

**OFFICE OF
STATE AUDITOR**

AUDIT REPORT

**CITY OF HILLSBORO
HILLSBORO, NORTH DAKOTA**

FOR THE YEAR ENDED DECEMBER 31, 2010



CITY OF HILLSBORO
Hillsboro, North Dakota

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December 31, 2010

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CITY OF HILLSBORO
Hillsboro, North Dakota

CITY OFFICIALS

December 31, 2010

Mark Forseth

President

Curt Kaufman
Lorraine Tibbert
Charles Stock
Dave Sather

Vice-President
Board Member
Board Member
Board Member

Lesley Connelly

Auditor

Becky Foss

Deputy Auditor

John Juelson

Attorney

STATE AUDITOR

ROBERT R. PETERSON
Phone (701) 328-2241
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Local Government Division:
FARGO OFFICE
MANAGER – DAVID MIX
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STATE OF NORTH DAKOTA
OFFICE OF THE STATE AUDITOR
STATE CAPITOL
600 E. BOULEVARD AVENUE - DEPT. 117
BISMARCK, NORTH DAKOTA 58505

INDEPENDENT AUDITOR'S REPORT

City Commission
City of Hillsboro
Hillsboro, North Dakota 58045

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hillsboro, North Dakota, as of and for the year ended December 31, 2010, which collectively comprise the City's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the City of Hillsboro, North Dakota's, management. Our responsibility is to express opinions on these financial statements based on our audit.

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

As discussed in Note 1, the City of Hillsboro, North Dakota, prepares its financial statements on the modified cash basis, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the financial statements, management has not recorded capital assets in the governmental activities, the business-type activities and the major business-type funds and accordingly, has not recorded depreciation expense on those assets. Accounting principles generally accepted in the United States of America require that capital assets be capitalized and depreciated, which would increase the assets, net assets and expenses of the governmental activities, the business-type activities and the major business-type funds. The amount by which this departure would affect the assets, net assets and expenses of the governmental activities, the business-type activities and the business-type funds is not reasonably determinable.

In our opinion, because of the effects of the matter discussed in the preceding paragraph, the financial statements referred to above do not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of the governmental activities, the business-type activities and the major business-type funds of the City of Hillsboro, North Dakota, as of December 31, 2010, and the changes in financial position thereof for the year then ended.

In addition, in our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position modified cash basis of each major governmental fund, and the aggregate remaining fund information of the governmental funds and business-type funds of the City of Hillsboro, North Dakota, as of December 31, 2010, and the respective changes in financial position modified cash basis thereof, for the year then ended in conformity with the basis of accounting described in Note 1.

CITY OF HILLSBORO

Independent Auditor's Report - Continued

In accordance with *Government Auditing Standards*, we have also issued our report dated March 12, 2012, on our consideration of the City of Hillsboro's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The *budgetary comparison information* on pages 25 through 27 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

The City of Hillsboro, North Dakota, has not presented the management's discussion and analysis that accounting principles generally accepted in the United States has determined is necessary to supplement, although not required to be part of, the basic financial statements.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Hillsboro's basic financial statements. The schedule of fund activity and schedule of expenditures of federal awards as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations* are presented for purposes of additional analysis and are not a required part of the basic financial statements. The schedule of fund activity and the schedule of expenditures of federal awards have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole on the basis of accounting described in Note 1.



Robert R. Peterson
State Auditor

March 12, 2012

CITY OF HILLSBORO
Hillsboro, North Dakota

STATEMENT OF NET ASSETS - MODIFIED CASH BASIS
December 31, 2010

	Primary Government		
	Governmental Activities	Business-type Activities	Total
ASSETS:			
Cash	\$ 876,316	\$ 270,941	\$ 1,147,257
Investments	122,107	757,684	879,791
Other Assets	-	72	72
Total Assets	\$ 998,423	\$ 1,028,697	\$ 2,027,120
LIABILITIES:			
Benefits Payable	\$ 1,792	\$ -	\$ 1,792
Long-Term Liabilities:			
Due Within One Year:			
Special Assessment Bonds Payable	435,000	-	435,000
Revenue Bonds Payable	-	115,000	115,000
State Revolving Loan Fund Payable	-	-	-
Due After One Year:			
Special Assessment Bonds Payable	5,670,000	-	5,670,000
Revenue Bonds Payable	-	1,519,129	1,519,129
State Revolving Loan Fund Payable	371,478	-	371,478
Total Liabilities	\$ 6,478,270	\$ 1,634,129	\$ 8,112,399
NET ASSETS:			
Restricted for:			
Debt Service	\$ 572,762	\$ -	\$ 572,762
Special Purposes	439,543	-	439,543
Unrestricted	(6,492,152)	(605,432)	(7,097,584)
Total Net Assets	\$ (5,479,847)	\$ (605,432)	\$ (6,085,279)

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

CITY OF HILLSBORO
Hillsboro, North Dakota

STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS
For the Year Ended December 31, 2010

Functions/Programs	Program Revenues			Net (Expense) Revenue and Changes in Net Assets		
	Expenses	Charges for Services	Operating Grants and Contributions	Primary Government		Total
				Governmental Activities	Business-Type Activities	
<u>Governmental Activities:</u>						
General Government	\$ 254,124	\$ 22,419	\$ -	\$ (231,705)	\$ -	\$ (231,705)
Public Safety	137,751	740	-	(137,011)	-	(137,011)
Public Works/Infrastructure	193,240	16,230	103,445	(73,565)	-	(73,565)
Culture and Recreation	61,260	12,334	-	(48,926)	-	(48,926)
Economic Development	9,219	-	-	(9,219)	-	(9,219)
Miscellaneous	149,305	-	-	(149,305)	-	(149,305)
Capital Outlay	232,114	-	-	(232,114)	-	(232,114)
Interest on Long-Term Debt	269,740	-	-	(269,740)	-	(269,740)
Total Governmental Activities	\$ 1,306,753	\$ 51,723	\$ 103,445	\$ (1,151,585)	\$ -	\$ (1,151,585)
<u>Business-Type Activities:</u>						
Water Projects 425	\$ 47,475	\$ 26	\$ -	\$ -	\$ (47,449)	\$ (47,449)
Regional Water Treatment 430	249,932	-	-	-	(249,932)	(249,932)
Water Tower Construction 431	1,067,979	-	-	-	(1,067,979)	(1,067,979)
Water Department 601	160,131	286,689	-	-	126,558	126,558
Sewer Department 602	73,307	104,393	-	-	31,086	31,086
Electric Department 604	1,531,904	1,692,120	-	-	160,216	160,216
Non-Major Enterprise Funds	196,219	294,461	-	-	98,242	98,242
Total Business-Type Activities	\$ 3,326,947	\$ 2,377,689	\$ -	\$ -	\$ (949,258)	\$ (949,258)
Total Primary Government	\$ 4,633,700	\$ 2,429,412	\$ 103,445	\$ (1,151,585)	\$ (949,258)	\$ (2,100,843)
<u>General Revenues:</u>						
Taxes:						
Property taxes levied for general purposes	\$ 100,328	\$ -	\$ 100,328			
Tax increment financing taxes	8,578	-	8,578			
Property taxes levied for special purposes	86,189	-	86,189			
Property taxes levied for debt service	653,066	-	653,066			
Sales taxes	272,617	-	272,617			
State Aid Distribution	84,441	-	84,441			
Interest Income	11,650	9,284	20,934			
Miscellaneous Revenue	53,670	12,991	66,661			
Transfers	198,672	(198,672)	-			
Total General Revenues and Transfers	\$ 1,469,211	\$ (176,397)	\$ 1,292,814			
Change in Net Assets	\$ 317,626	\$ (1,125,655)	\$ (808,029)			
Net Assets - January 1	\$ (5,909,028)	\$ 631,778	\$ (5,277,250)			
Prior Period Adjustment	111,555	(111,555)	-			
Net Assets - January 1, as restated	\$ (5,797,473)	\$ 520,223	\$ (5,277,250)			
Net Assets - December 31	\$ (5,479,847)	\$ (605,432)	\$ (6,085,279)			

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

CITY OF HILLSBORO
Hillsboro, North Dakota

BALANCE SHEET - MODIFIED CASH BASIS
GOVERNMENTAL FUNDS
For the Year Ended December 31, 2010

	Major Funds					
	General Fund	Highway Tax Fund	City Sales Tax Fund	2008 Highway 200 Project	2007-1 Street Project	Riverbend
<u>ASSETS</u>						
Cash and Cash Equivalents	\$ -	\$ 57	\$ 11,961	\$ -	\$ -	\$ 35,315
Investments	-	-	-	-	-	122,107
Due from Other Funds	-	74,374	267,146	-	-	-
Total Assets	\$ -	\$ 74,431	\$ 279,107	\$ -	\$ -	\$ 157,422
<u>LIABILITIES AND FUND BALANCES</u>						
<u>Liabilities:</u>						
Benefits Payable	\$ 1,522	\$ 40	\$ -	\$ -	\$ -	\$ -
Due to Other Funds	11,993	-	-	108,426	171,412	-
Total Liabilities	\$ 13,515	\$ 40	\$ -	\$ 108,426	\$ 171,412	\$ -
<u>Fund Balances:</u>						
Reserved for Debt Service	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 157,422
Unreserved, reported in:						
General Fund	(13,515)	-	-	-	-	-
Special Revenue Funds	-	74,391	279,107	-	-	-
Capital Projects Funds	-	-	-	(108,426)	(171,412)	-
Total Fund Balances	\$ (13,515)	\$ 74,391	\$ 279,107	\$ (108,426)	\$ (171,412)	\$ 157,422
Total Liabilities and Fund Balances	\$ -	\$ 74,431	\$ 279,107	\$ -	\$ -	\$ 157,422

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

2008 Highway 200	2007 Streets	Prairieview	Other Governmental Funds	Total Governmental Funds
\$ 130,491	\$ 456,212	\$ -	\$ 242,280	\$ 876,316
-	-	-	-	122,107
-	-	-	-	341,520
<u>\$ 130,491</u>	<u>\$ 456,212</u>	<u>\$ -</u>	<u>\$ 242,280</u>	<u>\$ 1,339,943</u>
\$ -	\$ -	\$ -	\$ 230	\$ 1,792
-	-	49,689	-	341,520
<u>\$ -</u>	<u>\$ -</u>	<u>\$ 49,689</u>	<u>\$ 230</u>	<u>\$ 343,312</u>
\$ 130,491	\$ -	\$ (49,689)	\$ 242,050	\$ 480,274
-	-	-	-	(13,515)
-	-	-	-	353,498
-	456,212	-	-	176,374
<u>\$ 130,491</u>	<u>\$ 456,212</u>	<u>\$ (49,689)</u>	<u>\$ 242,050</u>	<u>\$ 996,631</u>
<u>\$ 130,491</u>	<u>\$ 456,212</u>	<u>\$ -</u>	<u>\$ 242,280</u>	<u>\$ 1,339,943</u>

CITY OF HILLSBORO
Hillsboro, North Dakota

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET
TO THE STATEMENT OF NET ASSETS - MODIFIED CASH BASIS
GOVERNMENTAL FUNDS
December 31, 2010

Total *Fund Balances* for Governmental Funds \$ 996,631

Total *net assets* reported for governmental activities in the statement of net assets
is different because:

Long-term liabilities applicable to the City's governmental activities are not
due and payable in the current period and accordingly are not reported as
fund liabilities. All liabilities -both current and long-term- are reported in
the statement of net assets. Balances at December 31, 2010 are:

Special Assessment Bonds Payable	\$ (6,105,000)	
Loans Payable	<u>(371,478)</u>	
Total Long-Term Liabilities		<u>(6,476,478)</u>
Total Net Assets of Governmental Activities		<u>\$ (5,479,847)</u>

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

CITY OF HILLSBORO
Hillsboro, North Dakota

STATEMENT OF REVENUES, EXPENDITURES, AND
CHANGES IN FUND BALANCES - MODIFIED CASH BASIS
GOVERNMENTAL FUNDS
For the Year Ended December 31, 2010

	Major Funds						
	General Fund	Highway Tax Fund	City Sales Tax Fund	2008 Highway 200 Project	2007-1 Street Project	Riverbend	2008 Highway 200 Debt Retire.
Revenues:							
Property Taxes	\$ 100,328	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Sales Taxes	-	-	272,617	-	-	-	-
Special Assessments	-	-	-	-	-	97,791	97,823
Licenses, Permits and Fees	19,419	-	-	-	-	-	-
Intergovernmental	84,441	84,464	-	-	-	-	-
Charges for Services	12,334	-	-	-	-	-	-
Fines and Forfeits	740	-	-	-	-	-	-
Interest Income	4,216	-	1,420	-	92	3,058	-
Miscellaneous	31,283	567	-	-	-	-	-
Total Revenues	\$ 252,761	\$ 85,031	\$ 274,037	\$ -	\$ 92	\$ 100,849	\$ 97,823
Expenditures:							
Current:							
General Government	\$ 185,900	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Public Safety	137,751	-	-	-	-	-	-
Public Works	-	127,725	-	-	-	-	-
Culture and Recreation	61,260	-	-	-	-	-	-
Economic Development	-	-	-	-	-	-	-
Other	5,705	-	142,616	-	-	50	3
Capital Outlay	-	-	-	10,410	221,704	-	-
Dept Service:							
Principal	-	11,954	-	40,000	-	70,000	17,000
Interest	-	476	-	16,701	-	34,108	22,206
Fees	-	-	-	610	-	783	1,684
Total Expenditures	\$ 390,616	\$ 140,155	\$ 142,616	\$ 67,721	\$ 221,704	\$ 104,941	\$ 40,893
Excess (Deficiency) of Revenues Over Expenditures	\$ (137,855)	\$ (55,124)	\$ 131,421	\$ (67,721)	\$ (221,612)	\$ (4,092)	\$ 56,930
Other Financing Sources (Uses):							
Transfers In	\$ 133,590	\$ 88,010	\$ -	\$ -	\$ -	\$ -	\$ 20,000
Loan Proceeds	-	-	-	388,478	-	-	-
Transfers Out	-	(5,000)	(82,000)	-	-	-	-
Total Other Financing Sources and Uses	\$ 133,590	\$ 83,010	\$ (82,000)	\$ 388,478	\$ -	\$ -	\$ 20,000
Net Change in Fund Balances	\$ (4,265)	\$ 27,886	\$ 49,421	\$ 320,757	\$ (221,612)	\$ (4,092)	\$ 76,930
Fund Balances - January 1	\$ (9,250)	\$ 46,505	\$ 229,686	\$ (429,183)	\$ 50,200	\$ 161,514	\$ 53,561
Prior Period Adjustment	-	-	-	-	-	-	-
Fund Balance - Jan. 1, as restated	\$ (9,250)	\$ 46,505	\$ 229,686	\$ (429,183)	\$ 50,200	\$ 161,514	\$ 53,561
Fund Balance - December 31	\$ (13,515)	\$ 74,391	\$ 279,107	\$ (108,426)	\$ (171,412)	\$ 157,422	\$ 130,491

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

2007 Streets	Prairieview	Other Governmental Funds	Total Governmental Funds
\$ -	\$ 8,578	\$ 86,189	\$ 195,095
-	-	-	272,617
340,480	8,707	108,265	653,066
-	-	-	19,419
-	-	18,981	187,886
-	-	19,230	31,564
-	-	-	740
36	-	2,828	11,650
3,086	-	18,734	53,670
<u>\$ 343,602</u>	<u>\$ 17,285</u>	<u>\$ 254,227</u>	<u>\$ 1,425,707</u>
\$ -	\$ -	\$ 68,224	\$ 254,124
-	-	-	137,751
-	-	65,515	193,240
-	-	-	61,260
-	-	9,219	9,219
-	-	931	149,305
-	-	-	232,114
175,000	70,000	93,000	476,954
110,453	49,288	25,883	259,115
970	1,045	5,533	10,625
<u>\$ 286,423</u>	<u>\$ 120,333</u>	<u>\$ 268,305</u>	<u>\$ 1,783,707</u>
<u>\$ 57,179</u>	<u>\$ (103,048)</u>	<u>\$ (14,078)</u>	<u>\$ (358,000)</u>
\$ -	\$ -	\$ 58,000	\$ 299,600
-	-	-	388,478
-	-	(13,928)	(100,928)
<u>\$ -</u>	<u>\$ -</u>	<u>\$ 44,072</u>	<u>\$ 587,150</u>
<u>\$ 57,179</u>	<u>\$ (103,048)</u>	<u>\$ 29,994</u>	<u>\$ 229,150</u>
<u>\$ 399,033</u>	<u>\$ 53,359</u>	<u>\$ 100,501</u>	<u>\$ 655,926</u>
<u>-</u>	<u>-</u>	<u>111,555</u>	<u>111,555</u>
<u>\$ 399,033</u>	<u>\$ 53,359</u>	<u>\$ 212,056</u>	<u>\$ 767,481</u>
<u>\$ 456,212</u>	<u>\$ (49,689)</u>	<u>\$ 242,050</u>	<u>\$ 996,631</u>

CITY OF HILLSBORO
Hillsboro, North Dakota

RECONCILIATION OF GOVERNMENTAL FUNDS STATEMENT OF REVENUES,
EXPENDITURES AND CHANGES IN FUND BALANCES TO THE
STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS
For the Year Ended December 31, 2010

Net Change in *Fund Balances* - Total Governmental Funds \$ 229,150

The change in net assets reported for governmental activities in the statement of activities is different because:

Repayment of debt principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets. Issuance of long-term debt decreases net assets. This is the amount by which debt repayment exceeded debt proceeds.

Repayment of Capital Leases	\$ 11,954	
Repayment of Special Assessment Bonds	465,000	
Loans Issued	<u>(388,478)</u>	<u>88,476</u>

Change in Net Assets of Governmental Activities \$ 317,626

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

CITY OF HILLSBORO
Hillsboro, North Dakota

STATEMENT OF NET ASSETS - MODIFIED CASH BASIS
PROPRIETARY FUNDS
December 31, 2010

	Business-Type Activities - Enterprise Funds							
	Water Projects 425	Water Treatment Plant 430	Water Tower Construction 431	Water Dept. 601	Sewer Dept. 602	Electric Dept. 604	Other Enterprise Funds	Total Enterprise Funds
	ASSETS							
Cash and Cash Equivalents	\$ 7,612	\$ -	\$ -	\$ 72,316	\$ 34,616	\$ -	\$ 156,397	\$ 270,941
Investments	194,989	-	-	95,554	50,117	397,024	20,000	757,684
Due from Other Funds	-	-	-	157,375	2,289	290,674	-	450,338
Total Assets	\$ 202,601	\$ -	\$ -	\$ 325,245	\$ 87,022	\$ 687,698	\$ 176,397	\$ 1,478,963
LIABILITIES								
Current Liabilities:								
Benefits Payable	\$ -	\$ -	\$ -	\$ 659	\$ (718)	\$ (13)	\$ -	\$ (72)
Due to Other Funds	-	292,963	157,375	-	-	-	-	450,338
Bonds Payable	-	-	-	-	-	-	115,000	115,000
Total Current Liabilities	\$ -	\$ 292,963	\$ 157,375	\$ 659	\$ (718)	\$ (13)	\$ 115,000	\$ 565,266
Noncurrent Liabilities:								
Bonds Payable	\$ -	\$ -	\$ 979,129	\$ -	\$ -	\$ -	\$ 540,000	\$ 1,519,129
Total Noncurrent Liabilities	\$ -	\$ -	\$ 979,129	\$ -	\$ -	\$ -	\$ 540,000	\$ 1,519,129
Total Liabilities	\$ -	\$ 292,963	\$ 1,136,504	\$ 659	\$ (718)	\$ (13)	\$ 655,000	\$ 2,084,395
NET ASSETS								
Unrestricted	\$ 202,601	(292,963)	(1,136,504)	324,586	87,740	687,711	(478,603)	(605,432)
Total Net Assets	\$ 202,601	\$ (292,963)	\$ (1,136,504)	\$ 324,586	\$ 87,740	\$ 687,711	\$ (478,603)	\$ (605,432)

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

CITY OF HILLSBORO
Hillsboro, North Dakota

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS - MODIFIED CASH BASIS
PROPRIETARY FUNDS
For the Year Ended December 31, 2010

	Business-Type Activities - Enterprise Funds							
	Water Projects 425	Water Treatment Plant 430	Water Tower Construction 431	Water Dept. 601	Sewer Dept. 602	Electric Dept. 604	Other Enterprise Funds	Total Enterprise Funds
<u>Operating Revenues:</u>								
<u>Charges for Sales and Services:</u>								
Water Operations	\$ -	\$ -	\$ -	\$ 286,249	\$ -	\$ -	\$ -	\$ 286,249
Sanitary Sewer Operations	-	-	-	-	104,393	-	165,714	270,107
Electric Operations	-	-	-	-	-	1,686,916	-	1,686,916
MRES Billings	-	-	-	-	-	1,904	119,800	121,704
Other Operating Receipts	26	-	-	440	-	3,300	8,947	12,713
Total Operating Revenues	\$ 26	\$ -	\$ -	\$ 286,689	\$ 104,393	\$ 1,692,120	\$ 294,461	\$ 2,377,689
<u>Operating Expenses:</u>								
Salaries and Wages	\$ -	\$ -	\$ -	\$ 71,567	\$ 16,270	\$ 69,190	\$ -	\$ 157,027
Contracted Services	-	5,747	750	12,088	12,106	-	158,176	188,867
Operated Costs	-	-	-	-	-	36,288	-	36,288
Maintenance & Supplies	-	-	1,053	56,252	32,895	38,792	2,799	131,791
Purchased Power Costs	-	-	-	-	-	1,373,731	-	1,373,731
Miscellaneous	-	2,128	15	-	211	2,078	5,618	10,050
Total Operating Disbursements	\$ -	\$ 7,875	\$ 1,818	\$ 139,907	\$ 61,482	\$ 1,520,079	\$ 166,593	\$ 1,897,754
Operating Income (Loss)	\$ 26	\$ (7,875)	\$ (1,818)	\$ 146,782	\$ 42,911	\$ 172,041	\$ 127,868	\$ 479,935
<u>Nonoperating Revenues (Expenses):</u>								
Interest on Investments	\$ 2,201	\$ -	\$ -	\$ 1,304	\$ 962	\$ 3,636	\$ 1,181	\$ 9,284
Miscellaneous	-	-	-	1,017	3,590	8,384	-	12,991
Construction/Capital Outlay	(47,475)	(242,057)	(1,066,161)	(20,224)	(11,825)	(11,825)	-	(1,399,567)
Retirement of Debt - Interest & Fees	-	-	-	-	-	-	(29,626)	(29,626)
Total Nonoperating Revenues (Expenses)	\$ (45,274)	\$ (242,057)	\$ (1,066,161)	\$ (17,903)	\$ (7,273)	\$ 195	\$ (28,445)	\$ (1,406,918)
Income Before Transfers	\$ (45,248)	\$ (249,932)	\$ (1,067,979)	\$ 128,879	\$ 35,638	\$ 172,236	\$ 99,423	\$ (926,983)
Transfers In	\$ -	\$ -	\$ -	\$ 810	\$ 115	\$ 403	\$ -	\$ 1,328
Transfers Out	-	-	-	(5,000)	(5,000)	(190,000)	-	(200,000)
Total Transfers	\$ -	\$ -	\$ -	\$ (4,190)	\$ (4,885)	\$ (189,597)	\$ -	\$ (198,672)
Change in Net Assets	\$ (45,248)	\$ (249,932)	\$ (1,067,979)	\$ 124,689	\$ 30,753	\$ (17,361)	\$ 99,423	\$ (1,125,655)
Total Net Assets - January 1	\$ 247,849	\$ (43,031)	\$ (68,525)	\$ 199,897	\$ 56,987	\$ 705,072	\$ (578,026)	\$ 520,223
Total Net Assets - December 31	\$ 202,601	\$ (292,963)	\$ (1,136,504)	\$ 324,586	\$ 87,740	\$ 687,711	\$ (478,603)	\$ (605,432)

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

CITY OF HILLSBORO
Hillsboro, North Dakota

STATEMENT OF CASH FLOWS - MODIFIED CASH BASIS
PROPRIETARY FUNDS
For the Year Ended December 31, 2010

	Business-Type Activities - Enterprise Funds							Total Enterprise Funds
	Water Projects 425	Water Treatment Plant 430	Water Tower Construct. 431	Water Dept. 601	Sewer Dept. 602	Electric Dept. 604	Other Enterprise Funds	
Cash Flows from Operating Activities:								
Receipts from Customers and Users	\$ 26	\$ -	\$ -	\$ 286,689	\$ 104,393	\$ 1,692,120	\$ 294,461	\$ 2,377,689
Payments to Suppliers	-	(7,875)	(1,818)	(68,340)	(45,212)	(1,450,889)	(166,593)	(1,740,727)
Payments to Employees	-	-	-	(71,567)	(16,270)	(69,190)	-	(157,027)
Net Cash Provided (Used) by Operating Activities	\$ 26	\$ (7,875)	\$ (1,818)	\$ 146,782	\$ 42,911	\$ 172,041	\$ 127,868	\$ 479,935
Cash Flows from Noncapital Financing Activities:								
Miscellaneous Revenue (Expense)	\$ -	\$ -	\$ -	\$ 1,017	\$ 3,590	\$ 8,384	\$ -	\$ 12,991
Cash Overdraft Position Assumed to be Financed	-	249,932	88,850	(157,375)	(22,012)	(270,951)	-	(111,556)
Transfers from Other Funds	-	-	-	810	115	403	-	1,328
Transfers to Other Funds	-	-	-	(5,000)	(5,000)	(190,000)	-	(200,000)
Net Cash Provided (Used) by Noncapital Financing Activities	\$ -	\$ 249,932	\$ 88,850	\$ (160,548)	\$ (23,307)	\$ (452,164)	\$ -	\$ (297,237)
Cash Flows from Capital and Related Financing Activities:								
Purchases and Construction of Capital Assets	\$ (47,475)	\$ (242,057)	\$ (1,066,161)	\$ (20,224)	\$ (11,825)	\$ (11,825)	\$ -	\$ (1,399,567)
Issuance of Capital Debt	-	-	979,129	-	-	-	-	979,129
Principal Paid on Capital Debt	-	-	-	-	-	-	(110,000)	(110,000)
Interest Paid on Capital Debt	-	-	-	-	-	-	(29,626)	(29,626)
Net Cash Provided (Used) by Capital and Related Financing Activities	\$ (47,475)	\$ (242,057)	\$ (87,032)	\$ (20,224)	\$ (11,825)	\$ (11,825)	\$ (139,626)	\$ (560,064)
Cash Flows from Investing Activities:								
Purchases, Sales & Maturities of Investments	\$ (1,580)	\$ -	\$ -	\$ (580)	\$ 25,875	\$ (26,700)	\$ (20,000)	\$ (22,985)
Interest Income	2,201	-	-	1,304	962	3,636	1,181	9,284
Net Cash Provided (Used) by Investing Activities	\$ 621	\$ -	\$ -	\$ 724	\$ 26,837	\$ (23,064)	\$ (18,819)	\$ (13,701)
Net Increase (Decrease) in Cash and Cash Equivalents	\$ (46,828)	\$ -	\$ -	\$ (33,266)	\$ 34,616	\$ (315,012)	\$ (30,577)	\$ (391,067)
Cash and Cash Equivalents, January 1	\$ 54,440	\$ -	\$ -	\$ 105,582	\$ -	\$ 315,012	\$ 186,974	\$ 662,008
Cash and Cash Equivalents, December 31	\$ 7,612	\$ -	\$ -	\$ 72,316	\$ 34,616	\$ -	\$ 156,397	\$ 270,941
Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities								
Operating Income (Loss)	\$ 26	\$ (7,875)	\$ (1,818)	\$ 146,782	\$ 42,911	\$ 172,041	\$ 127,868	\$ 479,935
Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities:								
Change in Assets and Liabilities:								
Negative Cash	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Benefits Payable	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Net Cash Provided (Used) by Operating Activities	\$ 26	\$ (7,875)	\$ (1,818)	\$ 146,782	\$ 42,911	\$ 172,041	\$ 127,868	\$ 479,935

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

CITY OF HILLSBORO
Hillsboro, North Dakota

NOTES TO THE FINANCIAL STATEMENTS
December 31, 2010

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policy of the City of Hillsboro, North Dakota, is to maintain the accounting records on a modified cash basis, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The more significant of the government's accounting policies are described below.

A. Financial Reporting Entity

The accompanying financial statements present the activities of the City of Hillsboro. The city has considered all potential component units for which the city is financially accountable and other organizations for which the nature and significance of their relationships with the city are such that exclusion would cause the city's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. This criteria includes appointing a voting majority of an organization's governing body and (1) the ability of the City of Hillsboro to impose its will on that organization or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on the City of Hillsboro.

Based on these criteria, there are no component units to be included within the City of Hillsboro as a reporting entity.

B. Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all of the nonfiduciary activities of the primary government and the component unit of the City of Hillsboro. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for services.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

Fund Financial Statements: The fund financial statements provide information about the city's funds including its blended component units. Separate statements for each fund category—*governmental* and *proprietary*—are presented. The emphasis of fund financial statements is on major governmental and enterprise funds, each displayed in a separate column. All remaining governmental and enterprise funds are aggregated and reported as nonmajor funds.

Proprietary fund operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as subsidies and investment earnings, result from nonexchange transactions or ancillary activities.

The city reports the following major governmental funds:

General Fund. This is the city's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

Highway Tax/Streets Fund. This fund is used to account for taxes received for streets and highways and for repair and maintenance projects on them.

City Sales Tax Fund. This fund accounts for sales tax money for the city.

2008 Highway 200 Project Fund. This fund is used to account for construction costs related to the construction of this project.

2007-1 Street Project Fund. This fund is used to account for construction costs related to the construction of this project.

Riverbend Debt Service Fund. This fund is used to account for debt service payments related to debt issued for construction costs on the project.

2007 Street Project Fund. This fund is used to account for construction costs related to the construction of this project.

2008 Highway 200 Debt Service Fund. This fund is used to pay debt principal and interest for construction costs related to the Highway 200 project

Prairieview Debt Service Fund. This fund is used to pay debt principal and interest for construction costs related to the Prairieview project

The City reports the following major enterprise funds:

Water Projects Fund. This fund is used to account for construction costs of various water projects.

Water Treatment Plant Fund. This fund is used to account for construction costs of a regional water treatment plant.

Water Tower Construction Fund. This fund is used to account for construction costs of a new water tower.

Water Department Fund. This fund is used to account for customer receipts and payments for water fees.

Sewer Department Fund. This fund is used to account for customer receipts and payments for sewer fees.

Electric Department Fund. This fund is used to account for customer receipts and payments for electric fees.

C. Measurement Focus and Basis of Accounting

Measurement focus is a term used to describe "how" transactions are recorded within the various financial statements. Basis of accounting refers to "when" transactions are recorded regardless of the measurement focus applied.

MEASUREMENT FOCUS

In the government-wide Statement of Net Assets and the Statement of Activities, both governmental and business-like activities are presented using the economic resources measurement focus, within the limitations of the modified cash basis of accounting, as defined in item b below.

In the fund financial statements, the “current financial resources” measurement focus or the “economic resources” measurement focus, as applied to the modified cash basis of accounting, is used as appropriate:

- a) All governmental funds utilize a “current financial resources” measurement focus. Only current financial assets and liabilities are generally included on their balance sheets. Their operating statements present sources and uses of available spendable financial resources during a given period. These funds use fund balance as their measure of available spendable financial resources at the end of the period.
- b) The proprietary fund utilizes an “economic resources” measurement focus. The accounting objectives of this measurement focus are the determination of operating income, changes in net assets (or cost recovery), financial position, and cash flows. All assets and liabilities (whether current or noncurrent, financial, or nonfinancial) associated with their activities are reported. Proprietary fund equity is classified as net assets.

Basis of Accounting

In the government-wide Statement of Net Assets and Statement of Activities and the fund financial statements, governmental, and business-type activities are presented using a modified cash basis of accounting. This basis recognizes assets, liabilities, net assets/fund equity, revenues, and expenditures/expenses when they result from cash transactions in the government-wide statements, proprietary fund statements, and the similar discretely presented component unit statements. This basis is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

As a result of the use of this modified cash basis of accounting, certain assets and their related revenues (such as accounts receivable and revenue for billed or provided services not yet collected) and certain liabilities and their related expenses (such as accounts payable and expenses for goods or services received but not yet paid, and accrued expenses and liabilities) are not recorded in these financial statements.

If the City utilized the basis of accounting recognized as generally accepted, the fund financial statements for governmental funds would use the modified accrual basis of accounting, while the fund financial statements for proprietary fund types would use the accrual basis of accounting. All government-wide financials would be presented on the accrual basis of accounting.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the Governmental Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The city has elected not to follow subsequent private-sector guidance.

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

D. Cash, Cash Equivalents and Investments

Cash includes amounts in demand deposits and money market accounts. Cash equivalents on the statement of cash flows consist of highly liquid investments with an original maturity of three months or less (money markets). Deposits must either be deposited with the Bank of North Dakota or in other financial institution situated and doing business within the state. Deposits, other than with the Bank of North Dakota, must be fully insured or secured with pledges of securities equal to 110% of the uninsured balance.

CITY OF HILLSBORO

Notes to the Financial Statements - Continued

The investments of the City at December 31, 2010 consist of certificates of deposit stated at cost.

NOTE 2: LEGAL COMPLIANCE - BUDGETS**BUDGET AMENDMENTS**

The city's governing board approved the following amendments to the city budget in 2010:

Governmental Funds:	REVENUES/TRANSFERS/FINANCING SOURCES			Fund
	Original Budget	Amendment	Amended Budget	
General Fund	\$252,705	\$ 9,646	\$262,351	100
Streets	73,500	14,542	88,042	201
City Share of Specials	18,500	1,279	19,779	203
Emergency	150	23,536	23,686	206
Cemetery	8,250	1,016	9,266	208
Armory	11,550	181	11,731	209
MSCC	950	95	1,045	211
Sales Tax	252,000	22,037	274,037	212
Forestry	1,600	126	1,726	217
2006-1 2007 Street Project	-	92	92	428
Capital Projects	-	20,000	20,000	450
Project 96-2 & 96-3	13,000	339	13,339	510
2006 Water Main	107,048	3,188	110,236	526
2007 Streets	341,422	2,180	343,602	528
2008 Highway 200 Project	-	117,823	117,823	527
Mosquito Control	16,000	230	16,230	607

Governmental Funds:	EXPENDITURES AND TRANSFERS OUT			Fund
	Original Budget	Amendment	Amended Budget	
General	\$388,528	\$ 2,089	\$390,617	100
Social Security	30,000	15,904	45,904	202
City Share of Specials	22,895	335	23,230	203
Emergency	5,000	18,837	23,837	206
2007-1 Street Project	-	221,704	221,704	428
Cemetery	14,050	490	14,540	208
Armory	12,600	8,180	21,780	209
Riverbend Debt Service	104,890	50	104,950	525
Mosquito Control	6,300	1,429	7,729	607
Recreation District	8,200	437	8,637	806
2008 Highway 200	-	40,893	40,893	527

NOTE 3: DEPOSITS AND INVESTMENTS

In accordance with North Dakota Statutes, the City of Hillsboro maintains deposits and investments at the depository banks designated by the governing board. All depositories are members of the Federal Reserve System.

Deposits must either be deposited with the Bank of North Dakota or in other financial institution situated and doing business within the state. Deposits, other than with the Bank of North Dakota, must be fully insured or bonded. In lieu of a bond, a financial institution may provide a pledge of securities equal to 110% of the deposits not covered by insurance or bonds.

CITY OF HILLSBORO

Notes to the Financial Statements - Continued

Authorized collateral includes bills, notes, or bonds issued by the United States government, its agencies or instrumentalities, all bonds and notes guaranteed by the United States government, Federal land bank bonds, bonds, notes, warrants, certificates of indebtedness, insured certificates of deposit, shares of investment companies registered under the Investment Companies Act of 1940, and all other forms of securities issued by the State of North Dakota, its boards, agencies or instrumentalities or by any county, city, township, school district, park district, or other political subdivision of the state of North Dakota. Whether payable from special revenues or supported by the full faith and credit of the issuing body and bonds issued by a other state of the United States or such other securities approved by the banking board.

At year ended December 31, 2010, the city's carrying amount of deposits was \$2,026,869 and the bank balances totaled \$2,087,937. Of the bank balances, \$1,512,119 was covered by Federal Depository Insurance. The remaining balances totaling \$575,818 were collateralized with securities held by the pledging financial institution's agent in the government's name totaling \$635,546.

Credit Risk:

The City may invest idle funds as authorized in North Dakota Statutes, as follows:

- (a) Bonds, treasury bills and notes, or other securities that are a direct obligation insured or guaranteed by, the treasury of the United States, or its agencies, instrumentalities, or organizations created by an act of congress.
- (b) Securities sold under agreements to repurchase written by a financial institution in which the underlying securities for the agreement to repurchase are the type listed above.
- (c) Certificates of Deposit fully insured by the federal deposit insurance corporation.
- (d) Obligations of the state.

Investments:

As of December 31, 2010, the City held certificates of deposit with maturities in excess of 3 months in the amount of \$300,000, which are all considered investments.

Interest Rate Risk:

The city doesn't have a formal deposit policy that limits maturities as a means of managing exposure to fair-value losses arising from increasing interest rates.

Concentration of Credit Risk:

The city does not have a limit on the amount they may invest in any one issuer.

NOTE 4: PROPERTY TAXES

The county treasurer acts as an agent to collect property taxes levied in the county for all taxing authorities. Any material tax collections are distributed after the end of each month.

Property taxes are levied as of January 1. The property taxes attach as an enforceable lien on property on January 1 and may be paid in two installments. The first installment includes one-half of the real estate taxes and all the special assessments and the second installment is the balance of the real estate taxes. The first installment is due by March 1 and the second installment is due by October 15. A 5% discount on property taxes is allowed if all taxes and special assessments are paid by February 15. After the due dates, the bill becomes delinquent and penalties are assessed.

CITY OF HILLSBORO

Notes to the Financial Statements - Continued

Most property owners choose to pay property taxes and special assessments in a single payment on or before February 15 and receive the discount on the property taxes.

NOTE 5: DUE TO / FROM OTHER FUNDS

The composition of due to and due from other funds as of December 31, 2010 are as follows:

Due From Fund	Due To Fund	Amount
Highway Tax	General Fund	\$ 11,993
Sales Tax/Highway Tax	2008 Highway 200	108,426
Sales Tax	2007-1 Street Project	171,412
Sales Tax	Prairieview Debt Service	49,689
Water Department	Water Tower Construction	157,375
Electric Department	Water Treatment Plant	2,289
Sewer Department	Water Treatment Plant	290,674
	Total	\$791,858

The composition of due to and due from other funds is related to negative cash fund balances in various major funds for governmental and business type activities.

NOTE 6: TRANSFERS

The following is a reconciliation between transfers in and transfers out as reported in the basic financial statements for the year ended December 31, 2010:

Fund	Transfers In	Transfers Out
General Fund	\$133,590	\$ -
Highway Tax/Streets	88,010	5,000
Sales Tax	-	82,000
Sewer (Enterprise)	115	5,000
Water (Enterprise)	810	5,000
Electric (Enterprise)	402	190,000
Capital Projects	20,000	-
Emergency	-	13,928
MSCCC	12,000	-
Cemetery	6,000	-
Armory Operations	20,000	-
2008 Highway 200 Project	20,000	-
Total Transfers	\$300,928	\$300,928

NOTE 7: LONG-TERM LIABILITIES

During the year ended December 31, 2010 the following changes occurred in long-term liabilities of the city:

Governmental Activities:

Governmental Activities:	Balance 1-1-10	Increases	Decreases	Balance 12-31-10	Due Within One Year
Special Assessment Bonds	\$6,553,000	\$ -	\$448,000	\$6,105,000	\$435,000
Revolving Loan Payable	-	338,478	17,000	371,478	-
Leases Payable	11,954	-	11,954	-	-
Total Governmental Activities	\$6,564,954	\$338,478	\$476,954	\$6,476,478	\$435,000

CITY OF HILLSBORO

Notes to the Financial Statements - Continued

Business-Type Activities (Proprietary Funds):

Business-Type Activities:	Balance 1-1-10	Increases	Decreases	Balance 12-31-10	Due Within One Year
Revenue Bonds Payable	\$765,000	\$ -	\$110,000	\$ 655,000	\$115,000
Revolving Loan Payable	-	979,129	-	979,129	-
Revenue Bonds Payable	\$765,000	\$979,129	\$110,000	\$1,634,129	\$115,000

SPECIAL ASSESSMENT BONDS

\$740,000 2003 Refunding Improvement Bonds due in annual installments of \$5,000 to \$25,000 through May 2011; interest at 4.65%.	\$ 5,000
\$945,000 Improvement Bonds of 2007 due in annual installments of \$40,000 to \$95,000 through May 2019; interest at 4.0% to 4.8%.	735,000
\$2,865,000 Special Assessment Bonds of 2008 due in annual installments of \$165,000 to \$230,000 through May 2022; interest at 3.95% to 4.5%.	2,525,000
\$1,230,000 Special Assessment Bonds of 2008-B due in annual installments of \$70,000 to \$120,000 through May 2022; interest at 3.85% to 4.4%.	1,160,000
\$785,000 Special Assessment Bonds of 2010 due in annual installments of \$40,000 to \$65,000 through May 2024; interest at 3.5% to 4.75%.	745,000
\$1,150,563 Drinking Water Revolving Improvement Bonds of 2007 due in annual installments of \$70,563 to \$95,000 through September 2021; interest at 2.5%.	<u>935,000</u>
Total Special Assessment Bonds	<u>\$6,105,000</u>
\$388,478 Drawdown for the Highway 200 project, issued in 2010. No set payment schedule, interest at .5 to 2.5%. Note: the IRS is subsidizing part of each interest payment.	<u>371,478</u>
Total Governmental Activities	<u>\$6,476,478</u>

Special assessment bond debt service requirements to maturity are as follows:

GOVERNMENTAL ACTIVITIES		
Year Ending December 31	Bonds Payable	
	Principal	Interest
2011	\$ 435,000	\$ 236,452
2012	457,000	220,118
2013	469,000	202,835
2014	486,000	184,646
2015	508,000	165,496
2016 – 2020	2,705,000	503,528
2021 – 2025	1,045,000	57,916
Totals	\$6,105,000	\$1,570,991

CITY OF HILLSBORO

Notes to the Financial Statements - Continued

REVENUE BONDS

The city issues bonds where the city pledges income derived from the operations to pay debt service. The proceeds of the bonds are used to finance various capital improvement projects.

Business-Type Activities:

\$1,400,000 Refunding Electric Revenue bonds of 2003 due in annual installments of \$110,000 to \$135,000 to 2016 with interest of 3.5% to 4.5%.	\$ 655,000
\$979,129 Drawdown for the Water Treatment Plant, issued in 2010. No set payment schedule, interest at .5 to 2.5%.	<u>979,129</u>
Total Business-Type Activities	<u>\$1,634,129</u>

Revenue bond debt service requirements to maturity are as follows:

BUSINESS-TYPE ACTIVITIES		
Year Ending December 31	Bonds Payable	
	Principal	Interest
2011	\$115,000	\$13,502
2012	120,000	22,693
2013	120,000	17,893
2014	130,000	12,972
2015	135,000	7,448
2016 - 2019	35,000	1,575
Totals	\$655,000	\$76,083

NOTE 8: PENSION PLAN

The City of Hillsboro provides a retirement plan for City employees. The profit-sharing plan is a 401K defined contribution plan in which the City contributes up to 8% of gross salaries for each eligible employee. An employee's contribution can be any amount less than or equal to the amount allowed by the Federal Government. Contributions are determined on base salary and exclude any overtime or bonuses earned by employees. The plan uses the hour of service method. To initially be eligible for the plan, the employee must complete one year of service and at least 21 years old. Additionally, the employee must be credited with 1,000 hours of service in the twelve-month period beginning with the first day of work and ending on the anniversary date of the first day of work. An employee must have 1,000 hours of service in any plan year to remain eligible. Up to 501 hours of leave in any plan year may be counted toward hours of service. A break in service is considered when the employee is not credited with or paid for at least 500 hours of service. Once eligibility requirements are met for plan participation, an employee begins actual participation in the plan on the first day of the month coinciding with or next following the date the requirements were met. The employee is subject to a vesting schedule based on years of service. A deduction is made monthly and forwarded to the plan account, which is maintained by Northern Capital Trust. Upon termination of employment, the employee will receive his or her vested portion of the contribution. The city's share of pension costs for the years ended December 31, 2010, 2009 and 2008 were \$23,972, \$23,207, and \$21,416, respectively.

NOTE 9: CONDUIT DEBT

COMMUNITY DEVELOPMENT BLOCK GRANTS

From time to time, the city has obtained Community Development Block Grants (CBDG) to provide financial assistance to private-sector entities for the acquisition and construction of

CITY OF HILLSBORO

Notes to the Financial Statements - Continued

industrial and commercial facilities deemed to be in the public interest. The grants are secured by property financed and are payable solely from the payments received on the underlying mortgage grants. Upon repayment of the grants, ownership of the acquired facilities transfers to the private-sector entity served by the grant. Neither the City, the State, nor any political subdivision thereof is obligated in any manner for repayment of the grants. Accordingly, the grants are not reported as liabilities in the accompanying financial statements.

As of December 31, 2010, there were three Community Development Block Grants outstanding, with an aggregate principal amount payable of \$431,196. As of December 31, 2008, there were three Community Development Block Grants outstanding, with an aggregate principal amount payable of \$433,196.

NOTE 10: RISK MANAGEMENT

The City of Hillsboro is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters.

In 1986, state agencies and political subdivisions of the State of North Dakota joined together to form the North Dakota Insurance Reserve Fund (NDRIF), a public entity risk pool currently operating as a common risk management and insurance program for the state and over 2,000 political subdivisions. The City pays an annual premium to NDRIF for its general liability, auto, and public assets insurance coverage. The coverage by NDRIF is limited to losses of two million dollars per occurrence for general liability and automobile coverage and \$1,470,438 for public assets coverage.

The City of Hillsboro also participates in the North Dakota Fire and Tornado Fund and the State Bonding Fund. The city pays an annual premium to the Fire and Tornado Fund to cover property damage to buildings and personal property. Replacement cost coverage is provided by estimating replacement cost in consultation with the Fire and Tornado Fund. The Fire and Tornado Fund is reinsured by a third party insurance carrier for losses in excess of two million dollars per occurrence during a 12 month period. The State Bonding Fund currently provides political subdivisions with blanket fidelity bond coverage in the amount of \$1,600,000 for the city employees. The State Bonding Fund does not currently charge any premium for this coverage.

The City has workers compensation with the North Dakota Workforce Safety and Insurance. The city provides health insurance coverage to all full time employees.

Settled claims resulting from these risks have not exceeded insurance coverage in any of the past three fiscal years.

NOTE 11: FUND DEFICITS

The following funds were in a deficit position at December 31, 2010:

Fund Name	Balance
General Fund	\$ (13,515)
2008 Highway 200 Project	(108,426)
Social Security	(2,991)
Cemetery	(213)
Armory Operations Fund	(2,332)
2007-1 Street Project	(171,412)
Project 96-2 & 96-3	(6,425)
Prairieview Development	(49,689)
Recreation District	(668)
Regional Water Treatment Plant	(292,963)
Water Tower Construction	(157,375)

CITY OF HILLSBORO

Notes to the Financial Statements - Continued

NOTE 12: PRIOR PERIOD ADJUSTMENTS

A prior period adjustment was done to reclassify two construction funds from governmental capital projects funds to enterprise funds for water tower construction (fund 431) and regional water project (fund 430). The adjustments are listed below to governmental funds and activities and enterprise funds and activities:

Governmental Activities:	Amounts
Net Assets Equity Balance - January 1, 2010	\$(5,909,028)
Adjustments to restate the January 1, 2010 beginning net assets equity due to:	
Reclassify funds 430 and 431 from govt. to enterprise	111,555
Net Assets Equity (as restated) - January 1, 2010	<u>\$(5,797,473)</u>

Enterprise Activities:	Amounts
Net Assets Equity Balance - January 1, 2010	\$631,777
Adjustments to restate the January 1, 2010 beginning net assets equity due to:	
Reclassify funds 430 and 431 from govt. to enterprise	(111,555)
Net Assets Equity (as restated) - January 1, 2010	<u>\$520,222</u>

Governmental Funds:	Amounts
Fund Balances - January 1, 2010	\$655,926
Adjustments to restate the January 1, 2010 beginning Fund balances due to:	
Reclassify funds 430 and 431 from govt. to enterprise	111,555
Fund Balances (as restated) - January 1, 2010	<u>\$767,481</u>

Enterprise Funds:	Amounts
Net Assets Equity Balance - January 1, 2010	\$631,779
Adjustments to restate the January 1, 2010 beginning net assets equity due to :	
Reclassify funds 430 and 431 from govt. to enterprise	(111,555)
Net Assets (as restated) - January 1, 2010	<u>\$520,224</u>

NOTE 13: CONTINGENT LIABILITY

The City is a defendant in one lawsuit incident to its operations. The City is vigorously contesting the lawsuit. The maximum possible loss to the City is approximately \$197,000. Trial is scheduled for federal district court on March 13, 2012.

NOTE 14: CONSTRUCTION COMMITMENTS

The City of Hillsboro had the following open construction contracts on various projects with balances owing at December 31, 2010:

Project	Original Contract	Change Orders	Total Contract	Total Completed	Remaining Balance	Retainage
Water Tower Project	\$865,900	(\$9,622)	\$856,278	\$828,470	\$27,808	\$ -

NOTE 15: SUBSEQUENT EVENTS

In February of 2012, the City of Hillsboro approved the Resolution providing for the issuance of \$605,000 Refunding Improvement Bonds of 2012. The purpose of these bonds is to refinance the Improvement Bonds of 2004. The City will save approximately \$63,700 on the refinancing.

CITY OF HILLSBORO
Hillsboro, North Dakota

BUDGETARY COMPARISON SCHEDULE - MODIFIED CASH BASIS
GENERAL FUND
For the Year Ended December 31, 2010

	Original Budget	Final Budget	Actual	Variance with Final Budget
<u>Revenues:</u>				
Taxes	\$ 103,750	\$ 103,750	\$ 100,328	\$ (3,422)
Licenses, Permits and Fees	20,005	20,005	19,419	(586)
Charges for Services	11,000	11,000	12,334	1,334
Intergovernmental	90,000	90,000	84,441	(5,559)
Fines, Forfeitures and Penalties	250	250	740	490
Interest	3,000	3,000	4,216	1,216
Miscellaneous	24,700	34,346	31,283	(3,063)
Total Revenues	\$ 252,705	\$ 262,351	\$ 252,761	\$ (9,590)
<u>Expenditures:</u>				
Current:				
General Government	\$ 183,028	\$ 183,028	\$ 185,900	\$ (2,872)
Public Safety	138,500	138,500	137,751	749
Culture and Recreation	62,000	62,000	61,260	740
Other	5,000	7,089	5,705	1,384
Total Expenditures	\$ 388,528	\$ 390,617	\$ 390,616	\$ 1
Excess (Deficiency) of Revenues Over Expenditures	\$ (135,823)	\$ (128,266)	\$ (137,855)	\$ (9,589)
<u>Other Financing Sources (Uses):</u>				
Transfers In	\$ 124,000	\$ 124,000	\$ 133,590	\$ 9,590
Net Change in Fund Balances	\$ (11,823)	\$ (4,266)	\$ (4,265)	\$ 1
Fund Balances - January 1	\$ (9,250)	\$ (9,250)	\$ (9,250)	-
Fund Balances - December 31	\$ (21,073)	\$ (13,516)	\$ (13,515)	\$ 1

The accompanying required supplementary information notes are an integral part of this schedule.

CITY OF HILLSBORO
Hillsboro, North Dakota

BUDGETARY COMPARISON SCHEDULE - MODIFIED CASH BASIS
HIGHWAY TAX/STREETS FUND
For the Year Ended December 31, 2010

	Original Budget	Final Budget	Actual	Variance with Final Budget
<u>Revenues:</u>				
Intergovernmental	\$ 73,000	\$ 87,542	\$ 84,464	\$ (3,078)
Miscellaneous Revenue	500	500	567	67
Total Revenues	\$ 73,500	\$ 88,042	\$ 85,031	\$ (3,011)
<u>Expenditures:</u>				
Current:				
Public Works	\$ 165,575	\$ 165,575	\$ 127,725	\$ 37,850
Debt Service:				
Principal	-	-	11,954	(11,954)
Interest	-	-	476	(476)
Total Expenditures	\$ 165,575	\$ 165,575	\$ 140,155	\$ 25,420
Excess (Deficiency) of Revenues Over Expenditures	\$ (92,075)	\$ (77,533)	\$ (55,124)	\$ 22,409
<u>Other Financing Sources (Uses):</u>				
Transfers in	\$ 85,000	\$ 85,000	\$ 88,010	\$ 3,010
Transfers Out	(5,000)	(5,000)	(5,000)	-
Total Other Financing Sources (Uses)	\$ 80,000	\$ 80,000	\$ 83,010	\$ 3,010
Net Change in Fund Balances	\$ (12,075)	\$ 2,467	\$ 27,886	\$ 25,419
Fund Balances - January 1	\$ 46,505	\$ 46,505	\$ 46,505	\$ -
Fund Balances - December 31	\$ 34,430	\$ 48,972	\$ 74,391	\$ 25,419

The accompanying required supplementary information notes are an integral part of this schedule.

CITY OF HILLSBORO
Hillsboro, North Dakota

BUDGETARY COMPARISON SCHEDULE - MODIFIED CASH BASIS
SALES TAX FUND
For the Year Ended December 31, 2010

	Original Budget	Final Budget	Actual	Variance with Final Budget
<u>Revenues:</u>				
Taxes	\$ 250,000	\$ 272,037	\$ 272,617	\$ 580
Interest income	2,000	2,000	1,420	(580)
Total Revenues	<u>\$ 252,000</u>	<u>\$ 274,037</u>	<u>\$ 274,037</u>	<u>\$ -</u>
<u>Expenditures:</u>				
Current:				
Economic Development	<u>\$ 137,000</u>	<u>\$ 137,000</u>	<u>\$ 142,616</u>	<u>\$ (5,616)</u>
Excess (Deficiency) of Revenues Over Expenditures	<u>\$ 115,000</u>	<u>\$ 137,037</u>	<u>\$ 131,421</u>	<u>\$ (5,616)</u>
<u>Other Financing Sources (Uses):</u>				
Transfers out	<u>\$ (99,445)</u>	<u>\$ (99,445)</u>	<u>\$ (82,000)</u>	<u>\$ 17,445</u>
Net Change in Fund Balances	<u>\$ 15,555</u>	<u>\$ 37,592</u>	<u>\$ 49,421</u>	<u>\$ 11,829</u>
Fund Balances - January 1	<u>\$ 229,686</u>	<u>\$ 229,686</u>	<u>\$ 229,686</u>	<u>\$ -</u>
Fund Balances - December 31	<u>\$ 245,241</u>	<u>\$ 267,278</u>	<u>\$ 279,107</u>	<u>\$ 11,829</u>

The accompanying required supplementary information notes are an integral part of this schedule.

CITY OF HILLSBORO
Hillsboro, North Dakota

NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION
December 31, 2010

NOTE 1: STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Budgetary Information:

- The city commission adopts an “appropriated budget” on the modified cash basis of accounting.
- Annually on or before September tenth the city prepares a preliminary budget. NDCC 40-40-04
- The preliminary budget includes the estimated revenues and appropriations for the general fund, each special revenue fund and each debt service fund of the city. NDCC 40-40-05
- The city commission shall meet and hear any and all protests or objections to the items or amounts set forth in the preliminary budget. At the hearing, the city commission shall make any changes in the items or amounts shown in the preliminary budget. The final budget is prepared which includes a summary of the amounts levied for each fund and the total amount levied. NDCC 40-40-08
- The city commission, on or before October 7th, the final budget is completed. NDCC 40-40-09
- Each budget is controlled by the city auditor at the revenue and expenditure function/object level.
- The current budget, except for property taxes, may be amended during the year for any revenues and appropriations not anticipated at the time the budget was prepared. NDCC 57-15-31.1
- All appropriations lapse at year-end.

NOTE 2: EXPENDITURES IN EXCESS OF BUDGET

During fiscal year 2010, City of Hillsboro had the following fund expenditures in excess of budgeted amounts:

	Budget	Actual	Excess
Special Revenue Fund:			
City Sales Tax	\$137,000	\$142,616	\$(5,616)

No remedial action is anticipated or required regarding this excess expenditure.

CITY OF HILLSBORO
Hillsboro, North Dakota
SCHEDULE OF FUND ACTIVITY
ARISING FROM CASH TRANSACTIONS-Cash Amounts by Fund
For the Year Ended December 31, 2010

	Balance 1-1-10	Receipts	Transfers In	Debt Proceeds	Transfers Out	Disbursements	Balance 12-31-10
Major Governmental Funds:							
General Fund	\$ (9,250.09)	\$ 252,761.08	\$ 133,590.29	\$ -	\$ -	\$ 390,616.65	\$ (13,515.37)
Highway Tax/Streets	46,504.05	85,031.58	88,010.34	-	5,000.00	140,155.16	74,390.81
City Sales Tax Fund	229,685.63	274,037.07	-	-	82,000.00	142,615.62	279,107.08
2008 Highway 200 Project (Cap)	(429,182.99)	-	-	388,478.00	-	67,721.24	(108,426.23)
2006-1 2007 Street Project (Cap)	50,199.85	91.99	-	-	-	221,704.22	(171,412.38)
Riverbend (Debt Service)	161,513.83	100,848.85	-	-	-	104,940.50	157,422.18
2008 Hwy 200 Project Debt Retirement	53,560.79	97,822.82	20,000.00	-	-	40,892.84	130,490.77
Praireview	53,358.77	17,285.01	-	-	-	120,332.50	(49,688.72)
2007 Street Project Debt Retirement	399,032.79	343,602.15	-	-	-	286,422.50	456,212.44
Total Major Gov't Funds	\$ 555,422.63	\$ 1,171,480.55	\$ 241,600.63	\$ 388,478.00	\$ 87,000.00	\$ 1,515,401.23	\$ 754,580.58
Nonmajor Governmental Funds:							
<u>Special Revenue Funds:</u>							
Social Security	\$ 15,107.61	\$ 27,805.18	\$ -	\$ -	\$ -	\$ 45,903.64	\$ (2,990.85)
City's Share of Specials	4,282.46	19,779.33	-	-	-	23,230.06	831.73
Emergency	26,649.76	23,686.43	-	-	13,927.73	9,909.33	26,499.13
Planning and Zoning	442.07	490.95	-	-	-	740.00	193.02
Cemetery	(939.01)	9,265.74	6,000.00	-	-	14,539.98	(213.25)
Armory Operations	(13,282.86)	11,731.25	20,000.00	-	-	20,780.07	(2,331.68)
Main Street Community Center	2,026.77	1,045.00	12,000.00	-	-	1,711.54	13,360.23
Forestry	1,234.87	1,726.40	-	-	-	559.24	2,402.03
Mosquito Control	38,304.26	16,229.53	-	-	-	7,728.74	46,805.05
Airport	-	9,219.01	-	-	-	9,219.01	-
Recreation District	2,227.37	5,740.83	-	-	-	8,636.63	(668.43)
Total Special Revenue Funds	\$ 76,053.30	\$ 126,719.65	\$ 38,000.00	\$ -	\$ 13,927.73	\$ 142,958.24	\$ 83,886.98
<u>Debt Service Funds:</u>							
96-2 & 96-3	\$ 1,595.16	\$ 13,338.79	\$ -	\$ -	\$ -	\$ 21,358.50	\$ (6,424.55)
Project 98-1	44,564.45	3,808.35	-	-	-	-	48,372.80
2006 Water Main Debt Retirement	73,645.52	110,235.51	-	-	-	103,057.50	80,823.53
Total Debt Service Funds	\$ 119,805.13	\$ 127,382.65	\$ -	\$ -	\$ -	\$ 124,416.00	\$ 122,771.78
<u>Capital Projects Funds:</u>							
Capital Projects	\$ 16,197.94	\$ 124.16	\$ -	\$ -	\$ -	\$ 930.80	\$ 15,391.30
Equipment Fund	-	-	20,000.00	-	-	-	20,000.00
Total Capital Projects Funds	\$ 16,197.94	\$ 124.16	\$ 20,000.00	\$ -	\$ -	\$ 930.80	\$ 35,391.30
Total Nonmajor Gov't Funds	\$ 212,056.37	\$ 254,226.46	\$ 58,000.00	\$ -	\$ 13,927.73	\$ 268,305.04	\$ 242,050.06
Total Governmental Funds	\$ 767,479.00	\$ 1,425,707.01	\$ 299,600.63	\$ 388,478.00	\$ 100,927.73	\$ 1,783,706.27	\$ 996,630.64
Major Enterprise Funds:							
Water Projects	\$ 247,848.84	\$ 2,227.00	\$ -	\$ -	\$ -	\$ 47,474.40	\$ 202,601.44
Regional Water Treatment Plant	(43,030.90)	-	-	-	-	249,932.36	(292,963.26)
Water Tower Construction	(68,523.75)	-	-	979,129.00	-	1,067,980.12	(157,374.87)
Water Department	199,897.18	289,009.91	810.00	-	5,000.00	160,131.08	324,586.01
Sewer Department	56,986.63	108,945.80	115.14	-	5,000.00	73,307.36	87,740.21
Electric Department	705,072.34	1,704,141.08	401.96	-	190,000.00	1,531,903.76	687,711.62
Total Major Enterprise Funds	\$ 1,098,250.34	\$ 2,104,323.79	\$ 1,327.10	\$ 979,129.00	\$ 200,000.00	\$ 3,130,729.08	\$ 852,301.15
Nonmajor Enterprise Funds:							
Generation Project - Debt	\$ 131,558.33	\$ 120,981.20	\$ -	\$ -	\$ -	\$ 139,626.00	\$ 112,913.53
Sanitation Department	14,442.64	168,189.29	-	-	-	160,975.28	21,656.65
Meter Deposits	40,973.28	6,471.83	-	-	-	5,618.40	41,826.71
Total Nonmajor Enterprise Funds	\$ 186,974.25	\$ 295,642.32	\$ -	\$ -	\$ -	\$ 306,219.68	\$ 176,396.89
Total Enterprise Funds	\$ 1,285,224.59	\$ 2,399,966.11	\$ 1,327.10	\$ 979,129.00	\$ 200,000.00	\$ 3,436,948.76	\$ 1,028,698.04
Total Reporting Entity	\$ 2,052,703.59	\$ 3,825,673.12	\$ 300,927.73	\$ 1,367,607.00	\$ 300,927.73	\$ 5,220,655.03	\$ 2,025,328.68

CITY OF HILLSBORO
Hillsboro, North Dakota

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Year Ended December 31, 2010

Federal Grantor/ Pass-Through Grantor/ Program Title	Federal CFDA Number	Federal Expenditures
<u>U.S. ENVIRONMENTAL PROTECTION AGENCY:</u>		
<u>Passed through the State Department of Health:</u>		
Capitalization Grants for Drinking Water State Revolving Funds, Recovery	66.468	** \$ 1,367,607
<u>U.S. DEPARTMENT OF TRANSPORTATION:</u>		
Alcohol Impaired Driving Countermeasures Incentive Grants I	20.601	\$ 4,491
<u>U.S. DEPARTMENT OF HOMELAND SECURITY:</u>		
<u>Passed through the State Division of Emergency Services:</u>		
Disaster Grants - Public Assistance (Presidentially Declared Disasters)	97.036	\$ 4,928
Total Expenditures of Federal Awards		<u>\$ 1,377,026</u>

** - Major program

NOTE 1: BASIS OF PRESENTATION:

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the City of Hillsboro under programs of the federal government for the year ended December 31, 2010. The information in the schedule is presented in accordance with the requirements of the Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Because the schedule presents only a selected portion of the operations of the City of Hillsboro, it is not intended to and does not present the financial position or changes in net assets of the City of Hillsboro.

NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Expenditures reported on the Schedule are reported on the modified accrual basis of accounting. Such expenditures are recognized following the cost principles contained in OMB Circular A-87, *Cost Principles for State, Local and Indian Tribe Governments*, wherein certain types of expenditures are allowable or are limited as to reimbursement.

STATE AUDITOR

ROBERT R. PETERSON
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Local Government Division:
FARGO OFFICE
MANAGER – DAVID MIX
Phone: (701) 239-7252 Fax: (701) 239-7251

STATE OF NORTH DAKOTA
OFFICE OF THE STATE AUDITOR
STATE CAPITOL
600 E. BOULEVARD AVENUE - DEPT. 117
BISMARCK, NORTH DAKOTA 58505

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*

City Commission
City of Hillsboro
Hillsboro, North Dakota 58045

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hillsboro, North Dakota, as of and for the year ended December 31, 2010, which collectively comprise City of Hillsboro's basic financial statements and have issued our report thereon dated March 12, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered City of Hillsboro's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of City of Hillsboro's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of City of Hillsboro'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, and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the *accompanying schedule of findings and questioned costs*, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

A *deficiency in internal control* 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 such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the *accompanying schedule of findings and questioned costs as items 2010-01 and 2010-02* to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether City of Hillsboro's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of the City of Hillsboro, North Dakota, in a separate letter dated March 12, 2012.

City of Hillsboro's response to the findings identified in our audit are described in the accompanying *schedule of findings and questioned costs*. We did not audit City of Hillsboro's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, city commission, others within the city, federal awarding agencies, and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink, appearing to read "Bob Peterson". The signature is fluid and cursive, with a large initial "B" and "P".

Robert R. Peterson
State Auditor

March 12, 2012

STATE AUDITOR

ROBERT R. PETERSON
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Fax (701) 328-1406



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MANAGER – DAVID MIX
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STATE OF NORTH DAKOTA
OFFICE OF THE STATE AUDITOR
STATE CAPITOL
600 E. BOULEVARD AVENUE - DEPT. 117
BISMARCK, NORTH DAKOTA 58505

REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

Independent Auditor's Report

City Commission
City of Hillsboro
Hillsboro, North Dakota

Compliance

We have audited the City of Hillsboro's compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on the City of Hillsboro's major federal program for the year ended December 31, 2010. City of Hillsboro's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal program is the responsibility of the City of Hillsboro's management. Our responsibility is to express an opinion on the City of Hillsboro's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City of Hillsboro's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the City of Hillsboro's compliance with those requirements.

In our opinion, City of Hillsboro complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended December 31, 2010.

Internal Control Over Compliance

Management of the City of Hillsboro is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the City of Hillsboro's internal control over compliance with the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City of Hillsboro's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance 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 compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be *material weaknesses*, as defined above.

This report is intended solely for the information and use of management, the city commission, others within the city, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in cursive script, appearing to read "Bob Peterson".

Robert R. Peterson
State Auditor

March 12, 2012

CITY OF HILLSBORO
Hillsboro, North Dakota

SCHEDULE OF FINDINGS AND RESPONSES
For the Year Ended December 31, 2010

Section I - Summary of Auditor's Results

Financial Statements

Type of Auditor's Report Issued?

Governmental Activities	Adverse
Business-Type Activities	Adverse
Major Governmental Funds	Unqualified on modified cash basis
Major Business-Type Funds	Adverse
Aggregate Remaining Fund Information	Unqualified on modified cash basis

Internal Control over financial reporting:

Material weakness(es) identified?	X	Yes			No
Significant deficiencies identified?		Yes		X	No
Noncompliance material to financial statements noted?		Yes		X	No

Federal Awards

Internal Control over major programs:

Material Weakness Identified?		Yes		X	No
Reportable conditions identified not considered to be material weaknesses?		Yes		X	None reported
Type of auditor's report issued on compliance for major program?	Unqualified				
Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?		Yes		X	No

Identification of major programs:

CFDA Numbers	Name of Federal Program Or Cluster
66.468 (ARRA)	Capitalization Grants for Drinking Water State Revolving Funds (ARRA)

Dollar threshold used to distinguish between Type A and B programs:

\$ 300,000

Auditee qualified as low-risk auditee?		Yes		X	No
--	--	-----	--	---	----

Section II - Financial Statement Findings

2010-01 - CAPITAL ASSET RECORDS

Condition

The City of Hillsboro, North Dakota, does not maintain complete capital asset records for the governmental activities, the business-type activities and the major business-type funds.

CITY OF HILLSBORO

Schedule of Findings and Responses – Continued

Criteria

Accounting principles generally accepted in the United States of America require the financial statements include capital assets for governmental activities, business-type activities and major business-type funds, net of accumulated depreciation.

Effect

The omission of capital assets from the financial statements results in an incomplete presentation of the City of Hillsboro's financial statements and adverse opinions on the city's financial statements for governmental activities, business-type activities and major business-type funds.

Recommendation

The city should establish and maintain capital asset records for governmental activities, business-type activities and major business-type funds using historical cost or estimated historical cost and set up and maintain depreciation schedules for these assets. Also detailed capital asset records showing additions and deletions should be maintained.

Client Response

We agree with this recommendation. However the board does not concur that this is a cost effective to establish capital asset records at this time according to Auditor recommendation.

2010-02 - SEGREGATION OF DUTIES

Condition

The City of Hillsboro, North Dakota has one city auditor and one deputy auditor responsible for accounting functions including maintaining accounting records, reconciling accounts and paying bills.

Criteria

Proper internal control over financial reporting and custody of assets dictates that there should be sufficient accounting personnel so duties of employees are segregated. The segregation of duties would provide better control over the assets of the city.

Effect

There is no segregation of duties as one employee is responsible to collect monies, deposit monies, issue checks, send checks to vendors, record receipts and disbursements in journals, maintain the general ledger, and prepare financial statements. This increases the risk of misstatement of the city's financial condition.

Recommendation

Due to the size of the city, it is not feasible to obtain proper separation of duties and no recommendation will be made. However, duties should be segregated to the extent possible within the Auditor's office.

Client Response

I agree with this finding except for the fact that is not feasible at this time due to the number of personnel in the office and cost considerations to add any additional staff.

Section III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

No matters were reported.