

# STATE OF MINNESOTA

## Office of the State Auditor



**Rebecca Otto**  
**State Auditor**

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

YEARS ENDED APRIL 30, 2017 AND 2016

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

The mission of the Office of the State Auditor is to oversee local government finances for Minnesota taxpayers by helping to ensure financial integrity and accountability in local governmental financial activities.

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 150 financial and compliance audits per year and has oversight responsibilities for over 3,300 local units of government throughout the state. The office currently maintains five divisions:

**Audit Practice** - conducts financial and legal compliance audits of 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 approximately 650 public pension funds; and

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

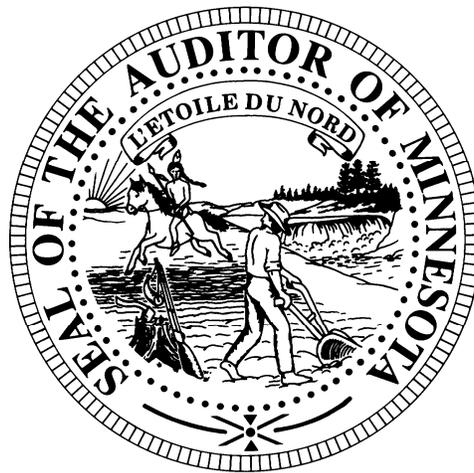
The State Auditor serves on the State Executive Council, State Board of Investment, Land Exchange Board, Public Employees Retirement Association Board, Minnesota Housing Finance Agency, and the Rural Finance Authority Board.

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

**Years Ended April 30, 2017 and 2016**



**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, 2017

	<u>Term Ending</u>
Directors	
David Kohlhaas	June 30, 2017
Dan O'Neill	June 30, 2017
Erik Viken	June 30, 2018
Kathryn Ferguson	June 30, 2018
Elaine Hansen	June 30, 2017
Jane Gilbert-Howard	June 30, 2018
Cory Salmela	June 30, 2017
Todd Torvinen	June 30, 2017
Executive Director	
Brandy Ream	
Officers	
Chair	
David Kohlhaas	
Vice Chair	
Cory Salmela	
Secretary	
Dan O'Neill	

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REBECCA OTTO  
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, Minnesota

Board of Directors  
Spirit Mountain Recreation Area Authority  
Duluth, Minnesota

### Report on the Financial Statements

We have audited the accompanying financial statements of the Spirit Mountain Recreation Area Authority, a component unit of the City of Duluth, Minnesota, as of and for the years ended April 30, 2017 and 2016, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, as listed in the table of contents.

#### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

#### *Auditor's Responsibility*

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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Authority's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### ***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, 2017 and 2016, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### ***Other Matters***

#### ***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Required Supplementary Information as listed in the table of contents be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

#### ***Supplementary Information***

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Spirit Mountain Recreation Area Authority's basic financial statements. The supplementary information as listed in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements. The supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial

statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated February 1, 2018, 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* in considering the Spirit Mountain Recreation Area Authority's internal control over financial reporting and compliance.

*/s/Rebecca Otto*

*/s/Greg Hierlinger*

REBECCA OTTO  
STATE AUDITOR

GREG HIERLINGER, CPA  
DEPUTY STATE AUDITOR

February 1, 2018

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

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

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
APRIL 30, 2017  
(Unaudited)**

This section presents management's analysis of the Authority's financial condition and activities for the fiscal year ended April 30, 2017. This information should be read in conjunction with the financial statements.

**FINANCIAL HIGHLIGHTS**

- Fiscal year 2017 proved to be difficult in relationship to weather. We opened for the winter season in mid-December, with 50 percent of terrain available. The warm weather and rain continued throughout most of the season.
- Wedding and banquet business continues to see an increase in revenue. This is due to alignment of pricing, update on contracts, and marketing efforts for exposure, which results in additional bookings.
- Mountain biking continues to increase in growth slightly. The campground is remaining a strong source of revenue for summer months.

**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, 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 position; a statement of revenues, expenses, and changes in net position; a statement of cash flows; and notes to the financial statements. The statement of net position presents the financial position of the Authority on a full accrual, economic resource basis. While the statement of net position provides information about the nature and amount of resources and obligations at year-end, the statement of revenues, expenses, and changes in net position presents the results of the business activities over the course of the

fiscal year and information as to how the net position changed during the year. All changes in net position 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 presents changes in cash and cash equivalents, resulting from operating, capital, 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 nine community members to serve on the Board of Directors that oversees the Authority.

The main forms of recreation provided to both local residents and visitors is skiing, alpine, Nordic, snowboarding, and in fiscal year 2012, added in the Timber Twister Alpine Coaster was joined by the new year-round Timber Flyer Zip Line, a 9-hole miniature golf course, and a new snow tubing park, now branded as the Spirit Mountain Adventure Park. The Authority also hosts the world's largest on-snow Snocross race, the Duluth National, over Thanksgiving weekend. Summertime activities include special events, banquets, meetings, corporate events, mountain biking, and camping, with banquets becoming an even larger business for the Authority, with wedding receptions and corporate/other events. In the summer of 2012, the Authority installed a new four-place detachable lift to replace a similar lift and added a new chalet with a bar and restaurant and a new parking lot at the Grand Avenue entrance. During 2014, two mountain bike trails were constructed, which added lift access mountain biking to the list of summer attractions and further established Spirit Mountain as a year-round recreational facility. The Authority currently has eight mountain bike trails and a skills park.

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 Statements of Net Position

	FY 2017	FY 2016	Change from 2016 to 2017		FY 2015
			Dollar	Percent (%)	
Current and other assets	\$ 512,380	\$ 780,050	\$ (267,670)	(34)	\$ 1,248,835
Capital assets	19,065,345	19,748,423	(683,078)	(3)	14,388,502
<b>Total Assets</b>	<b>\$ 19,577,725</b>	<b>\$ 20,528,473</b>	<b>\$ (950,748)</b>	<b>(5)</b>	<b>\$ 15,637,337</b>
Deferred outflows of resources					
Deferred pension outflows	\$ 941,501	\$ 341,888	\$ 599,613	175	\$ 278,000
Current liabilities	\$ 2,357,934	\$ 2,298,383	\$ 59,551	3	\$ 2,711,138
Long-term liabilities	3,320,571	3,034,754	285,817	9	3,294,425
<b>Total Liabilities</b>	<b>\$ 5,678,505</b>	<b>\$ 5,333,137</b>	<b>\$ 345,368</b>	<b>6</b>	<b>\$ 6,005,563</b>
Deferred inflows of resources					
Deferred pension inflows	\$ 583,130	\$ 460,187	\$ 122,943	27	\$ 401,086
Net Position					
Net investment in capital assets	\$ 17,537,746	\$ 17,938,270	\$ (400,524)	(2)	\$ 12,198,983
Unrestricted	(3,280,155)	(2,861,233)	(418,922)	15	(2,690,295)
<b>Total Net Position</b>	<b>\$ 14,257,591</b>	<b>\$ 15,077,037</b>	<b>\$ (819,446)</b>	<b>(5)</b>	<b>\$ 9,508,688</b>

**Condensed Statements of Revenues, Expenses, and Changes in Net Position  
(Comparative Amounts)**

	FY 2017	FY 2016	Change from 2016 to 2017		FY 2015
			Dollar	Percent (%)	
Operating revenues	\$ 4,315,778	\$ 4,265,806	\$ 49,972	1	\$ 4,316,070
Nonoperating revenues	395,700	1,408,569	(1,012,869)	(72)	748,514
Contributions from City of Duluth	47,367	5,192,543	(5,145,176)	(99)	725,848
<b>Total Revenues</b>	<b>\$ 4,758,845</b>	<b>\$ 10,866,918</b>	<b>\$ (6,108,073)</b>	<b>(56)</b>	<b>\$ 5,790,432</b>
Operating expenses	\$ 4,446,715	\$ 4,191,494	\$ 255,221	6	\$ 4,311,916
Nonoperating expenses	52,886	75,285	(22,399)	(30)	84,386
Depreciation/amortization	1,078,690	1,031,790	46,900	5	707,976
<b>Total Expenses</b>	<b>\$ 5,578,291</b>	<b>\$ 5,298,569</b>	<b>\$ 279,722</b>	<b>5</b>	<b>\$ 5,104,278</b>
Changes in Net Position	\$ (819,446)	\$ 5,568,349	\$ (6,387,795)	(115)	\$ 686,154
Beginning Net Position	15,077,037	9,508,688	5,568,349	59	8,822,534
Ending Net Position	<u>\$ 14,257,591</u>	<u>\$ 15,077,037</u>	<u>\$ (819,446)</u>	<u>(5)</u>	<u>\$ 9,508,688</u>

**Condensed Statement of Revenues, Expenses, and Change in Net Position  
(2017 Budget and Actual)**

	Actual	Budget	Budget to Actual Variance	Budget % Variance
Operating revenues	\$ 4,315,778	\$ 4,664,409	\$ (348,631)	(7)
Nonoperating revenues	395,700	395,700	-	-
Contributions from City of Duluth	47,367	-	47,367	100
<b>Total Revenues</b>	<b>\$ 4,758,845</b>	<b>\$ 5,060,109</b>	<b>\$ (301,264)</b>	<b>(6)</b>
Operating expenses	\$ 4,446,715	\$ 4,075,005	\$ (371,710)	(9)
Nonoperating expenses	52,886	92,892	40,006	43
Depreciation/amortization	1,078,690	859,200	(219,490)	(26)
<b>Total Expenses</b>	<b>\$ 5,578,291</b>	<b>\$ 5,027,097</b>	<b>\$ (551,194)</b>	<b>(11)</b>
Changes in Net Position	\$ (819,446)	\$ 33,012	\$ (852,458)	(2,582)
Beginning Net Position	15,077,037	15,077,037	-	-
Ending Net Position	<u>\$ 14,257,591</u>	<u>\$ 15,110,049</u>	<u>\$ (852,458)</u>	<u>(6)</u>

## Revenues

The Authority earns operating revenues in both winter and summer. Operating revenues increased \$49,972, or 1 percent, in 2017 compared to 2016. Nonoperating revenues and contributions decreased by \$6,158,045, or 93 percent, in 2017 compared to 2016 due to the completion of the water project.

## Expenses

The Authority's operating expenses increased \$302,121, or 6 percent, from 2016 due mainly to an increase in personal service costs.

## Budgetary Highlights

The Authority creates an annual operating budget, which includes proposed expenses and 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 were \$348,631, or 7 percent, below budget due mainly to season passes, daily lift tickets, and Grand Avenue Chalet sales being lower than anticipated.

## CAPITAL ASSETS

	FY 2017	FY 2016	Change	
			Dollar	Percent (%)
Land and land improvements	\$ 2,553,244	\$ 2,553,244	\$ -	-
Equipment	11,744,112	11,442,009	302,103	3
Plant equipment	984,081	958,481	25,600	3
Buildings and structures	14,923,939	14,908,536	15,403	1
Furniture and fixtures	259,831	259,831	-	-
Other capital assets	843,955	802,903	41,052	5
Construction in progress	500,489	509,885	(9,396)	(2)
Subtotal	\$ 31,809,651	\$ 31,434,889	\$ 374,762	1
Less: accumulated depreciation	(12,744,306)	(11,686,466)	(1,057,840)	(9)
Total Capital Assets, Net	<u>\$ 19,065,345</u>	<u>\$ 19,748,423</u>	<u>\$ (683,078)</u>	(3)

The Authority’s ongoing capital plan improvements are made with the long-term goals of the Spirit Mountain Master Plan in mind. Building new attractions is the keystone to the area becoming a true four-season recreation venue. As always, we continue to seek ways to streamline the operation, find efficiencies, and provide the best possible guest experience.

**Debt Administration**

	FY 2017	FY 2016	Change	
			Dollar	Percent (%)
Alpine Coaster lease	\$ 1,401,446	\$ 1,551,723	\$ (150,277)	(10)
Groomer leases	126,153	237,789	(111,636)	(47)
Zip/Tube/Golf lease	-	20,641	(20,641)	(100)
<b>Total Debt</b>	<b>\$ 1,527,599</b>	<b>\$ 1,810,153</b>	<b>\$ (282,554)</b>	<b>(16)</b>

During fiscal year 2017, the Authority’s outstanding debt decreased \$282,554.

**ECONOMIC AND OTHER FACTORS**

The Authority must consider many factors when setting the fiscal year budgets. Spirit Mountain is not immune from lessened consumer confidence and shrinking spending habits; additionally, weather challenges hamper the consumers’ excitement for winter sporting activities. The entire pricing structure on tickets and season passes has been evaluated and restructured. We continue to offer an affordable season pass that has value to our operation. Our pricing for walk-up tickets was reviewed and changed as well. The Adventure Park is open seasonally, and we have had strong attendance during the winter season.

We have continued to add attractions to complement the coaster, such as mountain bike trails, and feel the key to our growth and success will be more year-round activities that appeal to families. The Adventure Park has increased our visibility, as new visitors to the resort are exposed to the many opportunities available for winter recreation, camping, lodging at the Villas, and banquets.

The banquet business continues to be a strong revenue source for Spirit Mountain. However, after a detailed analysis of our pricing structure, it was found that our pricing was not reflective of the cost of business, and we were not seeing the revenues Spirit Mountain had anticipated. With this stated, all pricing for banquets has been adjusted, and significant changes will come forth in 2018.

We look forward to an improved economy, additional four-season recreational enhancements, and a successful winter and summer season.

## **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.

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## **BASIC FINANCIAL STATEMENTS**

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

**EXHIBIT 1**

**COMPARATIVE STATEMENT OF NET POSITION  
APRIL 30, 2017 AND 2016**

	<b>2017</b>	<b>2016</b>
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 335,637	\$ 571,469
Accounts receivable	16,833	2,328
Due from City of Duluth	-	47,367
Prepaid insurance	-	13,247
Inventory	112,448	75,941
	<b>\$ 464,918</b>	<b>\$ 710,352</b>
<b>Noncurrent assets</b>		
Planning and development costs - net of accumulated amortization	<b>\$ 47,462</b>	<b>\$ 69,698</b>
Capital assets		
Non-depreciable	\$ 3,053,733	\$ 3,063,129
Depreciable	28,755,918	28,371,760
Less: accumulated depreciation	(12,744,306)	(11,686,466)
	<b>\$ 19,065,345</b>	<b>\$ 19,748,423</b>
<b>Total capital assets - net of accumulated depreciation</b>	<b>\$ 19,065,345</b>	<b>\$ 19,748,423</b>
<b>Total noncurrent assets</b>	<b>\$ 19,112,807</b>	<b>\$ 19,818,121</b>
<b>Total Assets</b>	<b>\$ 19,577,725</b>	<b>\$ 20,528,473</b>
<b>Deferred Outflows of Resources</b>		
Deferred pension outflows	<b>\$ 941,501</b>	<b>\$ 341,888</b>
<b>Liabilities</b>		
<b>Current liabilities</b>		
Accounts payable	\$ 144,681	\$ 118,681
Contracts payable	-	47,367
Due to City of Duluth	1,207,248	1,207,035
Due to other governments	21,327	23,630
Accrued salaries payable	73,216	30,236
Accrued vacation payable	99,314	87,700
Accrued interest payable	3,273	5,187
Leases payable	228,785	273,147
Unearned revenue	580,090	505,400
	<b>\$ 2,357,934</b>	<b>\$ 2,298,383</b>
<b>Total current liabilities</b>	<b>\$ 2,357,934</b>	<b>\$ 2,298,383</b>
<b>Noncurrent liabilities</b>		
Leases payable	\$ 1,298,814	\$ 1,537,006
Net pension liability	2,021,757	1,497,748
	<b>\$ 3,320,571</b>	<b>\$ 3,034,754</b>
<b>Total noncurrent liabilities</b>	<b>\$ 3,320,571</b>	<b>\$ 3,034,754</b>
<b>Total Liabilities</b>	<b>\$ 5,678,505</b>	<b>\$ 5,333,137</b>

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

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

***EXHIBIT 1  
(Continued)***

**COMPARATIVE STATEMENT OF NET POSITION  
APRIL 30, 2017 AND 2016**

	<b>2017</b>	<b>2016</b>
<b>Deferred Inflows of Resources</b>		
Deferred pension inflows	<b>\$ 583,130</b>	<b>\$ 460,187</b>
<b>Net Position</b>		
Net investment in capital assets	\$ 17,537,746	\$ 17,938,270
Unrestricted	(3,280,155)	(2,861,233)
<b>Total Net Position</b>	<b>\$ 14,257,591</b>	<b>\$ 15,077,037</b>

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

**EXHIBIT 2**

**COMPARATIVE STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION  
FOR THE YEARS ENDED APRIL 30, 2017 AND 2016**

	<b>2017</b>	<b>2016</b>
<b>Operating Revenues</b>		
Sales	\$ 1,113,595	\$ 1,122,683
Less: cost of goods sold	(403,640)	(436,984)
<b>Gross profit on sales</b>	<b>\$ 709,955</b>	<b>\$ 685,699</b>
Charges for services	3,458,214	3,476,905
Miscellaneous	147,609	103,202
<b>Total Operating Revenues</b>	<b>\$ 4,315,778</b>	<b>\$ 4,265,806</b>
<b>Operating Expenses</b>		
Personal services	\$ 2,791,831	\$ 2,476,999
Supplies	242,467	279,167
Utilities	401,467	399,498
Other services and charges	1,010,950	1,035,830
Amortization	20,850	21,097
Depreciation	1,057,840	1,010,693
<b>Total Operating Expenses</b>	<b>\$ 5,525,405</b>	<b>\$ 5,223,284</b>
<b>Operating Income (Loss)</b>	<b>\$ (1,209,627)</b>	<b>\$ (957,478)</b>
<b>Nonoperating Revenues (Expenses)</b>		
Grant revenue	\$ -	\$ 962,869
Tourism tax	395,700	445,700
Interest expense	(52,886)	(75,285)
<b>Total Nonoperating Revenues (Expenses)</b>	<b>\$ 342,814</b>	<b>\$ 1,333,284</b>
<b>Income (loss) before contributions</b>	<b>\$ (866,813)</b>	<b>\$ 375,806</b>
Capital contributions from City of Duluth	47,367	5,192,543
<b>Changes in Net Position</b>	<b>\$ (819,446)</b>	<b>\$ 5,568,349</b>
<b>Net Position - May 1</b>	<b>15,077,037</b>	<b>9,508,688</b>
<b>Net Position - April 30</b>	<b>\$ 14,257,591</b>	<b>\$ 15,077,037</b>

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

**EXHIBIT 3**

**COMPARATIVE STATEMENT OF CASH FLOWS  
FOR THE YEARS ENDED APRIL 30, 2017 AND 2016**

	<b>2017</b>	<b>2016</b>
<b>Cash Flows from Operating Activities</b>		
Cash received from customers	\$ 4,636,984	\$ 4,900,917
Cash paid to suppliers	(2,062,864)	(2,131,874)
Cash paid to employees	(2,689,898)	(2,461,883)
Other cash received	147,609	103,202
	<b>\$ 31,831</b>	<b>\$ 410,362</b>
<b>Cash Flows from Capital and Related Financing Activities</b>		
Capital grants	\$ -	\$ 962,869
Capital contributions from City of Duluth	47,367	5,192,543
City of Duluth hotel/motel taxes	395,700	445,700
Capital lease payments	(335,968)	(455,758)
Acquisition and construction of capital assets	(374,762)	(6,318,174)
	<b>\$ (267,663)</b>	<b>\$ (172,820)</b>
<b>Net cash provided by (used in) operating activities</b>	<b>\$ 31,831</b>	<b>\$ 410,362</b>
<b>Net Increase (Decrease) in Cash and Cash Equivalents</b>	<b>\$ (235,832)</b>	<b>\$ 237,542</b>
<b>Cash and Cash Equivalents - May 1</b>	<b>571,469</b>	<b>333,927</b>
<b>Cash and Cash Equivalents - April 30</b>	<b>\$ 335,637</b>	<b>\$ 571,469</b>
<b>Reconciliation of operating income (loss) to net cash provided by (used in) operating activities</b>		
Net operating income (loss)	<b>\$ (1,209,627)</b>	<b>\$ (957,478)</b>
<b>Adjustments to reconcile net operating income (loss) to net cash provided by (used in) operating activities</b>		
Depreciation	1,057,840	1,010,693
Amortization	20,850	21,097
Change in assets and liabilities		
Decrease (increase) in receivables	(14,505)	75,922
Decrease (increase) in prepaid insurance	13,247	78,780
Decrease (increase) in inventory	(36,507)	13,108
Increase (decrease) in payables	23,910	(2,922)
Increase (decrease) in accrued salaries payable	42,980	(1,649)
Increase (decrease) in accrued vacation payable	11,614	8,214
Increase (decrease) in deferred pension outflows	(599,613)	(63,888)
Increase (decrease) in deferred pension inflows	122,943	59,101
Increase (decrease) in net pension liability	524,009	13,338
Increase (decrease) in unearned revenue	74,690	156,046
	<b>\$ 31,831</b>	<b>\$ 410,362</b>
<b>Net Cash Provided by (Used in) Operating Activities</b>	<b>\$ 31,831</b>	<b>\$ 410,362</b>

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

NOTES TO THE FINANCIAL STATEMENTS  
AS OF AND FOR THE YEARS ENDED APRIL 30, 2017 AND 2016

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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 nine 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 with accounting principles generally accepted in the United States of America.

A. Financial Reporting Entity

The Authority is a discretely presented component unit of the City of Duluth reporting entity and, therefore, is included in the City's Comprehensive Annual Financial Report because of the significance of its operations and financial relationships with the City.

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 and then unrestricted resources as 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 full accrual, economic resource basis of accounting. Revenues are recognized when they are earned, and expenses are recognized when they are incurred, regardless of the timing of cash flows.

D. Assets, Liabilities, Deferred Outflows/Inflows of Resources, and Net Position

1. Cash and Cash Equivalents

Cash and cash equivalents consist of cash and investments held by the Treasurer of the City of Duluth. Investments are stated at fair value, and investment revenue is recorded as it is earned. 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.

2. Inventories

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

3. Capital Assets

Purchased or constructed capital assets are stated at cost. Donated capital assets are recorded at acquisition value on the date of donation. 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 capital assets	2 to 40 years

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

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1. Summary of Significant Accounting Policies

D. Assets, Liabilities, Deferred Outflows/Inflows of Resources, and Net Position  
(Continued)

4. Accrued Vacation Payable

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.

5. Unearned Revenue

Unredeemed passes and gift certificates are reported as unearned revenue until they are earned.

6. Deferred Outflows/Inflows of Resources

In addition to assets, the statement of financial position reports a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period(s) and will not be recognized as an outflow of resources (expense) until then. Currently, the Authority has one item, deferred pension outflows, that qualifies for reporting in this category. This amount consists of pension plan contributions paid subsequent to the measurement date, differences between projected and actual earnings on pension plan investments, changes in actuarial assumptions, and differences between expected and actual economic experience.

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

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1. Summary of Significant Accounting Policies

D. Assets, Liabilities, Deferred Outflows/Inflows of Resources, and Net Position

6. Deferred Outflows/Inflows of Resources (Continued)

In addition to liabilities, the statement of financial position reports a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The Authority has only one type of item, deferred pension inflows, that qualifies for reporting in this category. This amount consists of differences between expected and actual pension plan economic experience, pension plan changes in proportionate share, and differences between projected and actual earnings on pension plan investments.

7. Pension Plan

For purposes of measuring the net pension liability, deferred outflows/inflows of resources, and pension expense, information about the fiduciary net position of the Public Employees Retirement Association (PERA) and additions to/deductions from PERA's fiduciary net position have been determined on the same basis as they are reported by PERA, except that PERA's fiscal year-end is June 30. For this purpose, plan contributions are recognized as of employer payroll paid dates and benefit payments and refunds are recognized when due and payable in accordance with the benefit terms. Plan investments are reported at fair value.

8. Classification of Net Position

Net position is classified in the following categories:

Net investment in capital assets - the amount of net position representing capital assets, net of accumulated depreciation, and reduced by outstanding debt, if any, attributed to the acquisition, construction, or improvement of the assets.

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

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1. Summary of Significant Accounting Policies

D. Assets, Liabilities, Deferred Outflows/Inflows of Resources, and Net Position

8. Classification of Net Position (Continued)

Restricted net position - the amount of net position for which external restrictions have been imposed by creditors, grantors, contributors, or laws or constitutional provisions or enabling legislation.

Unrestricted net position - the amount of net position that does not meet the definition of restricted or net investment in capital assets.

E. Trade-Offs

The Authority issues 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 accounting principles generally accepted in the United States of America requires management to make certain estimates and assumptions that affect the reported amounts of assets, deferred outflows or resources, liabilities, and deferred inflows of resources; 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.

G. Reclassifications

Certain items on the Statement of Revenues, Expenses, and Changes in Net Position have been reclassified from the previous years; however, total revenue, expenses, and net position were unchanged.

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

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, 2017 and 2016 follows:

	2017		
	Budget	Actual	Variance
Operating Revenues			
Sales	\$ 1,035,508	\$ 1,113,595	\$ 78,087
Less: cost of goods sold	(519,739)	(403,640)	116,099
Gross profit on sales	\$ 515,769	\$ 709,955	\$ 194,186
Charges for services	4,125,821	3,458,214	(667,607)
Miscellaneous	22,819	147,609	124,790
Total Operating Revenues	\$ 4,664,409	\$ 4,315,778	\$ (348,631)
Operating Expenses			
Personal services	\$ 2,600,018	\$ 2,791,831	\$ (191,813)
Supplies	293,979	242,467	51,512
Utilities	358,661	401,467	(42,806)
Other services and charges	822,347	1,010,950	(188,603)
Amortization	23,400	20,850	2,550
Depreciation	835,800	1,057,840	(222,040)
Total Operating Expenses	\$ 4,934,205	\$ 5,525,405	\$ (591,200)
Operating Income (Loss)	\$ (269,796)	\$ (1,209,627)	\$ (939,831)
Nonoperating Revenues (Expenses)			
Tourism tax	\$ 395,700	\$ 395,700	\$ -
Interest expense	(92,892)	(52,886)	40,006
Total Nonoperating Revenues (Expenses)	\$ 302,808	\$ 342,814	\$ 40,006
Income (loss) before contributions	\$ 33,012	\$ (866,813)	\$ (899,825)
Capital contributions from City of Duluth	-	47,367	47,367
Change in Net Position	\$ 33,012	\$ (819,446)	\$ (852,458)

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

2. Detailed Notes

A. Budget (Continued)

	2016		
	Budget	Actual	Variance
Operating Revenues			
Sales	\$ 965,317	\$ 1,122,683	\$ 157,366
Less: cost of goods sold	(528,272)	(436,984)	91,288
Gross profit on sales	\$ 437,045	\$ 685,699	\$ 248,654
Charges for services	4,271,971	3,476,905	(795,066)
Miscellaneous	-	103,202	103,202
Total Operating Revenues	\$ 4,709,016	\$ 4,265,806	\$ (443,210)
Operating Expenses			
Personal services	\$ 2,680,086	\$ 2,476,999	\$ 203,087
Supplies	446,947	279,167	167,780
Utilities	374,000	399,498	(25,498)
Other services and charges	575,762	1,035,830	(460,068)
Amortization	22,320	21,097	1,223
Depreciation	775,200	1,010,693	(235,493)
Total Operating Expenses	\$ 4,874,315	\$ 5,223,284	\$ (348,969)
Operating Income (Loss)	\$ (165,299)	\$ (957,478)	\$ (792,179)
Nonoperating Revenues (Expenses)			
Grant revenue	\$ -	\$ 962,869	\$ 962,869
Tourism tax	97,136	445,700	348,564
Interest expense	(92,892)	(75,285)	17,607
Total Nonoperating Revenues (Expenses)	\$ 4,244	\$ 1,333,284	\$ 1,329,040
Income (loss) before contributions	\$ (161,055)	\$ 375,806	\$ 536,861
Capital contributions from City of Duluth	-	5,192,543	5,192,543
Change in Net Position	\$ (161,055)	\$ 5,568,349	\$ 5,729,404

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

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2. Detailed Notes (Continued)

B. Deposits

The Treasurer of the City of Duluth is designated by Minn. Laws 1973, ch. 327, as Treasurer of the Authority. Authority deposits are pooled with all other City deposits. The City Treasurer is authorized by Minn. Stat. §§ 118A.02 and 118A.04 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.

The Authority invests funds in the City of Duluth's investment pool. The fair value of the investment is the fair value per share of the underlying portfolio. The Authority invests in this pool for the purpose of joint investment with the City in order to enhance investment earnings. There are no redemption limitations. The types of investment securities available to the City of Duluth Treasurer are authorized by Minn. Stat. §§ 118A.04 and 118A.05.

Additional disclosures required by Governmental Accounting Standards Board 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	
	<u>2017</u>	<u>2016</u>
City Treasurer	\$ 291,392	\$ 529,224
Petty cash and change funds	<u>44,245</u>	<u>42,245</u>
Total Cash and Cash Equivalents	<u>\$ 335,637</u>	<u>\$ 571,469</u>

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

2. Detailed Notes (Continued)

C. Capital Assets

A summary of the changes in capital assets for the years ended April 30, 2017 and 2016, follows:

	Balance May 1, 2016	Additions	Deductions	Balance April 30, 2017
Capital assets not depreciated				
Land and land improvements	\$ 2,553,244	\$ -	\$ -	\$ 2,553,244
Construction in progress	509,885	799	10,195	500,489
<b>Total capital assets not depreciated</b>	<b>\$ 3,063,129</b>	<b>\$ 799</b>	<b>\$ 10,195</b>	<b>\$ 3,053,733</b>
Capital assets depreciated				
Buildings and structures	\$ 14,908,536	\$ 15,403	\$ -	\$ 14,923,939
Equipment	12,400,490	327,703	-	12,728,193
Furniture and fixtures	259,831	-	-	259,831
Other capital assets	802,903	41,052	-	843,955
<b>Total capital assets depreciated</b>	<b>\$ 28,371,760</b>	<b>\$ 384,158</b>	<b>\$ -</b>	<b>\$ 28,755,918</b>
Less: accumulated depreciation for				
Buildings and structures	\$ 4,293,020	\$ 519,678	\$ -	\$ 4,812,698
Equipment	6,587,520	506,912	-	7,094,432
Furniture and fixtures	254,657	2,637	-	257,294
Other capital assets	551,269	28,613	-	579,882
<b>Total accumulated depreciation</b>	<b>\$ 11,686,466</b>	<b>\$ 1,057,840</b>	<b>\$ -</b>	<b>\$ 12,744,306</b>
<b>Total capital assets depreciated, net</b>	<b>\$ 16,685,294</b>	<b>\$ (673,682)</b>	<b>\$ -</b>	<b>\$ 16,011,612</b>
<b>Capital Assets, Net</b>	<b>\$ 19,748,423</b>	<b>\$ (672,883)</b>	<b>\$ 10,195</b>	<b>\$ 19,065,345</b>

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

2. Detailed Notes

C. Capital Assets (Continued)

	Balance May 1, 2015	Additions	Deductions	Balance April 30, 2016
Capital assets not depreciated				
Land and land improvements	\$ 2,553,244	\$ -	\$ -	\$ 2,553,244
Construction in progress	1,252,661	6,192,324	6,935,100	509,885
 Total capital assets not depreciated	 \$ 3,805,905	 \$ 6,192,324	 \$ 6,935,100	 \$ 3,063,129
Capital assets depreciated				
Buildings and structures	\$ 7,966,219	\$ 6,942,317	\$ -	\$ 14,908,536
Equipment	12,232,573	167,917	-	12,400,490
Furniture and fixtures	256,675	3,156	-	259,831
Other capital assets	802,903	-	-	802,903
 Total capital assets depreciated	 \$ 21,258,370	 \$ 7,113,390	 \$ -	 \$ 28,371,760
Less: accumulated depreciation for				
Buildings and structures	\$ 3,755,651	\$ 537,369	\$ -	\$ 4,293,020
Equipment	6,148,071	439,449	-	6,587,520
Furniture and fixtures	250,324	4,333	-	254,657
Other capital assets	521,727	29,542	-	551,269
 Total accumulated depreciation	 \$ 10,675,773	 \$ 1,010,693	 \$ -	 \$ 11,686,466
 Total capital assets depreciated, net	 \$ 10,582,597	 \$ 6,102,697	 \$ -	 \$ 16,685,294
 Capital Assets, Net	 \$ 14,388,502	 \$ 12,295,021	 \$ 6,935,100	 \$ 19,748,423

D. Vacation, Sick Leave, and Compensatory Time

Unpaid vacation pay earned as of April 30, 2017 and 2016, is \$99,314 and \$87,700, 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**

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2. Detailed Notes (Continued)

E. Due to City of Duluth

The amounts due to the City at April 30, 2017 and 2016, follow:

	2017	2016
General Fund - sales tax	\$ 7,248	\$ 7,035
General Fund - line of credit	1,200,000	1,200,000
Total	\$ 1,207,248	\$ 1,207,035

The City of Duluth extends the Authority a line of credit each year to assist in the management of cash flow within the budget approved. The Spirit Mountain Recreation Area Authority is allowed to draw upon the line of credit as needed to assist in the management of cash flows. The amounts withdrawn need to be repaid in full at least once per calendar year.

F. Pledge Agreement with City of Duluth

On February 23, 2012, the City of Duluth issued General Obligation Tax Abatement Bonds, Series 2012A, in the amount of \$7,055,000. The proceeds from these bonds were used to finance capital improvements to the Spirit Mountain Recreation Area Authority, including lift improvements, parking lot improvements, and a new chalet on Grand Avenue.

The Authority entered into a pledge agreement with the City of Duluth dated February 23, 2012. Under this agreement, the City has pledged tax abatement revenue for paying the principal and interest on the bonds, but the City's and Authority's plan of finance for the project is for the City to provide \$500,000 per year of tourism taxes toward the repayment of the bond principal and interest, and the Authority to pledge operating revenues to pay the balance of the principal and interest owed each year until the bond is paid off in 2030.

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

2. Detailed Notes (Continued)

G. Capitalized Lease Obligations

Capitalized lease obligations consist of the following at April 30, 2017 and 2016:

<u>Type of Property</u>	<u>2017</u>	<u>2016</u>
Equipment	\$ 3,453,731	\$ 3,453,731
Less: accumulated amortization	<u>(1,336,347)</u>	<u>(1,136,398)</u>
Net Capital Lease Property	<u>\$ 2,117,384</u>	<u>\$ 2,317,333</u>

Minimum future lease payments follow:

<u>Fiscal Year Ended April 30, 2017</u>	<u>Principal</u>	<u>Interest</u>
2018	\$ 228,785	\$ 58,139
2019	207,455	49,893
2020	185,486	41,805
2021	178,917	34,290
2022	186,235	26,973
2023 - 2025	<u>540,721</u>	<u>34,046</u>
Total	<u>\$ 1,527,599</u>	<u>\$ 245,146</u>

<u>Fiscal Year Ended April 30, 2016</u>	<u>Principal</u>	<u>Interest</u>
2017	\$ 273,147	\$ 67,732
2018	230,215	58,139
2019	207,455	49,893
2020	200,763	41,805
2021	178,917	34,290
2022 - 2025	<u>719,656</u>	<u>61,019</u>
Total	<u>\$ 1,810,153</u>	<u>\$ 312,878</u>

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

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2. Detailed Notes

G. Capitalized Lease Obligations (Continued)

Capitalized lease obligations at April 30, 2017 and 2016, consist of the following leases:

	2017	2016
A \$2,340,150 lease purchase for purchase, design, and installation of an Alpine Coaster and construction of a ticket/concession building and parking lot, dated January 26, 2010, due in periodic installments commencing September 1, 2010, through February 1, 2025, with interest at 3.96 percent.	\$ 1,401,446	\$ 1,551,723
A \$600,000 lease purchase for purchase, design, and installation of a zip line, tubing hill, and mini golf course, dated June 1, 2011, due in periodic installments commencing October 1, 2011, through June 1, 2016, with interest at 4.05 percent.	-	20,641
A \$266,519 lease purchase for a groomer, dated October 15, 2012, due in periodic installments through October 1, 2017, with interest at 3.50 percent.	29,271	86,170
A \$202,200 lease purchase for a groomer, dated December 23, 2014, due in periodic installments through December 23, 2019, with interest at 3.50 percent.	96,882	151,619
Total	\$ 1,527,599	\$ 1,810,153
Current portion	\$ 228,785	\$ 273,147
Long-term portion	1,298,814	1,537,006
Total	\$ 1,527,599	\$ 1,810,153

H. Operating Lease

The Authority is obligated under an operating lease for office equipment. Lease expense for each of fiscal years 2017 and 2016 is \$4,500. The future minimum rental payments, which are not reported as liabilities in the financial statements at April 30, 2017, and April 30, 2016, are \$4,500 due in fiscal years 2018 and 2017.

**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 November 2016, 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 \$27,000 plus ten percent of gross sales.

3. Risk Management

The Authority uses State Fund Mutual (SFM) to insure against its obligation to provide benefits to employees pursuant to the Minnesota Workers' Compensation Act. The Authority participates in the League of Minnesota Cities (LMC) for commercial insurance and to insure against general liability claims, except the liability claims arising by reason of selling, serving, or furnishing alcoholic beverages. There were no significant reductions in insurance coverage from the previous year. There was no settlements in excess of insurance for any of the past three fiscal years. No liability has been recognized in the financial statements for excess workers' compensation claims and costs.

For general liability claims insured through the LMC, the Authority retains responsibility for paying the first \$50,000 of each loss resulting from each occurrence. The maximum coverage provided by the LMC was \$500,000 per claimant; \$2,000,000 per occurrence. The estimated liability of the Authority for general liability claims, where coverage is not provided, is accrued if the Authority's attorney determines settlement is probable, based on a case-by-case evaluation.

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

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4. Defined Benefit Pension Plan

A. Plan Description

All full-time and certain part-time employees of the Spirit Mountain Recreation Area Authority are covered by a defined benefit pension plan administered by the Public Employees Retirement Association of Minnesota (PERA). PERA administers the General Employees Retirement Plan, which is a cost-sharing, multiple-employer retirement plan. The plan is established and administered in accordance with Minn. Stat. chs. 353 and 356. PERA's defined benefit pension plan is a tax qualified plan under Section 401(a) of the Internal Revenue Code.

The General Employees Retirement Plan (accounted for in the General Employees Fund) has multiple benefit structures with members belonging to either the Coordinated Plan or the Basic Plan. Coordinated Plan members are covered by Social Security and Basic Plan members are not. The Basic Plan was closed to new members in 1967. All new members must participate in the Coordinated Plan, for which benefits vest after five years of credited service.

B. Benefits Provided

PERA provides retirement benefits as well as disability benefits to members and benefits to survivors upon death of eligible members. Benefit provisions are established by state statute and can be modified only by the state legislature. Benefit increases are provided to benefit recipients each January. Increases are related to the funding ratio of the plan. Benefit recipients receive a future annual 1.0 percent post-retirement benefit increase. If the funding ratio reaches 90 percent for two consecutive years, the benefit increase will revert to 2.5 percent. If, after reverting to a 2.5 percent benefit increase, the funding ratio declines to less than 80 percent for one year or less than 85 percent for two consecutive years, the benefit increase will decrease to 1.0 percent.

The benefit provisions stated in the following paragraph 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 their public service.

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

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4. Defined Benefit Pension Plan

B. Benefits Provided (Continued)

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 General Employees Retirement Plan Coordinated and Basic Plan members. Members hired prior to July 1, 1989, receive 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 remaining year. The annuity accrual rate for a Coordinated Plan member is 1.2 percent of average salary for each of the first ten years of service and 1.7 percent for each remaining year. Under 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 General Employees Retirement Plan members hired prior to July 1, 1989, a full annuity is available when age plus years of service equal 90, and normal retirement age is 65. For members hired on or after July 1, 1989, normal retirement age is the age for unreduced Social Security benefits capped at 66. Disability benefits are available for vested members and are based on years of service and average high-five salary.

C. Contributions

Pension benefits are funded from member and employer contributions and income from the investment of fund assets. Rates for employer and employee contributions are set by Minn. Stat. ch. 353. These statutes are established and amended by the state legislature. General Employees Retirement Plan Basic members and Coordinated Plan members were required to contribute 9.10 percent and 6.50 percent, respectively, of their annual covered salary for the year ended April 30, 2017.

During the current year, the Authority was required to contribute the following percentages of annual covered salary:

General Employees Retirement Plan	
Basic Plan members	11.78%
Coordinated Plan members	7.50

The employee and employer contribution rates did not change from the previous year.

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

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4. Defined Benefit Pension Plan

C. Contributions (Continued)

The Authority's contributions for the General Employees Retirement Plan for the years ended April 30, 2017 and 2016, were \$125,108 and \$115,982, respectively. The contributions are equal to the contractually required contributions as set by state statute.

D. Pension Costs

At April 30, 2017 and 2016, the Authority reported a liability of \$2,021,757 and \$1,497,748, respectively, for its proportionate share of the General Employees Retirement Plan's net pension liability. The net pension liability was measured as of June 30, 2016 and 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of those dates. The Authority's proportion of the net pension liability was based on the Authority's contributions received by PERA during the measurement period for employer payroll paid dates from July 1, 2015, through June 30, 2016; and July 1, 2014, through June 30, 2015, relative to the total employer contributions received from all of PERA's participating employers. At June 30, 2016, the Authority's proportion was 0.0249 percent. It was 0.0289 percent measured as of June 30, 2015. For the years ended April 30, 2017 and 2016, the Authority recognized pension expense of \$198,930 and \$209,622, respectively, for its proportionate share of the General Employees Retirement Plan's pension expense.

The Authority also recognized \$7,897 as revenue, which results in a reduction of the net pension liability, for its proportionate share of the State of Minnesota's contribution to the General Employees Retirement Plan, which qualifies as a special funding situation. Legislation requires the State of Minnesota to contribute \$6 million to the General Employees Retirement Plan each year, starting September 15, 2015, through September 15, 2031.

The Authority's proportionate share of the net pension liability	\$ 2,021,757
State of Minnesota's proportionate share of the net pension liability associated with the Authority	<u>26,483</u>
Total	<u>\$ 2,048,240</u>

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

4. Defined Benefit Pension Plan

D. Pension Costs (Continued)

The Authority reported its proportionate share of the General Employees Retirement Plan's deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	2017		2016	
	Deferred Outflows of Resources	Deferred Inflows of Resources	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual economic experience	\$ 7,593	\$ 171,205	\$ 15,187	\$ 75,512
Changes in actuarial assumptions	441,851	-	91,977	-
Difference between projected and actual investment earnings	398,457	183,408	141,785	275,112
Changes in proportion	-	228,517	-	109,563
Contributions paid to PERA subsequent to the measurement date	93,600	-	92,939	-
Total	<u>\$ 941,501</u>	<u>\$ 583,130</u>	<u>\$ 341,888</u>	<u>\$ 460,187</u>

The \$93,600 reported as deferred outflows of resources related to pensions resulting from contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended April 30, 2018. At April 30, 2016, \$92,939 was reported as deferred outflows of resources related to pensions resulting from the Authority's contributions subsequent to the measurement date and was recognized as a reduction of the net pension liability. Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

As of April 30, 2017:

Year Ended April 30	Pension Expense Amount
2018	\$ 48,500
2019	(5,078)
2020	148,316
2021	73,033

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

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4. Defined Benefit Pension Plan

D. Pension Costs (Continued)

As of April 30, 2016:

Year Ended April 30	Pension Expense Amount
2017	\$ (64,368)
2018	(64,368)
2019	(117,950)
2020	35,448

E. Actuarial Assumptions

The total pension liability in the June 30, 2016, and June 30, 2015, actuarial valuations was determined using the individual entry age normal actuarial cost method and the following additional actuarial assumptions:

June 30, 2016	
Inflation	2.50 percent per year
Active member payroll growth	3.25 percent per year
Investment rate of return	7.50 percent
June 30, 2015	
Inflation	2.75 percent per year
Active member payroll growth	3.50 percent per year
Investment rate of return	7.90 percent

Salary increases were based on a service-related table. Mortality rates for active members, retirees, survivors, and disabilitants were based on RP-2014 tables in the June 30, 2016, valuation. The cost of living benefit increases for retirees is assumed to be 1.0 percent. The RP-2000 tables were used in the June 30, 2015, valuation for males or females, as appropriate, with slight adjustments. The cost of living benefit increases for retirees was assumed to be 1.0 percent effective every January 1 through 2035, and 2.5 percent thereafter.

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

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4. Defined Benefit Pension Plan

E. Actuarial Assumptions (Continued)

Actuarial assumptions used in the June 30, 2016, valuations were based on the results of actuarial experience studies. The experience study in the General Employees Retirement Plan was for the period 2008 through 2015.

In 2015, an updated experience study was done for PERA's General Employees Retirement Plan for the six-year period ending June 30, 2014, which would result in a larger pension liability. However, PERA will not implement the changes in assumptions until its June 30, 2016, estimate of pension liability.

The long-term expected rate of return on pension plan investments is 7.50 percent. The State Board of Investment, which manages the investments of PERA, prepares an analysis of the reasonableness of the long-term expected rate of return on a regular basis using a building-block method in which best-estimate ranges of expected future rates of return are developed for each major asset class. These ranges are combined to produce an expected long-term rate of return by weighting the expected future rates of return by the target asset allocation percentages. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
Domestic stocks	45%	5.50%
International stocks	15	6.00
Bonds	18	1.45
Alternative assets	20	6.40
Cash	2	0.50

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

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4. Defined Benefit Pension Plan (Continued)

F. Discount Rate

The discount rate used to measure the total pension liability was 7.50 percent in 2016, a reduction of the 7.90 percent used in 2015. The projection of cash flows used to determine the discount rate assumed that employee and employer contributions will be made at the rate specified in statute. Based on that assumption, the fiduciary net position of the General Employees Retirement Plan was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to determine the total pension liability.

G. Changes in Actuarial Assumptions

The following changes in actuarial assumptions occurred in 2016:

General Employees Retirement Plan

- The assumed post-retirement benefit increase rate was changed from 1.00 percent per year through 2035 and 2.50 percent per year thereafter, to 1.00 percent for all future years.
- The assumed investment rate was changed from 7.90 percent to 7.50 percent. The single discount rate was also changed from 7.90 percent to 7.50 percent.
- Other assumptions were changed pursuant to the experience study dated June 30, 2015. The assumed payroll growth and inflation were decreased by 0.25 percent. Payroll growth was reduced from 3.50 percent to 3.25 percent. Inflation was reduced from 2.75 percent to 2.50 percent.

H. Pension Liability Sensitivity

The following presents the Authority's proportionate share of the net pension liability calculated using the discount rate disclosed in the preceding paragraph, as well as what the Authority's proportionate share of the net pension liability would be if it were calculated using a discount rate 1.00 percentage point lower or 1.00 percentage point higher than the current discount rate:

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

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4. Defined Benefit Pension Plan

H. Pension Liability Sensitivity (Continued)

	1% Decrease in Discount Rate (6.5%)	Discount Rate (7.5%)	1% Increase in Discount Rate (8.5%)
Proportionate share of the General Employees Retirement Plan net pension liability as of June 30, 2016	\$ 2,871,493	\$ 2,021,757	\$ 1,321,805
	1% Decrease in Discount Rate (6.9%)	Discount Rate (7.9%)	1% Increase in Discount Rate (8.9%)
Proportionate share of the General Employees Retirement Plan net pension liability as of June 30, 2015	\$ 2,354,992	\$ 1,497,748	\$ 789,796

I. Pension Plan Fiduciary Net Position

Detailed information about the pension plan's fiduciary net position is available in a separately issued PERA financial report that includes financial statements and required supplementary information. 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, St. Paul, Minnesota 55103-2088; or by calling 651-296-7460 or 1-800-652-9026.

**REQUIRED SUPPLEMENTARY INFORMATION**

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

*EXHIBIT A-1*

**SCHEDULE OF PROPORTIONATE SHARE OF NET PENSION LIABILITY  
PERA GENERAL EMPLOYEES RETIREMENT PLAN  
APRIL 30, 2017**

<b>Measurement Date</b>	<b>Employer's Proportion of the Net Pension Liability (Asset)</b>	<b>Employer's Proportionate Share of the Net Pension Liability (Asset) (a)</b>	<b>State's Proportionate Share of the Net Pension Liability Associated with the Spirit Mountain Recreation Area Authority (b)</b>	<b>Employer's Proportionate Share of the Net Pension Liability and the State's Related Share of the Net Pension Liability (Asset) (a + b)</b>	<b>Covered Payroll (c)</b>	<b>Employer's Proportionate Share of the Net Pension Liability (Asset) as a Percentage of Covered Payroll (a/c)</b>	<b>Plan Fiduciary Net Position as a Percentage of the Total Pension Liability</b>
2016	0.0249%	\$ 2,021,757	\$ 26,483	\$ 2,048,240	\$ 1,659,293	121.84%	68.91%
2015	0.0289	1,497,748	N/A	1,497,748	1,670,387	89.66	78.19
2014	0.0316	1,484,410	N/A	1,484,410	1,737,780	85.42	78.75

This schedule is intended to show information for ten years. Additional years will be displayed as they become available.  
The measurement date for each year is June 30.  
N/A - Not Applicable

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

**EXHIBIT A-2**

**SCHEDULE OF CONTRIBUTIONS  
PERA GENERAL EMPLOYEES RETIREMENT PLAN  
APRIL 30, 2017**

<b>Year Ending</b>	<b>Statutorily Required Contributions (a)</b>	<b>Actual Contributions in Relation to Statutorily Required Contributions (b)</b>	<b>Contribution (Deficiency) Excess (b - a)</b>	<b>Covered Payroll (c)</b>	<b>Actual Contributions as a Percentage of Covered Payroll (b/c)</b>
2017	\$ 125,108	\$ 125,108	\$ -	\$ 1,668,107	7.50%
2016	115,982	115,982	-	1,546,427	7.50
2015	127,523	104,147	(23,376)	1,737,780	5.99

This schedule is intended to show information for ten years. Additional years will be displayed as they become available.  
The Authority's year-end is April 30.

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

NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION  
FOR THE YEARS ENDED APRIL 30, 2017 AND 2016

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Defined Benefit Pension Plan - Changes in Significant Plan Provisions, Actuarial Methods, and Assumptions

The following changes were reflected in the valuation performed on behalf of the Public Employees Retirement Association for the year ended June 30, 2016:

General Employees Retirement Plan

- The assumed post-retirement benefit increase rate was changed from 1.00 percent per year through 2035 and 2.50 percent per year thereafter, to 1.00 percent for all future years.
- The assumed investment rate was changed from 7.90 percent to 7.50 percent. The single discount rate was also changed from 7.90 percent to 7.50 percent.
- Other assumptions were changed pursuant to the experience study dated June 30, 2015. The assumed payroll growth and inflation were decreased by 0.25 percent. Payroll growth was reduced from 3.50 percent to 3.25 percent. Inflation was reduced from 2.75 percent to 2.50 percent.

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**SUPPLEMENTARY INFORMATION**

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

**EXHIBIT B-1**

**COMPARATIVE STATEMENT OF OPERATING REVENUES  
YEARS ENDED APRIL 30, 2017 AND 2016**

	<b>2017</b>	<b>2016</b>
<b>Sales</b>		
Food	\$ 526,913	\$ 506,953
Liquor	289,994	271,969
Ski shop	97,750	108,583
Grand Avenue Chalet	198,938	235,178
Less: cost of goods sold	(403,640)	(436,984)
<b>Net sales</b>	<b>\$ 709,955</b>	<b>\$ 685,699</b>
<b>Charges for Services</b>		
Season pass	\$ 842,125	\$ 787,985
Daily lift tickets	919,064	908,392
Alpine Coaster	717,560	818,548
Ski school and snow sports	122,032	118,255
Ski rental	195,762	231,945
Snowboard rental	38,231	46,215
Locker rental	15,888	19,784
Nordic tickets and rental	706	895
Snocross	195,484	179,424
Campground	169,436	161,292
Mountain Villas management fee	111,210	105,618
Marketing revenue	9,794	8,675
Summer activities	120,922	89,877
<b>Total charges for services</b>	<b>\$ 3,458,214</b>	<b>\$ 3,476,905</b>
<b>Miscellaneous</b>		
Other revenues	<b>\$ 147,609</b>	<b>\$ 103,202</b>
<b>Total Operating Revenues</b>	<b>\$ 4,315,778</b>	<b>\$ 4,265,806</b>

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

**EXHIBIT B-2**

**COMPARATIVE STATEMENT OF OPERATING EXPENSES  
YEARS ENDED APRIL 30, 2017 AND 2016**

	<b>2017</b>	<b>2016</b>
<b>Department</b>		
Food and beverage	\$ 425,301	\$ 385,946
Housekeeping	46,117	46,031
Rental	68,330	45,998
Ski shop	38,926	41,682
Campground	80,998	60,212
Parking and shuttle	3,638	4,221
Building and grounds	296,770	319,237
Snocross	127,345	111,719
Ski school and snow sports center	163,047	105,240
Child care	-	753
Outside mountain operations	1,177,766	1,112,437
Nordic	2,856	7,607
Ski patrol	8,911	6,879
Sales and marketing	299,948	297,131
Office administration	1,236,953	1,142,200
Mountain Villas	55,814	46,825
Grand Avenue Chalet	143,817	185,911
Summer activities	3,312	16,132
Adventure Park	266,866	255,333
<b>Total departmental costs</b>	<b>\$ 4,446,715</b>	<b>\$ 4,191,494</b>
Amortization	20,850	21,097
Depreciation	1,057,840	1,010,693
<b>Total Operating Expenses</b>	<b>\$ 5,525,405</b>	<b>\$ 5,223,284</b>



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REBECCA OTTO  
STATE AUDITOR

# STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

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## 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*

### Independent Auditor's Report

Mayor and City Council  
City of Duluth, Minnesota

Board of Directors  
Spirit Mountain Recreation Area Authority  
Duluth, Minnesota

We have audited, 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, the financial statements of the Spirit Mountain Recreation Area Authority, a component unit of the City of Duluth, Minnesota, as of and for the year ended April 30, 2017, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated February 1, 2018.

### **Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Spirit Mountain Recreation Area Authority's internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over financial reporting.

A deficiency in internal control over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit, we did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify a deficiency in internal control over financial reporting, described in the accompanying Schedule of Findings and Recommendations as item 2015-001, that we consider to be a significant deficiency.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Spirit Mountain Recreation Area Authority's financial statements are free from 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**

The *Minnesota Legal Compliance Audit Guide for Cities*, promulgated by the State Auditor pursuant to Minn. Stat. § 6.65, contains seven categories of compliance to be tested in connection with the audit of the Authority's financial statements: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, miscellaneous provisions, and tax increment financing. Our audit considered all of the listed categories, except that we did not test for compliance with the provisions of deposits and investments because the City of Duluth has custody of the Authority's deposits and is responsible for compliance. We also did not test for compliance with the provisions of tax increment financing because the Authority does not administer any tax increment financing districts.

In connection with our audit, nothing came to our attention that caused us to believe that the Spirit Mountain Recreation Area Authority failed to comply with the provisions of the *Minnesota Legal Compliance Audit Guide for Cities*. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the Authority's noncompliance with the above referenced provisions.

## **Spirit Mountain Recreation Area Authority's Response to Finding**

The Spirit Mountain Recreation Area Authority's response to the internal control finding identified in our audit is described in the Corrective Action Plan. The Authority's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

### **Purpose of This Report**

The purpose of this report is solely to describe the scope of our testing of internal control over financial reporting, compliance, and the provisions of the *Minnesota Legal Compliance Audit Guide for Cities* and the results of that testing, and not to provide an opinion on the effectiveness of the Authority's internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance. Accordingly, this communication is not suitable for any other purpose.

*/s/Rebecca Otto*

REBECCA OTTO  
STATE AUDITOR

*/s/Greg Hierlinger*

GREG HIERLINGER, CPA  
DEPUTY STATE AUDITOR

February 1, 2018

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

**SCHEDULE OF FINDINGS AND RECOMMENDATIONS  
FOR THE YEAR ENDED APRIL 30, 2017**

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

INTERNAL CONTROL

PREVIOUSLY REPORTED ITEM NOT RESOLVED

Finding Number 2015-001

Segregation of Duties

**Criteria:** Management is responsible for establishing and maintaining internal control. Adequate segregation of duties is a key internal control in preventing and detecting errors or irregularities. To protect the Spirit Mountain Recreation Area Authority's assets, proper segregation of record-keeping, custody, and authorization functions should be in place, and where management decides segregation of duties may not be cost effective, compensating controls should be in place.

**Condition:** Due to the limited number of personnel, segregation of duties necessary to ensure adequate internal accounting control is not possible.

**Context:** The size of the Authority and its staffing limits the internal control that management can design and implement into the organization. Without proper segregation of duties, errors or irregularities may not be detected timely.

**Effect:** Inadequate segregation of duties could adversely affect the Authority's ability to detect misstatements in a timely period by employees in the normal course of performing their assigned functions.

**Cause:** The size of the Spirit Mountain Recreation Area Authority and its staffing limits the internal control that management can design and implement into the organization.

**Recommendation:** Management should be aware that segregation of duties is not adequate from an internal control point of view. We recommend the Board of Directors and management be mindful that limited staffing causes inherent risks in safeguarding the Authority's assets and the proper reporting of its financial activity. We recommend the Board of Directors and management continue to implement oversight procedures and monitor those procedures to determine if they are still effective internal controls.

**View of Responsible Official:** Acknowledged

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**REPRESENTATION OF THE  
SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

**CORRECTIVE ACTION PLAN  
FOR THE YEAR ENDED APRIL 30, 2017**

**Finding Number: 2015-001**

**Finding Title: Segregation of Duties**

Name of Contact Person Responsible for Corrective Action:

Brandy Ream, Executive Director

Corrective Action Planned:

Due to the limited number of personnel, segregation of accounting duties necessary to ensure adequate internal accounting control is not possible. We currently have policies and procedures in place to provide an on-going monitoring system. We will continue with this monitoring and develop additional policies and procedures as needed to improve our internal control.

Anticipated Completion Date:

Ongoing

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**REPRESENTATION OF THE  
SPIRIT MOUNTAIN RECREATION AREA AUTHORITY  
DULUTH, MINNESOTA**

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS  
FOR THE YEAR ENDED APRIL 30, 2017

**Finding Number: 2015-001**

**Finding Title: Segregation of Duties**

**Summary of Condition:** Due to the limited number of personnel, segregation of duties necessary to ensure adequate internal accounting control is not possible.

**Summary of Corrective Action Previously Reported:** The cost of adding additional staff outweighs the benefit. The Spirit Mountain Recreation Area Authority understands the risk and is willing to assume the responsibility.

**Status:** Not Corrected. The Spirit Mountain Recreation Area Authority understands the risk and is willing to assume the responsibility.

Was corrective action taken significantly different than the action previously reported?

Yes \_\_\_\_\_ No   X