



PRIOR LAKE FIRE RELIEF ASSOCIATION
PRIOR LAKE, MINNESOTA

MANAGEMENT LETTER

YEAR ENDED
DECEMBER 31, 2008



11 Civic Center Plaza
Suite 300
P.O. Box 3166
Mankato, MN 56002-3166

Board of Trustees
Prior Lake Fire Relief Association
Prior Lake, Minnesota

We have audited the financial statements of the governmental and fiduciary activities of the Prior Lake Fire Relief Association (the Association) for the year ended December 31, 2008, and have issued our report thereon dated June 5, 2009. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility under Auditing Standards Generally Accepted in the United States of America

As stated in our engagement letter, our responsibility, as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve you or management of your responsibilities.

Our responsibility is to plan and perform the audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement.

As part of our audit, we considered the internal control of the Association. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

Significant Audit Findings

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

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects the Association's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Association's financial statements, that is more than inconsequential, will not be prevented or detected by the Association's internal control. We consider the following deficiencies to be significant deficiencies in internal control:



2008-1 Segregation of Duties (Finding Since 2007)

- Condition: During our audit we reviewed procedures over cash disbursements, cash receipts and investment transactions and found the Association to have limited segregation of duties related to these areas.
- Criteria: There are four general categories of duties: authorization, custody, recordkeeping and reconciliation. In an ideal system, different employees perform each of these four major functions. In other words, no one person has control of two or more of these responsibilities.
- Effect: The existence of this limited segregation of duties increases the risk of fraud.

Internal Control over Cash Disbursements

- Cause: As a result of the small number of volunteers, the Treasurer controls and maintains the check stock, opens the mail, sets up and maintains vendors, approves bills for payment, prepares checks, signs the checks in conjunction with the secretary or vice president, mails checks to vendors, maintains the accounts payable records, posts transactions to the general ledger, and reconciles bank accounts.
- Recommendation: While we recognize the volunteer pool is not large enough to eliminate this deficiency, we recommend that an individual, separate from the Treasurer, review the cancelled checks received with the bank statement and investigate items such as; voided checks, inconsistencies in check sequence, possible alterations, and unusual payees. This individual should also review bank reconciliations for accuracy and timeliness of preparation. It is important that the Trustees are aware of this condition and that they monitor all financial information.

Updated Progress From Prior Year

The secretary reviews the bank statements and all items received in the mail before giving it to the treasurer.

Internal Control over Cash Receipts

- Cause: As a result of the small number of volunteers, the Treasurer opens the mail, receives and endorses checks and currency, prepares and takes the deposit to the bank, sets up and maintains customers (if needed), maintains accounts receivable records, posts transactions to the general ledger, and reconciles bank accounts.
- Recommendation: While we recognize the volunteer pool is not large enough to eliminate this deficiency, we recommend that an individual, separate from the Treasurer, open the mail and prepare the deposit. Two people should handle the money at fundraising events. After verifying the total amount to deposit, one of these volunteers should initial the bank deposit and another member should take the money to the bank. The Treasurer should verify that the amount was initialed and deposited in a timely manner by reviewing the bank statement and deposit slip, at the end of the month. It is important that the Trustees are aware of this condition and monitor all financial information.

Updated Progress From Prior Year

Two members of the fundraising committee count the money, agree on the total amount collected, then give the money to the treasurer to deposit.

**2008-1 Segregation of Duties (Finding Since 2007) - Continued****Internal Control over Investment Transactions**

Cause: As a result of the small number of volunteers, the Treasurer receives investment statements in the mail, initiates investment transactions, maintains and posts activity to the general ledger, and reconciles investment accounts.

Recommendation: While we recognize the volunteer pool is not large enough to eliminate this deficiency, it is important that the Trustees are aware of this condition and monitor all financial information.

Updated Progress From Prior Year:

Management agrees with recommendations and will continue to monitor all financial information.

2008-2 Financial Report Preparation

Condition: As in prior years, we were requested to draft the audited financial statements and related footnote disclosures as part of our regular audit services. Recent auditing standards require auditors to communicate this situation to the Board as an internal control deficiency. Ultimately, it is management's responsibility to provide for the preparation of your statements and footnotes, and the responsibility of the auditor to determine the fairness of presentation of those statements. From a practical standpoint we do both for you at the same time in connection with our audit. This is not unusual for us to do with Associations of your size. However, based on recent auditing standards, it is our responsibility to inform you that this deficiency could result in a material misstatement to the financial statements that could have been prevented or detected by your management. Essentially, the auditors cannot be part of your internal control process.

Criteria: Internal controls should be in place to provide reasonable assurance over financial reporting.

Cause: From a practical standpoint we do both for you at the same time in connection with our audit. This is not unusual for us to do with Associations of your size.

Effect: The effectiveness of the internal control system relies on enforcement by management. The effect of deficiencies in internal controls can result in undetected errors in financial reporting.

Recommendation: Under these circumstances, the most effective controls lie in management's knowledge of the Association's financial operations. It is the responsibility of management and those charged with governance to make the decision whether to accept the degree of risk associated with this condition because of cost and other considerations. Regarding the specific situation listed above, we would offer the following specific recommendation: 1) Utilize a disclosure checklist to ensure all required disclosures are present and agree to work papers, and 2) Agree your checking and investment information to the amounts reported in the financial statements plus or minus any applicable accruals.

Management Response

For now, the Association's management accepts the degree of risk associated with this condition and thoroughly reviews a draft of the financial statements.



A material weakness is a significant deficiency, or combination of significant deficiencies, that result in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control. We believe the deficiencies described above do not constitute material weaknesses.

As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of compliance with certain provisions of Minnesota statutes. However, the objective of our tests was not to provide an opinion on compliance with such provisions. We noted no instance of noncompliance with Minnesota statutes.

Planned Scope and Timing of the Audit

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

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the Association are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year. We noted no transactions entered into by the governmental unit during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimate affecting the financial statements was the actuarial accrued liability. This is based on the funding formula prescribed by the State of Minnesota. We evaluated the key factors and assumptions used to develop the estimate in determining that it is reasonable in relation to the financial statements taken as a whole.

The disclosures in the financial statements are neutral, consistent, and clear. Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. There were no misstatements noted during the audit.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting or auditing matter that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated June 5, 2009.



Other Matters

Our principal observations and recommendations are summarized below. These recommendations resulted from our observations made in connection with our audit of the Association’s financial statements for the year ended December 31, 2008.

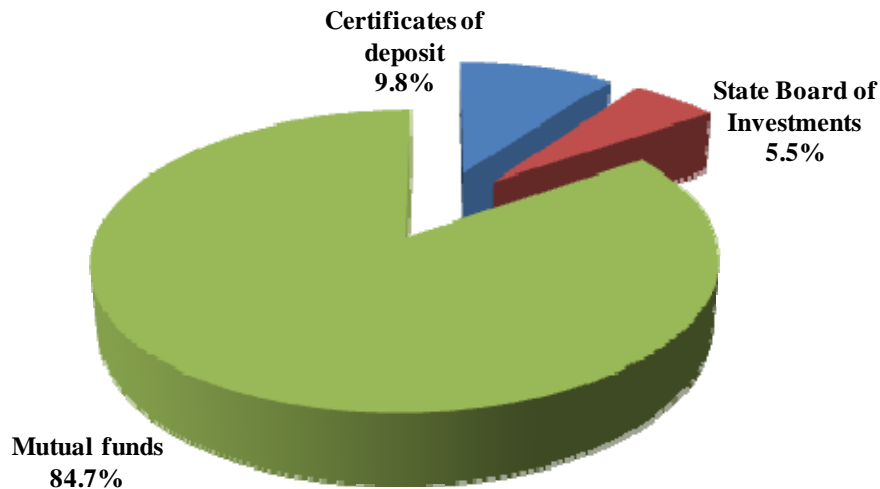
Financial Position

Investments

Investments for the Association for 2008 totaled \$1,685,391. This is a decrease of 27.8 percent under the 2007 investments of \$2,334,791. *This information is also presented in graphic form below.*

Investment	2008	Percent of Total	2007	Increase (Decrease) From 2007
Cash and cash equivalents	\$ 544	- %	\$ 442	\$ 102
Certificates of deposit	165,000	9.8	49,809	115,191
State Board of Investments	93,212	5.5	156,137	(62,925)
Mutual funds	1,426,635	84.7	2,128,403	(701,768)
Total investments	\$ 1,685,391	100.0 %	\$ 2,334,791	\$ (649,400)

Investments



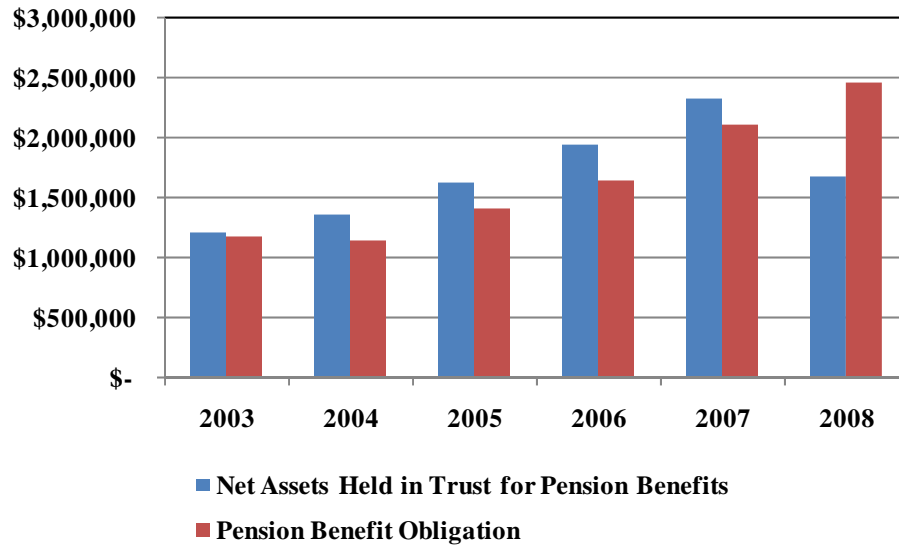


Net Assets and Accrued Pension Liability Comparison

A comparison of net assets and accrued pension liability for the past six years is as follows:

Year	Net Assets Held in Trust for Pension Benefits	Pension Benefit Obligation	Pension Percentage Funded	Funded Pension Benefits Obligation
2003	\$ 1,209,111	\$ 1,184,154	102.1 %	\$ 24,957
2004	1,362,132	1,145,542	118.9	216,590
2005	1,630,142	1,411,697	115.5	218,445
2006	1,958,241	1,652,010	118.5	306,231
2007	2,334,978	2,122,529	110.0	212,449
2008	1,686,933	2,474,055	68.2	(787,122)

Net Assets and Accrued Pension Liability



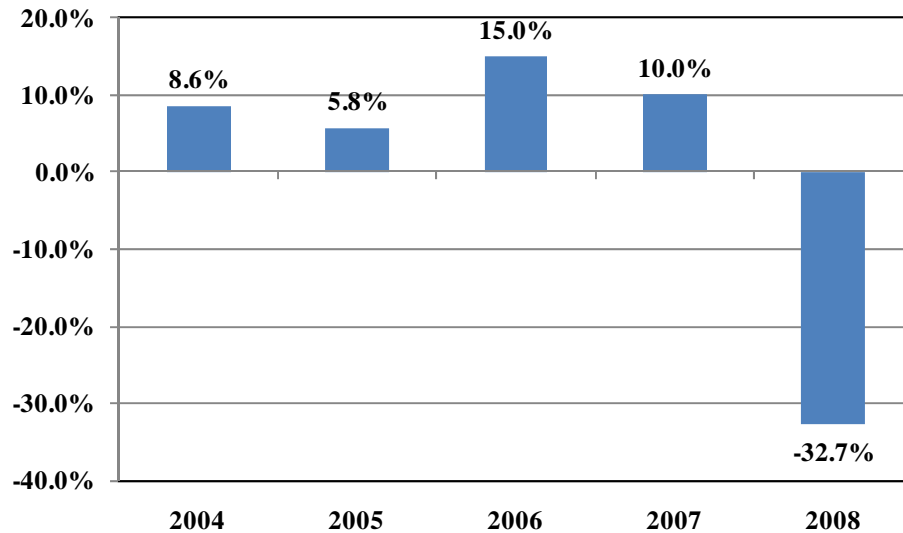


Rates of Return

The Association's investment rates of return are based on the total investment income as a percentage of the total net assets held in trust for pension benefits.

Year	Interest and Dividends	Appreciation of Investments	Total Investment Income	Net Assets Held in Trust for Pension Benefits	Investment Rate of Return
2004	\$ 18,020	\$ 85,425	\$ 103,445	\$ 1,362,132	8.6
2005	28,026	50,317	78,343	1,630,142	5.8
2006	42,306	201,766	244,072	1,958,241	15.0
2007	61,937	134,346	196,283	2,334,978	10.0
2008	64,922	(827,954)	(763,032)	1,686,933	(32.7) %

Investment Rates of Return



Other Matters

As of December 31, 2008, there was an accounts receivable balance of \$1,000. This amount is due from the State for supplemental benefit reimbursement for the pension payout to Dave Chromy. Form SBR should be completed and sent to the Minnesota Department of Revenue in order to receive this reimbursement.



Peer Group Comparisons

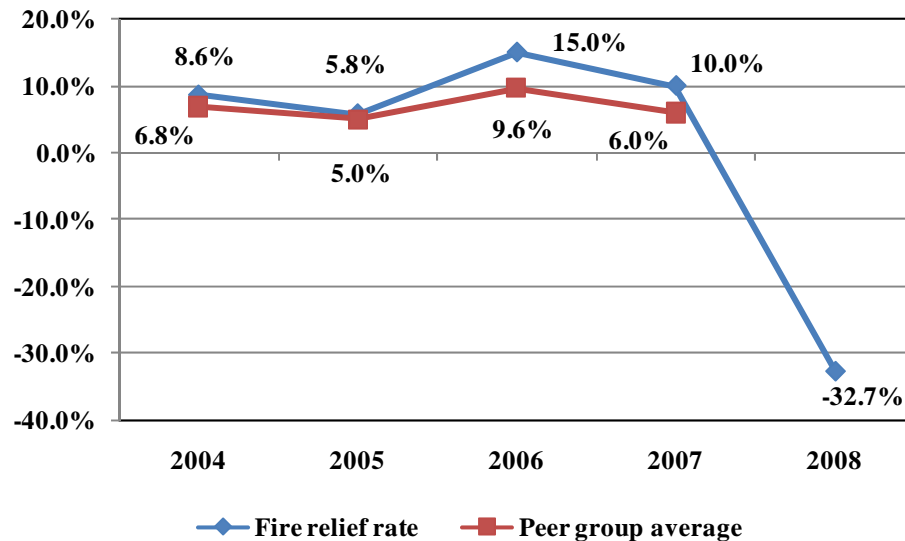
The following are two comparisons of statistics that will provide information on how your organization compares with other fire relief associations around the state. We used averages from approximately 60 fire relief associations with under \$200,000 in assets to several million in assets. These averages include a 5-year trend of the rate of return and a 5-year trend of funding percentage as compared to averages of the other 60 relief associations.

Averages	Calculation	Year				
		2004	2005	2006	2007	2008
Average rate of returns	Net investment income/ beginning net assets	8.6%	5.8%	15.0%	10.0%	-32.7%
		6.8%	5.0%	9.6%	6.0%	N/A
Percentage funded	Net assets/accrued liability	118.9%	115.5%	118.5%	110.0%	68.2%
		108.1%	104.1%	110.0%	109.8%	N/A

Prior Lake Fire Relief
Peer Group

Rate of Return

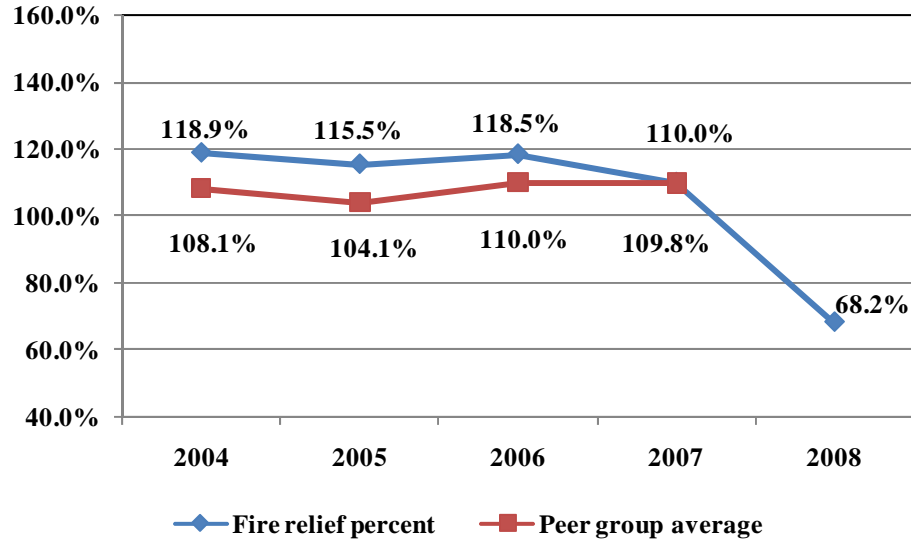
The rate of return is calculated by taking the net investment income and dividing it by the beginning net assets. This graph shows a trend of your returns over a 5 year period in relationship to other relief associations.





Funding Percentage

The funding percentage is calculated by taking the Special fund net assets and dividing it by the accrued pension liability. This graph shows your funding percentage for a 5-year period in comparison to other relief associations.



Market Concerns

There was a significant downturn in the investment income during the 4th Quarter of 2008 that resulted in considerable losses. The State decreased state aid by approximately 14 percent in 2008 with possible additional cuts in 2009. This decrease was due to past overstated amounts of insurance premiums that dealt with fire insurance and fewer taxes collected on insurance premiums. Fire state aid is a dedicated fund and the decrease is not due to the large budget deficit the State is currently facing. These decreases will have a significant impact on the required municipal contributions in future years until the market changes.

Best Practices in Monitoring Investment Results

The Board has a fiduciary responsibility to its membership related to its assets. In order to communicate relevant information to membership, we recommend the following:

- **Investment performance should be benchmarked and reviewed with membership**
 - We believe this can easily be addressed by more frequent reporting that uses complete financial information and appropriate investment benchmarks. With better information, more timely and prudent investment decisions can be made. We have provided a table for analysis in this letter. We recommend that the Board consider other performance measures and develop a strategy to report on them.
- **Investment policies should be developed and reviewed annually**
 - We recommend that the Association develop and/or review investment policies. Policies should:
 1. Contain enough detail to implement a specific investment strategy
 2. Outline the duties and responsibilities of all parties
 3. Set forth portfolio diversification, rebalancing and risk guidelines
 4. Incorporate specific, measurable investment objectives or benchmarks

We can assist with the implementation of either of these items.



* * * * *

This report is intended solely for the information and use of the members of the Board of Trustees, management, others within the administration of the Association and the Minnesota Office of the State Auditor, and is not intended to be and should not be used by anyone other than those specified parties.

The comments and recommendation in this report are purely constructive in nature, and should be read in this context and are not intended to be and should not be used by anyone other than these specified parties. Our audit would not necessarily disclose all weaknesses in the system because it was based on selected tests of the accounting records and related data.

If you have any questions or wish to discuss any of the items contained in this letter, please feel free to contact us at your convenience. We wish to thank you for the continued opportunity to be of service, and for the courtesy and cooperation extended to us by your staff.

June 5, 2009
Mankato, Minnesota

Abdo, Eick & Meyers, LLP
ABDO, EICK & MEYERS, LLP
Certified Public Accountants