |
| Chalet interior painting              | 15,100   | -  | 15,100            |
| Snowmobile                            | 12,500   | 543  | 13,043            |
| Rental remodel                        | 9,016  | -  | 9,016             |
| Spirit Express load cell upgrade      | 22,500   | 1,049  | 23,549            |
| Snowmaking pipe return lines          | 26,000   | 652  | 26,652            |
| Architectural fees                    | 6,721  | -  | 6,721             |
| Carpet in BP and EN                   | 55,000   | 226  | 55,226            |
| Rental equipment                      | 15,000   | 7,387  | 22,387            |
| Chalet sound system                   | 3,294  | -  | 3,294             |
| Boot racks                            | 9,585  | -  | 9,585             |
| Moosehead air conditioning            | -  | 1,838  | 1,838             |
| Conveyor lift                         | -  | 53,802   | 53,802            |
| Groomer                               | -  | 229,985  | 229,985           |
| Nordic groomer                        | -  | 1,477  | 1,477             |
| Office furniture                      | -  | 2,827  | 2,827             |
| Chairs for Moosehead                  | -  | 2,173  | 2,173             |
| Water heaters                         | -  | 4,533  | 4,533             |
|                                       | <b>\$ 179,716</b>  | <b>\$ 306,492</b>  | <b>\$ 486,208</b> |
| <b>Total Construction in Progress</b> | <b>\$ 179,716</b>  | <b>\$ 306,492</b>  | <b>\$ 486,208</b> |

**Repair and Replacement Account Summary**

|  |                   |
|--|-------------------|
| Net Assets - restricted for capital improvements at April 30, 2005 | \$ 254,480        |
| 2006 repair and replacement account deposits                       | 225,000           |
| Repair and replacement account capital improvements                | (179,716)         |
| Net Assets - restricted for capital improvements at April 30, 2006 | <b>\$ 299,764</b> |

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**SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

**Schedule 4**

SCHEDULE OF FINDINGS AND RECOMMENDATIONS  
FOR THE YEAR ENDED APRIL 30, 2006

**I. FINDINGS RELATED TO FINANCIAL STATEMENTS AUDITED IN  
ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

INTERNAL CONTROL

PREVIOUSLY REPORTED ITEM NOT RESOLVED

97-1 Segregation of Duties

Due to the limited number of office personnel within the Spirit Mountain Recreation Area Authority, segregation of the accounting functions necessary to ensure adequate internal accounting control is not possible. This is not unusual in operations the size of the Authority; however, the Authority's management should constantly be aware of this condition and realize that the concentration of duties and responsibilities in a limited number of individuals is not desirable from an accounting point of view.

We recommend that the Spirit Mountain Recreation Area Authority's management be aware of the lack of segregation of accounting functions and continue oversight procedures to ensure that the Authority's internal control policies and procedures are followed by staff.

Client's Response:

*The Authority's Board and Management will continue to review segregation of accounting duties and establish appropriate policies to deal with issues raised by a limited number of personnel. As does the Auditor, the Authority recognizes that the trade-off of additional personnel expenses and limited segregation of accounting duties is an ongoing one. We will continue to make sound business judgments regarding these issues and elicit specific suggestions and comments from the State Auditor's Office.*

**PREVIOUSLY REPORTED ITEMS RESOLVED**

**Ski Shop Inventory (05-1)**

The ski shop does not maintain a perpetual inventory system. An inventory count was conducted once a year at the end of the ski season. The ski shop did not have current inventory records available throughout the ski season. We recommended the Authority consider establishing a perpetual inventory system and monthly physical inventory counts be conducted by non-ski shop staff. Also, the accounting department should compare the monthly physical inventory counts to the perpetual inventory records.

**Resolution**

The Authority completes an inventory count on a monthly basis October through April. The ski shop is not open during the months of May through September. Some inventory items are sold at the campground during the summer, but it is not cost-efficient to do inventory during the summer months, and the amount of inventory is insignificant.

**Pay Adjustments for Employees with Missing Pay (05-2)**

The Authority did not have an adequate policy for paying adjustments to employees for missing payroll hours. We recommended the Authority create and adhere to a strict policy for adjusting employees' pay that does not include making cash payments.

**Resolution**

The Authority has implemented a "Pay Missing" policy, which is included in the handbook. If an employee is missing pay, they will either be paid on their next check or a check will be issued through the accounts payable system.

**II. OTHER FINDINGS AND RECOMMENDATIONS**

**MINNESOTA LEGAL COMPLIANCE**

**PREVIOUSLY REPORTED ITEM RESOLVED**

**In-Kind Benefits (05-3)**

We noted two instances where employees hosted wedding receptions and were not charged for room rental and also received discounted food and liquor prices. The Authority has no specific statutory authority to provide employees in-kind benefits. We recommended the Authority discontinue this practice until it has specific statutory authority to provide in-kind benefits to employees.

**Resolution**

The Authority no longer has a staff banquet policy or provides discounts to employees for events held at Spirit Mountain.

**III. OTHER ITEM FOR CONSIDERATION**

Other Postemployment Benefits (OPEB)

The Governmental Accounting Standards Board (GASB) recently issued Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pension Plans*, which governs employer accounting and financial reporting for OPEB. This standard, like what GASB Statement 27 did for government employee pension benefits and plans, provides the accounting standards for the various other postemployment benefits many local governments offer to their employees. OPEB can include many different benefits offered to retirees such as health, dental, life, and long-term care insurance coverage.

If retirees are included in an insurance plan and pay a rate similar to that paid for younger active employees, this implicit subsidy is considered OPEB. In fact, local governments may be required to continue medical insurance coverage pursuant to Minn. Stat. § 471.61, subd. 2b. This benefit is common when accumulated sick leave is used to pay for retiree medical insurance. Under the new GASB statement, accounting for OPEB is now similar to the accounting used by governments for pension plans.

Some of the issues the Authority's Board will need to address in order to comply with the statement are:

- determine if employees are provided OPEB;
- if OPEB are being provided, the Authority's Board will have to determine whether it will advance fund the benefits or pay for them on a pay-as-you-go basis;
- if OPEB are being provided, and the Authority's Board determines that the establishment of a trust is desirable in order to fund OPEB, the Board will have to wait until legislation is enacted authorizing the creation of an OPEB trust and establishing an applicable investment standard; and
- in order to determine annual costs and liabilities that need to be recognized, the Authority's Board will have to decide whether to hire an actuary.

**Schedule 4**  
***(Continued)***

If applicable for the Spirit Mountain Recreation Area Authority, GASB Statement 45 would be implemented for the year ended April 30, 2007.



STATE OF MINNESOTA  
OFFICE OF THE STATE AUDITOR

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PATRICIA ANDERSON  
STATE AUDITOR

**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***

Mayor and City Council  
City of Duluth

Board of Directors  
Spirit Mountain Recreation Area Authority

We have audited the financial statements of the Spirit Mountain Recreation Area Authority, a component unit of the City of Duluth, as of and for the year ended April 30, 2006, and have issued our report thereon dated July 31, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Spirit Mountain Recreation Area Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted a matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Authority's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. This reportable condition is described in the accompanying Schedule of Findings and Recommendations as item 97-1.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the

financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe the reportable condition indicated above is not a material weakness.

### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Spirit Mountain Recreation Area Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

### Minnesota Legal Compliance

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the provisions of the *Minnesota Legal Compliance Audit Guide for Local Government*, promulgated by the State Auditor pursuant to Minn. Stat. § 6.65. Accordingly, the audit included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

The *Minnesota Legal Compliance Audit Guide for Local Government* contains five categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, and claims and disbursements. Our study included all of the listed categories.

The results of our tests indicate that, for the items tested, the Spirit Mountain Recreation Area Authority complied with the material terms and conditions of applicable legal provisions.

This report is intended solely for the information and use of the Board of Directors, Mayor and City Council of Duluth, and the Authority's management and is not intended to be, and should not be, used by anyone other than those specified parties.

*/s/Pat Anderson*

PATRICIA ANDERSON  
STATE AUDITOR

*/s/Greg Hierlinger*

GREG HIERLINGER, CPA  
DEPUTY STATE AUDITOR

End of Fieldwork: July 31, 2006