

# STATE OF MINNESOTA

## Office of the State Auditor



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

---

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

**FOR THE YEARS ENDED APRIL 30, 2005 AND 2004**

## **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.

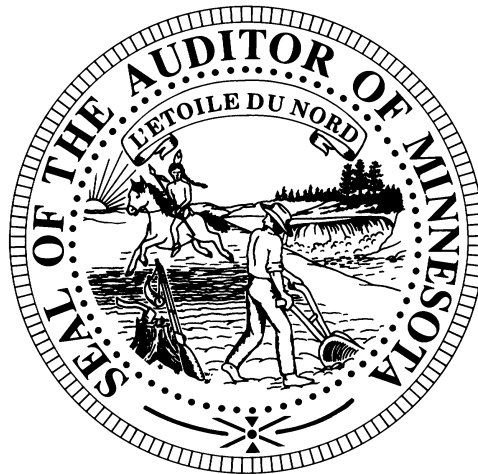
The State Auditor serves on the State Executive Council, State Board of Investment, Land Exchange Board, Public Employee's Retirement Association Board, Minnesota Housing Finance Agency, and the Rural Finance Authority Board.

Office of the State Auditor  
525 Park Street, Suite 500  
Saint Paul, Minnesota 55103  
(651) 296-2551  
state.auditor@state.mn.us  
www.auditor.state.mn.us

This document can be made available in alternative formats upon request. Call 651-296-2551 [voice] or 1-800-627-3529 [relay service] for assistance; or visit the State Auditor's web site: [www.auditor.state.mn.us](http://www.auditor.state.mn.us).

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

**For the Years Ended April 30, 2005 and 2004**



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

This page was left blank intentionally.

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

TABLE OF CONTENTS

	<u>Reference</u>	<u>Page</u>
<b>Introductory Section</b>		
Organization		1
<b>Financial Section</b>		
Independent Auditor's Report		2
Management's Discussion and Analysis		4
Financial Statements		
Comparative Statement of Net Assets	Exhibit A	10
Comparative Statement of Revenues, Expenses, and Changes in Net Assets	Exhibit B	11
Comparative Statement of Cash Flows	Exhibit C	12
Notes to the Financial Statements		13
Supplementary Information		
Comparative Statement of Operating Revenues	Schedule 1	28
Comparative Statement of Operating Expenses	Schedule 2	29
Statement of Capital Improvements	Schedule 3	30
<b>Management and Compliance Section</b>		
Schedule of Findings and Recommendations	Schedule 4	31
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>		37

This page was left blank intentionally.



This page was left blank intentionally.

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

ORGANIZATION  
APRIL 30, 2005

	<u>Term Ending</u>
Directors	
C. J. Bird	June 30, 2005
John Goldfine	June 30, 2005
Sidney Mason	June 30, 2005*
Nancy Nelson	June 30, 2006
Ken Buehler	June 30, 2006
Eric Kaiser	June 30, 2006
Pauline Olsen	June 30, 2006
Alan Johnson	June 30, 2008
 Executive Director	
Frederick Certano	
 Officers	
Chair	
Eric Kaiser	
Vice Chair	
Pauline Olsen	
Secretary	
John Goldfine	

\*Resigned October 15, 2004

This page was left blank intentionally.



This page was left blank intentionally.



PATRICIA ANDERSON  
STATE AUDITOR

# STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

SUITE 500  
525 PARK STREET  
SAINT PAUL, MN 55103-2139

(651) 296-2551 (Voice)  
(651) 296-4755 (Fax)  
state.auditor@state.mn.us (E-mail)  
1-800-627-3529 (Relay Service)

## INDEPENDENT AUDITOR'S REPORT

Mayor and City Council  
City of Duluth

Board of Directors  
Spirit Mountain Recreation Area Authority

We have audited the accompanying 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, 2005 and 2004. 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 at April 30, 2005 and 2004, and the changes in financial position and 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 management inquiries 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 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 financial statements of the Spirit Mountain Recreation Area Authority. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly presented in all material respects in relation to the financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 7, 2005, 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: November 7, 2005

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

This page was left blank intentionally.

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

**MANAGEMENT'S DISCUSSION AND ANALYSIS**

April 30, 2005

(Unaudited)

This section presents the Management's Discussion and Analysis (MD&A) of Spirit Mountain Recreation Area Authority's financial condition and activities for the fiscal year ended April 30, 2005. This information should be read in conjunction with the financial statements.

**FINANCIAL HIGHLIGHTS**

- Total net assets increased \$212,200, or nearly 7 percent, compared to fiscal year 2004. The increase was primarily due to current assets increasing \$132,101, or 18 percent.
- Operating income increased \$72,743, or 703 percent, compared to fiscal year 2004. The considerable increase was due primarily to an increase in revenue from charges for services, as well as a reduction in cost of goods sold.
- The City of Duluth issued a \$1,647,750 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 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, 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 that are 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 Recreation Area. The State Legislature itself conferred upon the Authority the power and responsibility for the operation and management of the Recreation 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 concerts, mountain bike races, banquets, and meetings.

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

	FY 2005	FY 2004	Change from 2004 to 2005		FY 2003
			Dollar	(%)	
Current and other assets	\$ 1,166,708	\$ 999,259	\$ 167,449	17	\$ 955,189
Capital assets	4,787,844	4,915,661	(127,817)	(3)	5,059,733
Total Assets	\$ 5,954,552	\$ 5,914,920	\$ 39,632	1	\$ 6,014,922
Current liabilities	\$ 788,947	\$ 870,627	\$ (81,680)	9	\$ 723,192
Long-term liabilities	1,760,990	1,851,878	(90,888)	(5)	1,987,756
Total Liabilities	\$ 2,549,937	\$ 2,722,505	\$ (172,568)	(6)	\$ 2,710,948
Net Assets					
Invested	\$ 2,963,292	\$ 2,774,302	\$ 188,990	7	\$ 2,906,220
Restricted	279,480	250,000	29,480	12	68,940
Unrestricted	161,843	168,113	(6,270)	(4)	328,814
Total Net Assets	\$ 3,404,615	\$ 3,192,415	\$ 212,200	7	\$ 3,303,974

As can be seen from the table, net assets increased \$212,200, to \$3,404,615 in 2005; up from \$3,192,415 in 2004. The increase in net assets was primarily due to a \$152,131 increase in cash and cash equivalents.

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

	FY 2005	FY 2004	Change from 2004 to 2005		FY 2003
			Dollar	(%)	
Operating revenues	\$ 3,494,563	\$ 3,317,737	\$ 176,826	5	\$ 3,300,957
Nonoperating revenues	231,626	10,294	221,332	2150	49,147
Total Revenues	\$ 3,726,189	\$ 3,328,031	\$ 398,158	12	\$ 3,350,104
Operating expenses	\$ 2,955,350	\$ 2,854,678	\$ 100,672	4	\$ 2,874,296
Nonoperating expenses	102,521	132,205	(29,684)	(22)	150,075
Depreciation/amortization	456,118	452,707	3,411	1	414,478
Total Expenses	\$ 3,513,989	\$ 3,439,590	\$ 74,399	2	\$ 3,438,849
Changes in Net Assets	\$ 212,200	\$ (111,559)	\$ 323,759	(290)	\$ (88,745)
Beginning Net Assets	3,192,415	3,303,974	(111,559)	(3)	3,392,719
Ending Net Assets	\$ 3,404,615	\$ 3,192,415	\$ 212,200	7	\$ 3,303,974

**Condensed Statements of Revenues, Expenses, and Changes in Net Assets  
(2005 Budget and Actual)**

	Actual	Budget	Budget to Actual Variance	Budget % Variance
Operating revenues	\$ 3,494,563	\$ 3,489,711	\$ 4,852	-
Nonoperating revenues	231,626	225,000	6,626	3
<b>Total Revenues</b>	<b>\$ 3,726,189</b>	<b>\$ 3,714,711</b>	<b>\$ 11,478</b>	<b>-</b>
Operating expenses	\$ 2,955,350	\$ 2,879,084	\$ 76,266	3
Nonoperating expenses	102,521	127,593	(25,072)	(20)
Depreciation/amortization	456,118	433,000	23,118	5
<b>Total Expenses</b>	<b>\$ 3,513,989</b>	<b>\$ 3,439,677</b>	<b>\$ 74,312</b>	<b>2</b>
Changes in Net Assets	\$ 212,200	\$ 275,034	\$ (62,834)	(23)
Beginning Net Assets	3,192,415	3,192,415	-	-
Ending Net Assets	<u>\$ 3,404,615</u>	<u>\$ 3,467,449</u>	<u>\$ (62,834)</u>	<u>(2)</u>

### Revenues

The Authority earns operating revenues in both winter and summer. Operating revenues increased to \$3,494,563 in 2005, up \$176,826 from 2004. Nonoperating revenues increased \$221,332 in 2005, due to the \$1,647,750 Gross Revenue Recreational Facility Bond issued and the City's pledge of \$225,000 per year in tourism tax. The Authority capitalized \$225,000 in 2005 facility improvements.

### Expenses

The Authority's operating expenses increased 4 percent over 2004, due primarily to the increase in personnel costs, as well as utility costs. Nonoperating expenses decreased 22 percent from 2004, due primarily to an 88 percent decrease in claims and judgments, as well as 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 \$4,852. The exceeded revenue was due primarily to the strength of the performance of campground personnel, as well as the organization of the food and beverage departments.

Operating expenses exceeded budgeted operating expenses by 3 percent, due primarily to personnel costs. Nonoperating expenses were almost 20 percent below budget. The decrease is due primarily to a reduction in claims and judgments.

## CAPITAL ASSETS

	<b>Capital Assets</b>			
	<u>FY 2005</u>	<u>FY 2004</u>	<u>Dollar Change</u>	<u>Total % Change</u>
Land	\$ 2,429,118	\$ 2,391,330	\$ 37,788	2
Equipment	6,744,963	6,691,454	53,509	1
Plant equipment	153,791	220,118	(66,327)	(30)
Building and improvements	3,465,395	3,216,639	248,756	8
Furniture and fixtures	197,013	236,891	(39,878)	(17)
Other capital assets	378,298	394,026	(15,728)	(4)
Work in progress	<u>100,746</u>	<u>30,007</u>	<u>70,739</u>	236
Subtotal	\$ 13,469,324	\$ 13,180,465	\$ 288,859	2
Less: accumulated depreciation	<u>(8,681,480)</u>	<u>(8,264,804)</u>	<u>(416,676)</u>	5
Net Property and Equipment	<u>\$ 4,787,844</u>	<u>\$ 4,915,661</u>	<u>\$ (127,817)</u>	(3)

By the end of fiscal year 2005, the Authority has invested \$13.469 million in capital assets. The \$288,860 increase in capital assets is primarily due to improvements made to the building, as well as equipment purchases for outside operations.

The Authority's five-year capital plan includes: continual upgrading of the snowmaking system, upgraded grooming equipment, air conditioning throughout the banquet spaces, roof replacement, deck repair and replacement, and new paint and carpeting throughout the chalet. Other planned improvements include an upgraded computer sales system to enable better quality controls and more timely reports, new rental equipment to replace aging equipment as needed, and remodeling of the Moosehead Saloon to accommodate summer restaurant business.

## DEBT ADMINISTRATION

	<b>Debt</b>			
	<u>FY 2005</u>	<u>FY 2004</u>	<u>Dollar Change</u>	<u>Total % Change</u>
Gas lease	\$ 97,046	\$ 118,359	\$ (21,313)	(18)
Groomer lease	213,083	277,839	(64,756)	(23)
Rental equipment lease	61,848	120,423	(58,575)	(49)
Lease/leaseback (revenue bonds)	<u>1,479,901</u>	<u>1,613,489</u>	<u>(133,588)</u>	(8)
Total Debt	<u>\$ 1,851,878</u>	<u>\$ 2,130,110</u>	<u>\$ (278,232)</u>	(13)

(Unaudited)

Page 8

At the end of fiscal year 2005, the Authority's outstanding debt decreased \$278,232 to \$1,851,878, down from \$2,130,110 at the end of fiscal year 2004. The decrease in outstanding debt is due primarily to the increase in payment principal being applied to the rental equipment lease. The payments for the rental equipment lease will be completed in fiscal year 2006.

## **ECONOMIC AND OTHER FACTORS**

The Authority considers many factors when setting the fiscal year 2006 budget, rates, and services. We continue to aggressively target to the Twin Cities area for both season pass holders and day skiers. These skiers provide a benefit to both Spirit Mountain and the Duluth hospitality industry, as they will 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 make us affordable to the local skiers as well. With affordability in mind, it was the decision of the Authority Board of Directors to retain the lower price structure enacted for the 2004-2005 ski season. We have added food and beverage outlets for the upcoming season to provide guests with more choices and easier access which will in turn enhance food and beverage revenues. We continue to actively promote and sell Spirit Mountain as a year-round venue, partnering with other entities to bring concerts and special events to the facility. Our banquet and meeting business continues to grow through our assertive sales efforts. The campground saw record revenues through increased promotion and continued upgrading of the sites and service building.

## **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.

## **FINANCIAL STATEMENTS**

This page was left blank intentionally.

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

**EXHIBIT A**

**COMPARATIVE STATEMENT OF NET ASSETS  
APRIL 30, 2005 AND 2004**

	<b>2005</b>	<b>2004</b>
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 722,629	\$ 599,978
Accounts receivable	63,408	40,565
Inventory	44,992	49,567
Prepaid items	21,593	30,411
<b>Total current assets</b>	<b>\$ 852,622</b>	<b>\$ 720,521</b>
<b>Noncurrent assets</b>		
Cash and cash equivalents - restricted for capital improvements	\$ 254,480	\$ 225,000
Planning and development costs - net of accumulated amortization	53,179	46,334
Debt issuance costs - net of accumulated amortization	6,427	7,404
<b>Total noncurrent assets, other than capital</b>	<b>\$ 314,086</b>	<b>\$ 278,738</b>
Capital assets	\$ 13,469,325	\$ 13,180,465
Less: allowance for depreciation	(8,681,481)	(8,264,804)
<b>Total capital assets - net of accumulated depreciation</b>	<b>\$ 4,787,844</b>	<b>\$ 4,915,661</b>
<b>Total noncurrent assets</b>	<b>\$ 5,101,930</b>	<b>\$ 5,194,399</b>
<b>Total Assets</b>	<b>\$ 5,954,552</b>	<b>\$ 5,914,920</b>
<b>Liabilities</b>		
<b>Current liabilities</b>		
Accounts payable	\$ 93,642	\$ 104,763
Due to City of Duluth	136,420	250,560
Due to other governments	2,853	2,217
Accrued salaries payable	17,528	35,179
Accrued vacation payable	51,271	50,116
Accrued interest payable	31,022	33,405
Leases payable	152,117	144,643
Revenue bonds payable	145,283	133,588
Deferred revenue	158,811	116,156
<b>Total current liabilities</b>	<b>\$ 788,947</b>	<b>\$ 870,627</b>
<b>Noncurrent liabilities</b>		
Due to City of Duluth	\$ 206,512	\$ -
Leases payable	219,860	371,977
Revenue bonds payable	1,334,618	1,479,901
<b>Total noncurrent liabilities</b>	<b>\$ 1,760,990</b>	<b>\$ 1,851,878</b>
<b>Total Liabilities</b>	<b>\$ 2,549,937</b>	<b>\$ 2,722,505</b>
<b>Net Assets</b>		
Invested in capital assets - net of related debt	\$ 2,963,292	\$ 2,774,302
Restricted for capital improvements	254,480	225,000
Restricted for workers' compensation claims	25,000	25,000
Unrestricted	161,843	168,113
<b>Total Net Assets</b>	<b>\$ 3,404,615</b>	<b>\$ 3,192,415</b>

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

Page 10

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

**EXHIBIT B**

**COMPARATIVE STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS  
YEARS ENDED APRIL 30, 2005 AND 2004**

	<b>2005</b>	<b>2004</b>
<b>Operating Revenues</b>		
Sales	\$ 759,393	\$ 751,695
Less: cost of goods sold	(278,458)	(302,871)
<b>Gross profit on sales</b>	<b>\$ 480,935</b>	<b>\$ 448,824</b>
Charges for services	2,998,252	2,842,285
Miscellaneous	15,376	26,628
<b>Total Operating Revenues</b>	<b>\$ 3,494,563</b>	<b>\$ 3,317,737</b>
<b>Operating Expenses</b>		
Personal services	\$ 1,625,417	\$ 1,576,710
Supplies	220,120	217,277
Utilities	327,488	306,897
Other services and charges	782,325	753,794
Amortization	24,410	24,411
Depreciation	431,708	428,296
<b>Total Operating Expenses</b>	<b>\$ 3,411,468</b>	<b>\$ 3,307,385</b>
<b>Operating Income (Loss)</b>	<b>\$ 83,095</b>	<b>\$ 10,352</b>
<b>Nonoperating Revenues (Expenses)</b>		
Earnings on investments	\$ 6,626	\$ 10,294
Tourism tax	225,000	-
Gain (loss) on sale or disposition of capital assets - net	(5,531)	(1,222)
Claims and judgments	(3,218)	(27,527)
Interest expense	(93,772)	(103,456)
<b>Total Nonoperating Revenues (Expenses)</b>	<b>\$ 129,105</b>	<b>\$ (121,911)</b>
<b>Change in Net Assets</b>	<b>\$ 212,200</b>	<b>\$ (111,559)</b>
<b>Net Assets - May 1</b>	<b>3,192,415</b>	<b>3,303,974</b>
<b>Net Assets - April 30</b>	<b>\$ 3,404,615</b>	<b>\$ 3,192,415</b>

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

**EXHIBIT C**

**COMPARATIVE STATEMENT OF CASH FLOWS  
YEARS ENDED APRIL 30, 2005 AND 2004**

	<b>2005</b>	<b>2004</b>
<b>Cash Flows from Operating Activities</b>		
Cash received from customers	\$ 3,716,880	\$ 3,545,753
Cash paid to suppliers	(1,464,760)	(1,524,875)
Cash paid to employees	(1,641,913)	(1,569,052)
Cash paid for claims and judgments	(3,218)	(71,042)
Other cash received	15,376	26,628
	<b>\$ 622,365</b>	<b>\$ 407,412</b>
<b>Cash Flows from Capital and Related Financing Activities</b>		
Transfer to trustee debt service accounts	\$ -	\$ 50,303
Capital lease payments	(157,879)	(226,910)
Acquisition and construction of fixed assets	(318,981)	(169,561)
	<b>\$ (476,860)</b>	<b>\$ (346,168)</b>
<b>Cash Flows from Investing Activities</b>		
Interest on investments	\$ 6,626	\$ 10,294
	<b>\$ 152,131</b>	<b>\$ 71,538</b>
<b>Net Increase (Decrease) in Cash and Cash Equivalents</b>	<b>\$ 152,131</b>	<b>\$ 71,538</b>
<b>Cash and Cash Equivalents - May 1</b>	<b>824,978</b>	<b>753,440</b>
<b>Cash and Cash Equivalents - April 30</b>	<b>\$ 977,109</b>	<b>824,978</b>
<b>Reconciliation of operating income (loss) to net cash provided by (used in) operating activities</b>		
Net operating income (loss)	\$ 83,095	\$ 10,352
Adjustments to reconcile net operating income (loss) to net cash provided by (used in) operating activities		
Depreciation	431,708	428,296
Amortization	24,410	24,411
Claims and judgments	(3,218)	(71,042)
Change in assets and liabilities		
Decrease (increase) in receivables	(22,843)	(2,102)
Decrease (increase) in inventory	4,575	(7,307)
Decrease (increase) in prepaid items	8,818	(18,820)
Increase (decrease) in accounts payable	69,661	20,927
Increase (decrease) in salaries payable	1,155	-
Increase (decrease) in vacations payable	(17,651)	-
Increase (decrease) in deferred revenue	42,655	22,697
	<b>\$ 622,365</b>	<b>\$ 407,412</b>

**Noncash Investing, Capital, and Financing Activities  
Fiscal Year Ended April 30, 2005**

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.

This page was left blank intentionally.

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

**NOTES TO THE FINANCIAL STATEMENTS  
AS OF AND FOR THE YEARS ENDED APRIL 30, 2005 AND 2004**

---

---

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**

---

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**

---

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, 2005 and 2004, follows:

	2005		Variance Favorable (Unfavorable)
	Budget	Actual	
Operating Revenues			
Sales	\$ 356,657	\$ 759,393	\$ 402,736
Less: cost of goods sold	(267,445)	(278,458)	(11,013)
Gross profit on sales	\$ 89,212	\$ 480,935	\$ 391,723
Charges for services	3,385,499	2,998,252	(387,247)
Miscellaneous	15,000	15,376	376
Total Operating Revenues	\$ 3,489,711	\$ 3,494,563	\$ 4,852

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

2. Detailed Notes

A. Budget (Continued)

	2005		Variance Favorable (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 (Expenses)			
Earnings on investments	\$ -	\$ 6,626	\$ 6,626
City of Duluth hotel-motel, 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 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>

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

2. Detailed Notes

A. Budget (Continued)

	2004		Variance Favorable (Unfavorable)
	Budget	Actual	
Operating Revenues			
Sales	\$ 725,000	\$ 751,695	\$ 26,695
Less: cost of goods sold	(282,139)	(302,871)	(20,732)
Gross profit on sales	\$ 442,861	\$ 448,824	\$ 5,963
Charges for services	2,832,870	2,842,285	9,415
Miscellaneous	32,000	26,628	(5,372)
Total Operating Revenues	\$ 3,307,731	\$ 3,317,737	\$ 10,006
Operating Expenses			
Personal services	\$ 1,490,149	\$ 1,576,710	\$ (86,561)
Supplies	195,335	217,277	(21,942)
Utilities	315,993	306,897	9,096
Other services and charges	811,492	753,794	57,698
Amortization	23,000	24,411	(1,411)
Depreciation	410,000	428,296	(18,296)
Total Operating Expenses	\$ 3,245,969	\$ 3,307,385	\$ (61,416)
Operating Income (Loss)	\$ 61,762	\$ 10,352	\$ (51,410)
Nonoperating Revenues (Expenses)			
Earnings on investments	\$ 10,000	\$ 10,294	\$ 294
City of Duluth hotel-motel, food, and beverage tax	75,000	-	(75,000)
Gain (loss) on disposal of assets	-	(1,222)	(1,222)
Claims and judgments	(34,000)	(27,527)	6,473
Interest expense	(100,886)	(103,456)	(2,570)
Total Nonoperating Revenues (Expenses)	\$ (49,886)	\$ (121,911)	\$ (72,025)
Change in Net Assets	\$ 11,876	\$ (111,559)	\$ (123,435)

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

2. Detailed Notes (Continued)

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.

Additional disclosures as required by GASB Statement No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements*, 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	
	2005	2004
City Treasurer	\$ 711,262	\$ 385,800
Money market savings	257,347	433,678
Petty cash and change funds	8,500	5,500
Total Cash and Cash Equivalents	\$ 977,109	\$ 824,978

C. Capital Assets

A summary of the changes in capital assets for the years ended April 30, 2005 and 2004, follows:

	Balance May 1, 2004	Additions	Deductions	Reclassification	Balance 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

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

2. Detailed Notes

C. Capital Assets (Continued)

	Balance May 1, 2004	Additions	Deductions	Reclassification	Balance April 30, 2005
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
	<u>10,759,128</u>	<u>29,612</u>	<u>30,122</u>	<u>180,842</u>	<u>10,939,460</u>
Total capital assets depreciated					
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
	<u>8,264,804</u>	<u>431,708</u>	<u>15,032</u>	<u>-</u>	<u>8,681,480</u>
Total accumulated depreciation					
Total capital assets depreciated, net	<u>\$ 2,494,324</u>	<u>\$ (402,096)</u>	<u>\$ 15,090</u>	<u>\$ 180,842</u>	<u>\$ 2,257,980</u>
Capital Assets, Net	<u>\$ 4,915,661</u>	<u>\$ (105,327)</u>	<u>\$ 22,490</u>	<u>\$ -</u>	<u>\$ 4,787,844</u>

	Balance May 1, 2003	Additions	Deductions	Reclassification	Balance April 30, 2004
Capital assets not depreciated					
Land and land improvements	\$ 2,391,330	\$ -	\$ -	\$ -	\$ 2,391,330
Construction in progress	68,606	380,445	-	(419,044)	30,007
	<u>2,459,936</u>	<u>380,445</u>	<u>-</u>	<u>(419,044)</u>	<u>2,421,337</u>
Total capital assets not depreciated					
Capital assets depreciated					
Buildings and structures	\$ 3,216,639	\$ -	\$ -	\$ -	\$ 3,216,639
Equipment	6,682,950	-	164,950	393,572	6,911,572
Furniture and fixtures	227,147	-	-	9,744	236,891
Other capital assets	378,298	-	-	15,728	394,026
	<u>10,505,034</u>	<u>-</u>	<u>164,950</u>	<u>419,044</u>	<u>10,759,128</u>
Total capital assets depreciated					

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

2. Detailed Notes

C. Capital Assets (Continued)

	<u>Balance May 1, 2003</u>	<u>Additions</u>	<u>Deductions</u>	<u>Reclassification</u>	<u>Balance April 30, 2004</u>
Less: accumulated depreciation for					
Buildings and structures	\$ 1,819,459	\$ 113,247	\$ -	\$ -	\$ 1,932,706
Equipment	5,692,169	295,015	68,729	-	5,918,455
Furniture and fixtures	165,668	5,055	-	-	170,723
Other capital assets	<u>227,941</u>	<u>14,979</u>	<u>-</u>	<u>-</u>	<u>242,920</u>
 Total accumulated depreciation	 <u>\$ 7,905,237</u>	 <u>\$ 428,296</u>	 <u>\$ 68,729</u>	 <u>\$ -</u>	 <u>\$ 8,264,804</u>
 Total capital assets depreciated, net	 <u>\$ 2,599,797</u>	 <u>\$ (428,296)</u>	 <u>\$ 96,221</u>	 <u>\$ 419,044</u>	 <u>\$ 2,494,324</u>
 Capital Assets, Net	 <u><u>\$ 5,059,733</u></u>	 <u><u>\$ (47,851)</u></u>	 <u><u>\$ 96,221</u></u>	 <u><u>\$ -</u></u>	 <u><u>\$ 4,915,661</u></u>

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, 2005 and 2004, is \$50,116 and \$44,505, 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.

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

---

2. Detailed Notes (Continued)

E. Due to City of Duluth

The amounts due to the City at April 30, 2005 and 2004, follows:

	2005	2004
General Fund - cost allocation plan	\$ 143,967	\$ 108,661
General Fund - sales tax	734	446
Self-Insurance Fund - insurance premiums	198,231	141,453
Total	\$ 342,932	\$ 250,560

In 2005, the City of Duluth and Spirit Mountain agreed on a repayment schedule. Of the \$342,932 owed to the City, \$136,420 is expected to be repaid within the next year. Payments will be made through 2010. A summary of the payments by year due follows:

2006	\$ 25,000
2007	45,500
2008	45,500
2009	45,500
2010	45,012
Total	\$ 206,512

F. Long-Term Debt

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

	2005
Bonds Payable - May 1	\$ 1,613,489
Issued	-
Payments	(152,594)
Add: current year amount of unamortized refinancing deferred loss	19,006
Bonds Payable - April 30	\$ 1,479,901
 Amount Due Within One Year	 \$ 145,283

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

---

2. Detailed Notes

F. Long-Term Debt (Continued)

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 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:

Fiscal Year Ended April 30	Principal	Interest
2006	\$ 159,538	\$ 65,462
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>\$ 1,494,156</u>	<u>\$ 300,826</u>

G. Capitalized Lease Obligations

Capitalized lease obligations consist of the following at April 30, 2005:

Type of Property	
Building improvements	\$ 210,021
Equipment	636,552
Less: accumulated amortization	<u>(482,125)</u>
Net Capital Lease Property	<u>\$ 364,448</u>

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

---

2. Detailed Notes

G. Capitalized Lease Obligations (Continued)

Minimum future lease payments follow:

<u>Fiscal Year Ended April 30</u>	<u>Principal</u>	<u>Interest</u>
2006	\$ 152,117	\$ 16,948
2007	94,676	10,071
2008	99,030	5,450
2009	26,154	1,373
Total	<u>\$ 371,977</u>	<u>\$ 33,842</u>

Capitalized lease obligations at April 30, 2005, 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. \$ 97,046

A \$347,541 lease purchase for two groomers and an attachment, dated September 30, 2003, due in periodic installments during the ski season through April 2008, with interest at 4.69 percent. 213,083

A \$215,261 lease purchase for rental equipment, dated November 29, 2002, due in periodic installments during the ski season through April 2006, with interest at 5.0 percent. 61,848

Total \$ 371,977

Current portion \$ 152,117

Long-term portion 219,860

Total \$ 371,977

H. Operating Lease

The Authority is obligated under an operating lease for office equipment. Lease expense for fiscal year 2005 and 2004, is \$2,040 for each year. Future minimum rental payments, which are not reported as liabilities in the financial statements at April 30, 2005, are \$1,870 due in fiscal year 2006.

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

---

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 and 25 percent of any profit.

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 provide certain employees with dental benefits, 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.

Employee dental benefits are provided through the City of Duluth Group Health Internal Service Fund at premium rates established by the City for all plan participants.

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.

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

---

3. Risk Management (Continued)

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 Authority's attorney determines settlement is probable, based on a case-by-case evaluation. The attorney has indicated there are \$12,500 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**

---

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 of service 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 web at [mnpera.org](http://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**

---

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 are required to contribute 9.10 and 5.10 percent, respectively, of their annual covered salary. The Authority is required to contribute the following percentages of annual covered payroll:

Public Employees Retirement Fund	
Basic Plan members	11.78%
Coordinated Plan members	5.53

The Authority's contributions for the years ending April 30, 2005, 2004, and 2003, were \$46,307, \$45,380, and \$47,564, respectively, equal to the contractually required contributions for each year as set by state statute.

This page was left blank intentionally.

**SUPPLEMENTARY INFORMATION**

This page was left blank intentionally.

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

**Schedule 1**

**COMPARATIVE STATEMENT OF OPERATING REVENUES  
YEARS ENDED APRIL 30, 2005 AND 2004**

	<u>2005</u>	<u>2004</u>
<b>Sales</b>		
Food	\$ 449,650	\$ 398,224
Liquor	189,953	185,555
Ski shop	119,790	131,549
Paint ball	-	36,367
Cost of goods sold	<u>(278,458)</u>	<u>(302,871)</u>
<b>Net sales</b>	<b><u>\$ 480,935</u></b>	<b><u>\$ 448,824</u></b>
<b>Charges for Services</b>		
Season pass	\$ 1,142,692	\$ 1,108,364
Daily lift tickets	1,112,886	1,084,757
Ski school and snow sports	109,478	106,280
Ski rental	248,975	211,379
Snowboard rental	75,496	65,086
Locker rental	26,823	26,962
Nordic tickets and rental	21,394	14,895
Paintball admissions	1,851	5,288
Snocross	69,606	73,796
Campground	66,069	50,410
Summer events	22,962	10,728
MountainVilla management fee	80,741	84,340
Marketing revenue	<u>19,279</u>	<u>-</u>
<b>Total charges for services</b>	<b><u>\$ 2,998,252</u></b>	<b><u>\$ 2,842,285</u></b>
<b>Miscellaneous</b>		
Other revenues	<u>\$ 15,376</u>	<u>\$ 26,628</u>
<b>Total Operating Revenues</b>	<b><u><u>\$ 3,494,563</u></u></b>	<b><u><u>\$ 3,317,737</u></u></b>

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

**Schedule 2**

**COMPARATIVE STATEMENT OF OPERATING EXPENSES  
YEARS ENDED APRIL 30, 2005 AND 2004**

	<b>2005</b>	<b>2004</b>
<b>Department</b>		
Food and beverage	\$ 221,105	\$ 176,658
Housekeeping	51,794	61,716
Rental	78,776	74,161
Ski shop	23,807	24,551
Campground	86,077	86,306
Paintball	-	41,866
Parking and lockers	6,200	8,090
Building and grounds	168,744	152,087
Snocross	82,260	81,389
Summer events	28,387	12,256
Ski school and snow sports center	95,047	90,359
Outside mountain operations	870,458	843,627
Nordic tickets and rentals	17,129	15,418
Ski patrol	5,886	7,702
Sales and marketing	448,507	399,549
Office administration	732,091	740,094
Mountain Villas	39,082	38,849
	<b>\$ 2,955,350</b>	<b>\$ 2,854,678</b>
<b>Total departmental costs</b>		
Amortization	24,410	24,411
Depreciation	431,708	428,296
	<b>\$ 3,411,468</b>	<b>\$ 3,307,385</b>
<b>Total Operating Expenses</b>		

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

Schedule 3

**STATEMENT OF CAPITAL IMPROVEMENTS  
YEAR ENDED APRIL 30, 2005**

	<b>Repair and Replacement Account Capital Improvements</b>	<b>Non-Repair and Replacement Account Capital Improvements</b>	<b>Total</b>
<b>Construction in Progress</b>			
Air conditioning	\$ 17,410	\$ 35,324	\$ 52,734
Roof	30,255	-	30,255
Windows	11,832	-	11,832
Chalet blacktop	3,000	7,000	10,000
Software upgrades	10,000	2,340	12,340
Banquet chairs	2,295	-	2,295
Maintainence building roof	19,932	-	19,932
Trucks	40,000	4,948	44,948
ATVs	13,723	-	13,723
Rental equipment	-	19,155	19,155
Snowmobile	12,073	-	12,073
Portable handle tow	12,500	586	13,086
Festival grounds	22,500	2,431	24,931
Gandy extension	-	6,038	6,038
Security system	-	10,806	10,806
Kit vent work	-	12,621	12,621
	<b>\$ 195,520</b>	<b>\$ 101,249</b>	<b>\$ 296,769</b>
<b>Buildings and Structures</b>			
Elevator			29,612
<b>Total Capital Improvements</b>			<b>\$ 326,381</b>
 <b><u>Repair and Replacement Account Summary</u></b>			
Net assets - restricted for capital improvements at April 30, 2004			\$ 225,000
2005 repair and replacement account deposits			225,000
Repair and replacement account capital improvements			(195,520)
<b>Net assets - restricted for capital improvements at April 30, 2005</b>			<b>\$ 254,480</b>

This page was left blank intentionally.



This page was left blank intentionally.

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

**Schedule 4**

SCHEDULE OF FINDINGS AND RECOMMENDATIONS  
FOR THE YEAR ENDED APRIL 30, 2005

**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. Effective March 2005, we have hired a Finance Director to oversee and assist the Finance Department. 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.*

ITEMS ARISING THIS YEAR

05-1 Ski Shop Inventory

The ski shop does not maintain a perpetual inventory system. An inventory count is done once a year at the end of the ski season. The ski shop does not have current inventory records available throughout the ski season; thus, there is an increased risk of missing inventory going undetected.

We recommend the Authority consider establishing a perpetual inventory system for ski shop merchandise. SIRIUSWARE should be reviewed to determine whether it has this capability. Monthly physical inventory counts conducted by non-ski shop staff should also be considered. The accounting department should compare the monthly physical inventory counts to the perpetual inventory records.

Client's Response:

*We have reviewed our current inventory practice in the ski shop and concur with the State Auditor's recommendation of a monthly physical inventory. In addition, we will institute periodic spot checks of certain inventory to assure adequate control. Personnel from the accounting office will assist with end-of-year inventory as another method of maintaining strict inventory control.*

*There has been no instance of improper inventory count, but we feel it makes good business sense to institute these policy changes and have begun taking monthly inventory already.*

05-2 Pay Adjustments for Employees with Missing Pay

The Authority does not have an adequate policy for paying adjustments to employees for missing payroll hours. While reviewing payroll, we found that if an employee's check were incorrect, the Payroll Manager would pay the employee with cash from the vault. The Payroll Manager would calculate the total gross pay that was missing from the paycheck, and the employee would receive 80 percent of that in the form of cash from the vault. The employee would sign a form that indicated they were paid incorrectly and were receiving cash for payroll corrections. The Executive Director had advised the Payroll Manager that all employees would have to wait until the following pay date to get the amount owed, but the payroll manager continued to pay employees with cash from the vault.

We recommend the Authority create and adhere to a strict policy for adjusting employees' pay that does not include making cash payments. Available options include holding pay adjustments until the following pay date, running an additional pay check through Pay Expert with additional charges, or running a manual check through Pay Expert which will import all data without printing a check, and the Authority can print a check through accounts payable. Employees should not be paid cash from the vault.

Client's Response:

*We have instituted a new policy for paying employees who miss payroll hours. Employees' missing pay will be run through accounts payable and a check printed and issued to the employees. The Payroll Manager does not have access to the vault.*

PREVIOUSLY REPORTED ITEMS RESOLVED

**Inadequate Control Policies and Procedures for Skiing-Related Sales (04-1)**

A review of skiing-related sales activity revealed the following:

- The number of voided transactions for lift tickets and equipment rental, as identified on the point-of-sale software system (SIRIUSWARE), did not agree to the number of voided transactions documented by physical evidence.
- Many voided transactions had no supporting documentation.
- The Detail Cash Drawer Report generated from SIRIUSWARE disclosed many voids were made as cash refunds.
- Some voided transactions could not readily be matched to a similar sale earlier in the day.
- A Visa sale appears to have been refunded both as a credit back to the Visa account and as a cash transaction.
- No supporting documentation for ski-shop returns was available for inspection.
- Procedures did not include a mechanism to adequately screen for unusual sales activity.
- Reports itemizing all sales transactions were not reviewed.
- Voids were not accounted for.

- The Authority had no written policy detailing the procedures to properly account for voids and refunds.
- The written accounting policies and procedures in existence did not reflect current practices.

Similar questionable activity identified by a more extensive internal review led to an investigation and two employees being charged with felony theft.

We recommended the Authority's management design and implement controls to prevent and detect fraud and ensure accountability for sales.

**Resolution**

The Authority now documents and reconciles voids. Returns and voids are initialed, and the reason for the void is listed. Returns require a manager's approval and signature and the customer's name, address, telephone number, and signature.

Policies and procedures have been updated and include the following:

- Employees have been limited to one per register.
- Cash counts are now performed with two employees present.
- Sale locations have been centralized, and surveillance cameras are present at each register.
- SIRIUSWARE is used for all sales except cross country, which will be implemented for the 2005 - 2006 ski season.
- Equipment rental forms are now pre-numbered, and the forms are kept in the vault. Vault personnel will release 25 forms at a time to cashier. Cashiers will verify the count and sign off on receiving rental forms.

**Paintball Operations (04-2)**

The cost of goods sold ratio for paintball sales (excluding field fees and rentals) was 97 percent for fiscal year 2004 operations.

**Resolution**

The Authority no longer has paintball operations. Paintball equipment was sold during the summer of 2004.

**II. OTHER FINDINGS AND RECOMMENDATIONS**

A. MINNESOTA LEGAL COMPLIANCE

ITEM ARISING THIS YEAR

05-3 In-Kind Benefits

During our audit, we noted two instances where employees hosted wedding receptions at Spirit Mountain and were not charged for room rental. They also received discounted prices on food and liquor.

We believe that waiving room rental charges and discounting food and liquor charges constitute an in-kind benefit for employees. The Minnesota Attorney General has consistently held that in-kind benefits need specific statutory authority in order to be provided to public employees. (Ops. Atty. Gen. 359b, October 24, 1989; 161b-12, January 24, 1989.) The Authority has no specific statutory authority to provide the above in-kind benefits.

We recommend the Authority discontinue this practice until it has specific statutory authority to provide in-kind benefits to employees.

Client's Response:

*We will no longer provide discounts to employees for events held at Spirit Mountain.*

B. MANAGEMENT PRACTICES

PREVIOUSLY REPORTED ITEM RESOLVED

**Potential Insurance Coverage Loss (02-3)**

As of April 30, 2004, the Authority owed the City of Duluth \$141,453 for insurance premiums dating back to January 1, 2001. In addition, the Authority owed the City \$90,059 for administrative services billed for the period January 1, 2001, through December 31, 2003.

We recommended the Authority obtain City approval of a proposed repayment schedule and also be aware of the potential for loss of insurance coverage due to late payment and the impact on its operations.

**Resolution**

The City of Duluth has approved a repayment schedule, and the Authority has begun making payments.



**STATE OF MINNESOTA**  
**OFFICE OF THE STATE AUDITOR**

SUITE 500  
525 PARK STREET  
SAINT PAUL, MN 55103-2139

(651) 296-2551 (Voice)  
(651) 296-4755 (Fax)  
state.auditor@state.mn.us (E-mail)  
1-800-627-3529 (Relay Service)

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, 2005, and have issued our report thereon dated November 7, 2005. 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 certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. 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. Reportable conditions are described in the accompanying Schedule of Findings and Recommendations as items 97-1, 05-1, and 05-2.

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 none of the reportable conditions indicated above is 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, except as described in the Schedule of Findings and Recommendations as item 05-3.

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: November 7, 2005