VILLAGE OF KELLEYS ISLAND
ERIE COUNTY

REGULAR AUDIT

FOR THE YEARS ENDED DECEMBER 31, 2007 AND 2008

Mary Taylor, CPA
Auditor of State

VILLAGE OF KELLEYS ISLAND
ERIE COUNTY

TABLE OF CONTENTS

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Village of Kelleys Island
Erie County
121 Addison Street, P.O. Box 469
Kelleys Island, Ohio 43438-0469

To the Village Council:

As you are aware, the Auditor of State's Office (AOS) must modify the *Independent Accountants' Report* we provide on your financial statements due to an interpretation from the American Institute of Certified Public Accountants (AICPA). While AOS does not legally require your government to prepare financial statements pursuant to Generally Accepted Accounting Principles (GAAP), the AICPA interpretation requires auditors to formally acknowledge that you did not prepare your financial statements in accordance with GAAP. Our Report includes an adverse opinion relating to GAAP presentation and measurement requirements, but does not imply the amounts the statements present are misstated under the non-GAAP basis you follow. The AOS report also includes an opinion on the financial statements you prepared using the cash basis and financial statement format the AOS permits.

Mary Taylor

Mary Taylor, CPA
Auditor of State

November 10, 2009

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INDEPENDENT ACCOUNTANTS' REPORT

Village of Kelleys Island
Erie County
121 Addison Street, P.O. Box 469
Kelleys Island, Ohio 43438-0469

To the Village Council:

We have audited the accompanying financial statements of the Village of Kelleys Island, Erie County, (the Village) as of and for the years ended December 31, 2008 and 2007. These financial statements are the responsibility of the Village'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 the Comptroller General of the United States' *Government Auditing Standards*. Those standards require that we plan and perform the audits to reasonably assure 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 our audits provide a reasonable basis for our opinion.

As described more fully in Note 1, the Village has prepared these financial statements using accounting practices the Auditor of State prescribes or permits. These practices differ from accounting principles generally accepted in the United States of America (GAAP). Although we cannot reasonably determine the effects on the financial statements of the variances between these regulatory accounting practices and GAAP, we presume they are material.

Instead of the combined funds the accompanying financial statements present, GAAP require presenting entity wide statements and also presenting the Village's larger (i.e. major) funds separately. While the Village does not follow GAAP, generally accepted auditing standards requires us to include the following paragraph if the statements do not substantially conform to GAAP presentation requirements. The Auditor of State permits, but does not require villages to reformat their statements. The Village has elected not to follow GAAP statement formatting requirements. The following paragraph does not imply the amounts reported are materially misstated under the accounting basis the Auditor of State permits. Our opinion on the fair presentation of the amounts reported pursuant to its non-GAAP basis is in the second following paragraph.

In our opinion, because of the effects of the matter discussed in the preceding two paragraphs, the financial statements referred to above for the years ended December 31, 2008 and 2007 do not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of the Village as of December 31, 2008 and 2007, or its changes in financial position or cash flows, where applicable for the years then ended.

Also, in our opinion, the financial statements referred to above present fairly, in all material respects, the combined fund cash balances and reserves for encumbrances of the Village of Kelleys Island, Erie County, as of December 31, 2008 and 2007, and its combined cash receipts and disbursements for the years then ended on the accounting basis Note 1 describes.

The Village has not presented Management's Discussion and Analysis, which accounting principles generally accepted in the United States of America has determined is necessary to supplement, although not required to be part of, the financial statements.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 10, 2009, on our consideration of the Village's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. While we did not opine on the internal control over financial reporting or on compliance, that report describes the scope of our testing of internal control over financial reporting and compliance, and the results of that testing. That report is an integral part of an audit performed in accordance with *Government Auditing Standards*. You should read it in conjunction with this report in assessing the results of our audits.

Mary Taylor

Mary Taylor, CPA
Auditor of State

November 10, 2009

VILLAGE OF KELLEYS ISLAND
ERIE COUNTY

COMBINED STATEMENT OF CASH RECEIPTS, CASH DISBURSEMENTS, AND CHANGES IN FUND CASH BALANCES ALL GOVERNMENTAL FUND TYPES FOR THE YEAR ENDED DECEMBER 31, 2008

	Governmental Fund Types			
	General	Special Revenue	Capital Projects	Totals (Memorandum Only)
Cash Receipts:				
Property and Local Taxes	$248,693	$179,130		$427,823
Intergovernmental	251,959	89,329	$446,771	788,059
Special Assessments		3,151		3,151
Charges for Services	1,500	3,300		4,800
Fines, Licenses and Permits	44,255	8,210		52,465
Earnings on Investments	16,880	2,820		19,700
Miscellaneous	9,095	36,433		45,528
Total Cash Receipts	572,382	322,373	446,771	1,341,526
Cash Disbursements:				
Current:				
Security of Persons and Property	151,410	35,936		187,346
Public Health Services	1,261	35,920		37,181
Community Environment	26,079			26,079
Transportation	89,620	46,262		135,882
General Government	305,295	3,135		308,430
Debt Service:				
Redemption of Principal		4,809		4,809
Capital Outlay	84,076	109,660	437,724	631,460
Total Cash Disbursements	657,741	235,722	437,724	1,331,187
Total Receipts Over/(Under) Disbursements	(85,359)	86,651	9,047	10,339
Other Financing Receipts / (Disbursements):				
Transfers-In		1,930		1,930
Transfers-Out	(1,930)			(1,930)
Other Financing Sources	37			37
Total Other Financing Receipts / (Disbursements)	(1,893)	1,930		37
Excess of Cash Receipts and Other Financing Receipts Over/(Under) Cash Disbursements and Other Financing Disbursements	(87,252)	88,581	9,047	10,376
Fund Cash Balances, January 1	711,478	567,556	23,948	1,302,982
Fund Cash Balances, December 31	**$624,226**	**$656,137**	**$32,995**	**$1,313,358**
Reserve for Encumbrances, December 31	$52,707	$56,929		$109,636

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

VILLAGE OF KELLEYS ISLAND
ERIE COUNTY

COMBINED STATEMENT OF CASH RECEIPTS, CASH DISBURSEMENTS, AND CHANGES IN FUND CASH BALANCES - ALL PROPRIETARY AND FIDUCIARY FUND TYPES FOR THE YEAR ENDED DECEMBER 31, 2008

	Proprietary Fund Type	Fiduciary Fund Type	
	Enterprise	Agency	Totals (Memorandum Only)
Operating Cash Receipts:			
Charges for Services	$333,839		$333,839
Operating Cash Disbursements:			
Personal Services	173,268		173,268
Travel Transportation	2,430		2,430
Contractual Services	100,270		100,270
Supplies and Materials	65,914		65,914
Total Operating Cash Disbursements	341,882		341,882
Operating Loss	(8,043)		(8,043)
Non-Operating Cash Receipts:			
Special Assessments	72,001		72,001
Earnings on Investments	2,556		2,556
Other Debt Proceeds	106,555		106,555
Miscellaneous Receipts	61		61
Other Non-Operating Cash Receipts		$32,412	32,412
Total Non-Operating Cash Receipts	181,173	32,412	213,585
Non-Operating Cash Disbursements:			
Capital Outlay	159,505		159,505
Redemption of Principal	101,543		101,543
Interest and Other Fiscal Charges	41,180		41,180
Other Non-Operating Cash Disbursements	8	33,100	33,108
Total Non-Operating Cash Disbursements	302,236	33,100	335,336
Excess of Receipts Under Disbursements Before Interfund Transfers	(129,106)	(688)	(129,794)
Transfers-In	21,375		21,375
Transfers-Out	(21,375)		(21,375)
Net Receipts Under Disbursements	(129,106)	(688)	(129,794)
Fund Cash Balances, January 1	246,805	6,508	253,313
Fund Cash Balances, December 31	**$117,699**	**$5,820**	**$123,519**
Reserve for Encumbrances, December 31	$7,863		$7,863

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

VILLAGE OF KELLEYS ISLAND
ERIE COUNTY

COMBINED STATEMENT OF CASH RECEIPTS, CASH DISBURSEMENTS, AND CHANGES IN FUND CASH BALANCES
ALL GOVERNMENTAL FUND TYPES
FOR THE YEAR ENDED DECEMBER 31, 2007

	Governmental Fund Types			
	General	Special Revenue	Capital Projects	Totals (Memorandum Only)
Cash Receipts:				
Property and Local Taxes	$321,712	$192,944		$514,656
Intergovernmental	101,360	241,740	$279,836	622,936
Special Assessments		3,144		3,144
Charges for Services	750	4,500		5,250
Fines, Licenses and Permits	65,093	7,320		72,413
Earnings on Investments	58,130	9,463		67,593
Miscellaneous	1,759	2,180		3,939
Total Cash Receipts	548,804	461,291	279,836	1,289,931
Cash Disbursements:				
Current:				
Security of Persons and Property	161,642	26,206		187,848
Public Health Services		35,128		35,128
Leisure Time Activities	540			540
Community Environment	12,076			12,076
Transportation	66,107	53,677		119,784
General Government	283,519	1,909		285,428
Debt Service:				
Redemption of Principal		4,809		4,809
Capital Outlay	97,082	368,329	258,304	723,715
Total Cash Disbursements	620,966	490,058	258,304	1,369,328
Total Receipts Over/(Under) Disbursements	(72,162)	(28,767)	21,532	(79,397)
Other Financing Receipts / (Disbursements):				
Transfers-In		1,842		1,842
Transfers-Out	(1,842)			(1,842)
Advances-In	25,500			25,500
Advances-Out			(25,500)	(25,500)
Other Financing Uses	(25)			(25)
Total Other Financing Receipts / (Disbursements)	23,633	1,842	(25,500)	(25)
Excess of Cash Receipts and Other Financing Receipts Under Cash Disbursements and Other Financing Disbursements	(48,529)	(26,925)	(3,968)	(79,422)
Fund Cash Balances, January 1	760,007	594,481	27,916	1,382,404
Fund Cash Balances, December 31	**$711,478**	**$567,556**	**$23,948**	**$1,302,982**
Reserve for Encumbrances, December 31	$542	$6,089	$62,767	$69,398

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

VILLAGE OF KELLEYS ISLAND
ERIE COUNTY

COMBINED STATEMENT OF CASH RECEIPTS, CASH DISBURSEMENTS, AND CHANGES IN FUND CASH BALANCES - ALL PROPRIETARY AND FIDUCIARY FUND TYPES
FOR THE YEAR ENDED DECEMBER 31, 2007

	Proprietary Fund Type	Fiduciary Fund Type	
	Enterprise	Agency	Totals (Memorandum Only)
Operating Cash Receipts:			
Charges for Services	$330,049		$330,049
Miscellaneous	1,143		1,143
Total Operating Cash Receipts	331,192		331,192
Operating Cash Disbursements:			
Personal Services	161,272		161,272
Travel Transportation	2,122		2,122
Contractual Services	65,124		65,124
Supplies and Materials	30,424		30,424
Total Operating Cash Disbursements	258,942		258,942
Operating Income	72,250		72,250
Non-Operating Cash Receipts:			
Special Assessments	32,575		32,575
Earnings on Investments	11,852		11,852
Miscellaneous Receipts	78		78
Other Non-Operating Cash Receipts		$41,231	41,231
Total Non-Operating Cash Receipts	44,505	41,231	85,736
Non-Operating Cash Disbursements:			
Capital Outlay	22,968		22,968
Redemption of Principal	56,965		56,965
Interest and Other Fiscal Charges	40,497		40,497
Other Non-Operating Cash Disbursements		38,177	38,177
Total Non-Operating Cash Disbursements	120,430	38,177	158,607
Excess of Receipts Over/(Under) Disbursements Before Interfund Transfers	(3,675)	3,054	(621)
Transfers-In	19,731		19,731
Transfers-Out	(19,731)		(19,731)
Net Receipts Over/(Under) Disbursements	(3,675)	3,054	(621)
Fund Cash Balances, January 1	250,480	3,454	253,934
Fund Cash Balances, December 31	**$246,805**	**$6,508**	**$253,313**
Reserve for Encumbrances, December 31	$64,584		$64,584

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

NOTES TO THE FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Description of the Entity

The constitution and laws of the State of Ohio establish the rights and privileges of the Village of Kelleys Island, Erie County, (the Village) as a body corporate and politic. A publicly-elected six-member Council directs the Village. The Village provides water and sewer utilities, park operations, and police services

The Village participates in the Public Entities Pool of Ohio public entity risk pool. Note 8 to the financial statements provides additional information for this entity. This organization provides property and casualty coverage for its members.

The Village's management believes these financial statements present all activities for which the Village is financially accountable.

B. Accounting Basis

These financial statements follow the accounting basis the Auditor of State prescribes or permits. This basis is similar to the cash receipts and disbursements accounting basis. The Village recognizes receipts when received in cash rather than when earned, and recognizes disbursements when paid rather than when a liability is incurred. Budgetary presentations report budgetary expenditures when a commitment is made (i.e., when an encumbrance is approved).

These statements include adequate disclosure of material matters, as the Auditor of State prescribes or permits.

C. Fund Accounting

The Village uses fund accounting to segregate cash and investments restricted as to use. The Village classifies its funds into the following types:

1. General Fund

The General Fund reports all financial resources except those required to be accounted for in another fund.

2. Special Revenue Funds

These funds account for proceeds from specific sources (other than from capital projects, enterprise or agency funds) restricted to expenditure for specific purposes. The Village had the following significant Special Revenue Funds:

<u>Street Construction, Maintenance and Repair Fund</u> - This fund receives gasoline tax and motor vehicle tax money for constructing, maintaining, and repairing Village streets.

<u>Road Construction Fund</u> – This fund receives tax and special assessment funds for construction and repair of roads within the Village.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (CONTINUED)

Fireman's Levy Fund – This fund receives property tax revenue to provide fire protection services for the Village.

3. Capital Project Funds

These funds account for receipts restricted to acquiring or constructing major capital projects (except those financed through enterprise funds). The Village had the following significant capital project funds:

Airport Resurfacing Fund – This fund receives grant revenues used for airport improvements.

Issue II Fund – The Village received a grant from the State of Ohio for a road project.

4. Enterprise Funds

These funds account for operations similar to private business enterprises, where management intends to recover the significant costs of providing certain goods or services through user charges. The Village had the following significant Enterprise Fund:

Water Fund - This fund receives charges for services from residents to cover water service costs.

5. Fiduciary Funds

Fiduciary funds include private purpose trust funds and agency funds. Trust funds account for assets held under a trust agreement for individuals, private organizations, or other governments which are not available to support the Village's own programs. The Village has no trust funds.

Agency funds are purely custodial in nature and are used to hold resources for individuals, organizations or other governments. The Village disburses these funds as directed by the individual, organization or other government. The Village's agency fund accounts for the activity of the Mayor's Court.

D. Budgetary Process

The Ohio Revised Code requires each fund (except certain agency funds) be budgeted annually.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (CONTINUED)

1. Appropriations

Budgetary expenditures (that is, disbursements and encumbrances) may not exceed appropriations at the fund or department level, and appropriations may not exceed estimated resources. The Village Council must annually approve appropriation measures and subsequent amendments. The County Budget Commission must also approve the annual appropriation measure. Unencumbered appropriations lapse at year end.

2. Estimated Resources

Estimated resources include estimates of cash to be received (budgeted receipts) plus unencumbered cash as of January 1. The County Budget Commission must also approve estimated resources.

3. Encumbrances

The Ohio Revised Code requires the Village to reserve (encumber) appropriations when individual commitments are made. Encumbrances outstanding at year end are carried over, and need not be reappropriated.

The Village did not encumber all commitments required by Ohio law. Management has included audit adjustments in the accompanying budgetary presentations for material items that should have been encumbered.

A summary of 2008 and 2007 budgetary activity appears in Note 3.

E. Property, Plant, and Equipment

The Village records disbursements for acquisitions of property, plant, and equipment when paid. The accompanying financial statements do not report these items as assets.

F. Accumulated Leave

In certain circumstances, such as upon leaving employment, employees are entitled to cash payments for unused leave. The financial statements do not include a liability for unpaid leave.

2. EQUITY IN POOLED DEPOSITS

The Village maintains a deposit pool all funds use. The Ohio Revised Code prescribes allowable deposits and investments. The carrying amount of deposits and investments at December 31 was as follows:

	2008	2007
Demand deposits	$1,436,877	$1,556,295

Deposits: Deposits are insured by the Federal Depository Insurance Corporation or collateralized by securities specifically pledged by the financial institution to the Village.

3. BUDGETARY ACTIVITY

Budgetary activity for the years ending December 31, 2008 and 2007 follows:

2008 Budgeted vs. Actual Receipts

Fund Type	Budgeted Receipts	Actual Receipts	Variance
General	$791,117	$572,419	($218,698)
Special Revenue	492,681	324,303	(168,378)
Capital Projects	885,477	446,771	(438,706)
Enterprise	500,670	536,387	35,717
Total	$2,669,945	$1,879,880	($790,065)

2008 Budgeted vs. Actual Budgetary Basis Expenditures

Fund Type	Appropriation Authority	Budgetary Expenditures	Variance
General	$1,154,926	$712,378	$442,548
Special Revenue	594,621	292,651	301,970
Capital Projects	735,453	437,724	297,729
Enterprise	656,797	673,356	(16,559)
Total	$3,141,797	$2,116,109	$1,025,688

2007 Budgeted vs. Actual Receipts

Fund Type	Budgeted Receipts	Actual Receipts	Variance
General	$582,939	$548,804	($34,135)
Special Revenue	670,895	463,133	(207,762)
Capital Projects	776,048	279,836	(496,212)
Enterprise	383,829	395,428	11,599
Total	$2,413,711	$1,687,201	($726,510)

2007 Budgeted vs. Actual Budgetary Basis Expenditures

Fund Type	Appropriation Authority	Budgetary Expenditures	Variance
General	$743,662	$623,375	$120,287
Special Revenue	750,338	496,147	254,191
Capital Projects	778,458	321,071	457,387
Enterprise	443,087	463,687	(20,600)
Total	$2,715,545	$1,904,280	$811,265

3. BUDGETARY ACTIVITY (CONTINUED)

Contrary to Ohio law, budgetary expenditures exceeded appropriation authority in the Water Fund by $130,584 for the year ended December 31, 2008 and by $45,532 for the year ended December 31, 2007.

4. RESORT TAX

The Village levies a resort tax of 1.5 percent on income arising from business activities conducted within the Village. Businesses submit the tax to the Ohio Department of Taxation. The Ohio Department of Taxation remits the tax to the Village monthly.

5. PROPERTY TAX

Real property taxes become a lien on January 1 preceding the October 1 date for which the Council adopted tax rates. The State Board of Tax Equalization adjusts these rates for inflation. Property taxes are also reduced for applicable homestead and rollback deductions. The financial statements include homestead and rollback amounts the State pays as Intergovernmental Receipts. Payments are due to the County by December 31. If the property owner elects to pay semiannually, the first half is due December 31. The second half payment is due the following June 20.

Public utilities are also taxed on personal and real property located within the Village.

Tangible personal property tax is assessed by the property owners, who must file a list of such property to the County by each April 30.

The County is responsible for assessing property, and for billing, collecting, and distributing all property taxes on behalf of the Village.

6. DEBT

Debt outstanding at December 31, 2008 was as follows

	Principal	Interest Rate
OWDA Water Line Project Loan	$162,471	5.90%
OWDA Water Treatment Plan Loan	868,956	1.50%
USDA Water System Loan	226,600	6.13%
OPWC Road Project Loan	28,853	0.00%
WSOS Water Line Project Loan	63,972	3.00%
Total	$1,350,852	

The Ohio Water Development Authority (OWDA) loans relate to water system improvements. The Water Line Project Loan was obtained in 1990 and will be repaid in semiannual installments, including interest, over a period of 20 years. The Water Treatment Plant Loan was obtained in 2001 and will be repaid in semiannual installment, including interest, over a period of 30 years. These loans are collateralized by water receipts. The USDA Water System Loan relates to water

6. DEBT – (CONTINUED)

system improvements for rural development. The loan was obtained in 1990 and will be repaid in annual installments over 40 years. The OPWC Road Project Loan was obtained in 2001 for a road improvement project and will be repaid in semiannual installments over 12 years. The WSOS Water Line Project Loan relates to a water line improvement project. The loan was obtained in 2008 and will be repaid in monthly installments over 10 years.

Amortization of the above debt, including interest, is scheduled as follows: double underline the total amounts.

Year ending December 31:	OWDA Water Line Project Loand	OWDA Water Treatment Plan Loan	USDA Water Ssystem Loan	OPWC Road Project Loan
2009	$32,937	$44,807	$19,679	$4,809
2010	32,937	44,806	19,724	4,809
2011	32,937	44,807	19,744	4,809
2012	32,937	44,807	19,740	4,809
2013	32,936	44,807	19,711	4,809
2014 - 2018	32,935	224,036	98,400	4,808
2019 - 2023		224,236	98,569	
2024 - 2028		224,036	98,516	
2029 - 2032		134,422	9,976	
Total	$197,619	$1,030,764	$404,059	$28,853

The Village made an additional principal payment on the WSOS Water Line Project Loan in the amount of $35,592 during the year ended December 31, 2008. To date, WSOS has not provided the Village with a revised amortization schedule that reflects the additional principal payment.

7. RETIREMENT SYSTEMS

The Village's full-time Police Officers belong to the Police and Fire Pension Fund (OP&F). Other employees belong to the Ohio Public Employees Retirement System (OPERS). OP&F and OPERS are cost-sharing, multiple-employer plans. The Ohio Revised Code prescribes these plans' benefits, which include postretirement healthcare and survivor and disability benefits.

The Ohio Revised Code also prescribes contribution rates. For 2008 and 2007, OP&F participants contributed 10% of their wages. For 2008 and 2007, the Village contributed to OP&F an amount equal to 19.5% of full-time police members' wages. For 2008 and 2007, OPERS members contributed 9.5 and 10%, respectively, of their gross salaries and the Village contributed an amount equaling 13.85 and 14%, respectively, of participants' gross salaries. The Village has paid all contributions required through December 31, 2008.

8. RISK MANAGEMENT

Risk Pool Membership

The Village is exposed to various risks of property and casualty losses, and injuries to employees.

The Village insures against injuries to employees through the Ohio Bureau of Worker's Compensation.

The Village belongs to the Public Entities Pool of Ohio (PEP), a risk-sharing pool available to Ohio local governments. PEP provides property and casualty coverage for its members. PEP is a member of the American Public Entity Excess Pool (APEEP). Member governments pay annual contributions to fund PEP. PEP pays judgments, settlements and other expenses resulting from covered claims that exceed the members' deductibles.

<u>Casualty Coverage</u>
For an occurrence prior to January 1, 2006 PEP retains casualty risks up to $250,000 per occurrence, including claim adjustment expenses. PEP pays a percentage of its contributions to APEEP. APEEP reinsures claims exceeding $250,000, up to $1,750,000 per claim and $10,000,000 in the aggregate per year.

For an occurrence on or subsequent to January 1, 2006, the Pool retains casualty risk up to $350,000 per occurrence. Claims exceeding $350,000 are reinsured with APEEP in an amount not to exceed $2,650,000 for each claim and $10,000,000 in the aggregate per year. Governments can elect up to $10,000,000 in additional coverage with the General Reinsurance Corporation, through contracts with PEP.

If losses exhaust PEP's retained earnings, APEEP provides *excess of funds available* coverage up to $5,000,000 per year, subject to a per-claim limit of $2,000,000 (prior to January 1, 2006) or $3,000,000 (on or subsequent to January 1, 2006) as noted above.

<u>Property Coverage</u>
Beginning in 2005, APEEP established a risk-sharing property program. Under the program, Travelers reinsures specific losses exceeding $250,000 up to $600 million per occurrence. This amount was increased to $300,000 in 2007. For 2007, APEEP reinsures members for specific losses exceeding $100,000 up to $300,000 per occurrence, subject to an annual aggregate loss payment. For 2006, APEEP reinsures members for specific losses exceeding $100,000 up to $250,000 per occurrence, subject to an annual aggregate loss payment. Travelers provides aggregate stop-loss coverage based upon the combined members' total insurable values. If the stop loss is reached by payment of losses between $100,000 and $250,000 in 2006, or $100,000 and $300,000 in 2007, Travelers will then reinsure specific losses exceeding $100,000 up to their $600 million per occurrence limit. The aggregate stop-loss limit for 2007 was $2,014,548.

The aforementioned casualty and property reinsurance agreements do not discharge PEP's primary liability for claims payments on covered losses. Claims exceeding coverage limits are the obligation of the respective government.

8. RISK MANAGEMENT – (CONTINUED)

Property and casualty settlements did not exceed insurance coverage for the past three fiscal years.

Financial Position

PEP's financial statements (audited by other accountants) conform with generally accepted accounting principles, and reported the following assets, liabilities and retained earnings at December 31, 2007 and 2006 (the latest information available):

	2007	2006
Assets	$37,560,071	$36,123,194
Liabilities	(17,340,825)	(16,738,904)
Net Assets	$20,219,246	$19,384,290

At December 31, 2007 and 2006, respectively, the liabilities above include approximately $15.9 million and $15.0 million of estimated incurred claims payable. The assets and retained earnings above also include approximately $15.0 million and $14.4 million of unpaid claims to be billed to approximately 443 member governments in the future, as of December 31, 2007 and 2006, respectively. These amounts will be included in future contributions from members when the related claims are due for payment. The Village's share of these unpaid claims collectible in future years is approximately $44,000. This payable includes the subsequent year's contribution due if the Village terminates participation, as described in the last paragraph below.

Based on discussions with PEP, the expected rates PEP charges to compute member contributions, which are used to pay claims as they become due, are not expected to change significantly from those used to determine the historical contributions detailed below. By contract, the annual liability of each member is limited to the amount of financial contributions required to be made to PEP for each year of membership.

Contributions to PEP	
2005	$34,262
2006	$33,648
2007	$37,617

After completing one year of membership, members may withdraw on each anniversary of the date they joined PEP provided they provide written notice to PEP 60 days in advance of the anniversary date. Upon withdrawal, members are eligible for a full or partial refund of their capital contributions, minus the subsequent year's budgetary contribution. Withdrawing members have no other future obligation to the pool. Also upon withdrawal, payments for all casualty claims and claim expenses become the sole responsibility of the withdrawing member, regardless of whether a claim occurred or was reported prior to the withdrawal.

9. CONTINGENT LIABILITIES

Amounts grantor agencies pay to the Village are subject to audit and adjustment by the grantor, principally the federal government. The grantor may require refunding any disallowed costs. Management cannot presently determine amounts grantors may disallow. However, based on prior experience, management believes any refunds would be immaterial.

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INDEPENDENT ACCOUNTANTS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS REQUIRED BY *GOVERNMENT AUDITING STANDARDS*

Village of Kelleys Island
Erie County
121 Addison Street, P.O. Box 469
Kelleys Island, Ohio 43438-0469

To the Village Council:

We have audited the financial statements of the Village of Kelleys Island, Erie County, (the Village) as of and for the years ended December 31, 2008 and 2007, and have issued our report thereon dated November 10, 2009, wherein we noted the Village followed accounting practices the Auditor of State prescribes rather than accounting principles generally accepted in the United States of America. 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 the Comptroller General of the United States' *Government Auditing Standards*.

Internal Control over Financial Reporting

In planning and performing our audits, we considered the Village's internal control over financial reporting as a basis for designing our audit procedures for expressing our opinion on the financial statements, but not to opine on the effectiveness of the Village's internal control over financial reporting. Accordingly, we have not opined on the effectiveness of the Village's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Village's ability to initiate, authorize, record, process, or report financial data reliably in accordance with its applicable accounting basis, such that there is more than a remote likelihood that the Village's internal control will not prevent or detect a more-than-inconsequential financial statement misstatement.

We consider findings 2008-001 and 2008-002 described in the accompanying schedule of findings to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies resulting in more than a remote likelihood that the Village's internal control will not prevent or detect a material financial statement misstatement.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and accordingly, would not necessarily disclose all significant deficiencies that are also material weaknesses. We believe the significant deficiencies described above are also material weaknesses.

We also noted certain internal control matters that we reported to the Village's management in a separate letter dated November 10, 2009.

Compliance and Other Matters

As part of reasonably assuring whether the Village's financial statements are free of material misstatement, we tested its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could directly and materially affect the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audits and accordingly, we do not express an opinion. The results of our tests disclosed instances of noncompliance that we must report under *Government Auditing Standards* which are described in the accompanying schedule of findings as items 2008-002 through 2008-003.

We intend this report solely for the information and use of the audit committee, management, and the Village Council. We intend it for no one other than these specified parties.

Mary Taylor

Mary Taylor, CPA
Auditor of State

November 10, 2009

VILLAGE OF KELLEYS ISLAND
ERIE COUNTY

SCHEDULE OF FINDINGS
DECEMBER 31, 2008 AND 2007

FINDINGS RELATED TO THE FINANCIAL STATEMENTS
REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS

FINDING NUMBER 2008-001

Material Weakness

Financial Reporting

As a result of audit procedures performed, the following errors were noted in the financial statements that required audit adjustments for the year ending December 31, 2008:

- Approved appropriations differed from amounts posted to the Village's accounting system by $72,014 in the General Fund, $191,223 in the Capital Projects Fund Type and $138,813 in the Enterprise Fund Type. These amounts have been appropriately adjusted in the notes to the financial statements.
- The Village improperly accounted for $35,600 in special assessments revenue and debt service payments in a newly created special revenue fund. These amounts along with budgeted receipts and appropriations of $98,668 were reclassified into the Water Fund.

As a result of audit procedures performed, the following errors were noted in the financial statements that required audit adjustments for the year ending December 31, 2007:

- Approved appropriations differed from amounts posted to the Village's accounting system by $127,113 in the Special Revenue Fund Type. This amount has been appropriately adjusted in the notes to the financial statements.

Sound financial reporting is the responsibility of the Clerk-Treasurer and Village Council and is essential to ensure the information provided to the readers of the financial statements and accompanying notes is complete and accurate.

To ensure the Village's financial statements and notes to the statements are complete and accurate, the Village should adopt policies and procedures, including a final review of the statements and notes by the Clerk-Treasurer and Village Council to identify and correct errors and omissions. Also, the Clerk-Treasurer can refer to the Ohio Village Officer's Handbook at the following web site address for guidance on the posting of transactions http://www.auditor.state.oh.us/LGS/Publications/LocalGovernmentManualsHandbooks/village_officers_handbook.pdf

FINDING NUMBER 2008-002

Noncompliance Citation/Material Weakness

Ohio Revised Code § 5705.41 (D)(1) prohibits a subdivision or taxing authority from making any contract or ordering any expenditure of money unless a certificate signed by the fiscal officer is attached thereto. The fiscal officer must certify the amount required to meet any such contract or expenditure has been lawfully appropriated and is in the treasury, or in the process of collection to the credit of an appropriate fund free from any previous encumbrance.

There are several exceptions to the standard requirement above that a fiscal officer's certificate must be obtained prior to a subdivision or taxing authority entering into a contract or order involving the expenditure of money. The main exceptions are: "then and now" certificates, blanket certificates, and super blanket certificates, which are provided for in sections 5705.41(D)(1) and 5705.41(D)(3), respectively, of the Ohio Revised Code.

A. **"Then and Now" certificate -** If the fiscal officer can certify both at the time the contract or order was made ("then"), and at the time the fiscal officer is completing the certification ("now"), sufficient funds were available or in the process of collection, to the credit of a proper fund, properly appropriated and free from any previous encumbrance, the taxing authority can authorize the drawing of a warrant for the payment of the amount due. The taxing authority has thirty days from the receipt of the "then and now" certificate to approve payment by ordinance or resolution.

Amounts of less than $3,000 may be paid by the fiscal officer without a resolution or ordinance upon completion of the "then and now" certificate, provided the expenditure is otherwise lawful. This does not eliminate any otherwise applicable requirement for approval of expenditures by the taxing authority.

B. **Blanket Certificate** – Fiscal officers may prepare "blanket" certificates not exceeding an amount established by resolution or ordinance adopted by the legislative authority against any specific line item account over a period not exceeding three months or running beyond the current fiscal year. The blanket certificates may, but need not, be limited to a specific vendor. Only one blanket certificate may be outstanding at one particular time for any particular line item appropriation.

C. **Super Blanket Certificate** – The taxing authority may also make expenditures and contracts for any amount from a specific line-item appropriation account in a specified fund upon certification of the fiscal officer for most professional services, fuel, oil, food items, and any other specific recurring and reasonably predictable operating expense. This certification is not to extend beyond the current year (or quarterly spending plan for counties). More than one super blanket certificate may be outstanding at a particular time for any line item appropriation.

The Clerk-Treasurer did not properly certify the availability of funds prior to purchase commitment for 20 percent of expenditures we tested and there was no evidence the Village followed the aforementioned exceptions. The failure to properly certify the availability of funds can result in overspending funds and negative cash fund balances. In addition, the Village had $63,233 in outstanding purchase commitments as of December 31, 2007, that were not certified at year end. The accompanying budgetary presentations and financial statements have been adjusted to reflect this amount as an outstanding encumbrance at year end in the Water Fund.

FINDING NUMBER 2008-002
(Continued)

Unless the exceptions noted above are used, prior certification is not only required by statute but is a key control in the disbursement process to assure purchase commitments receive prior approval. To improve controls over disbursements and to help reduce the possibility of the Village's funds exceeding budgetary spending limitations, we recommend the Clerk-Treasurer certify the funds are or will be available prior to obligation by the Village. When prior certification is not possible, "then and now" certification should be used, with appropriate legislative approval following within thirty days.

We recommend the Clerk-Treasurer certify all purchases to which section 5705.41(D) applies. The Clerk-Treasurer should sign the certification at the time the Village incurs a commitment, and only when the requirements of 5705.41 (D) are satisfied. The Clerk-Treasurer should post approved purchase commitments to the proper appropriation code, to reduce the available appropriation.

FINDING NUMBER 2008-003

Noncompliance Citation

Ohio Revised Code § 5705.41(B) prohibits a subdivision from making an expenditure unless it has been properly appropriated.

As of December 31, 2008, Water Fund expenditures of $568,390 exceeded appropriations of $437,806 by $130,584.

As of December 31, 2007, Water Fund expenditures of $408,805 exceeded appropriations of $363,273 by $45,532.

The Clerk-Treasurer should not certify the availability of funds and should deny payment requests exceeding appropriations. The Treasurer may request the Village Council to approve increased expenditure levels by increasing appropriations and amending estimated resources, if necessary.

Officials' Response:
We did not receive a response from Officials to the findings reported above.

VILLAGE OF KELLEYS ISLAND
ERIE COUNTY

SCHEDULE OF PRIOR AUDIT FINDINGS
DECEMBER 31, 2008 AND 2007

Finding Number	Finding Summary	Fully Corrected?	Not Corrected, Partially Corrected; Significantly Different Corrective Action Taken; or Finding No Longer Valid; ***Explain***
2006-001	Federal Grants Management	Yes	

Mary Taylor, CPA
Auditor of State

VILLAGE OF KELLEYS ISLAND

ERIE COUNTY

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

CERTIFIED
DECEMBER 1, 2009

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