

OFFICE OF THE STATE AUDITOR

AUDIT REPORT

**CITY OF HILLSBORO
HILLSBORO, NORTH DAKOTA**

FOR THE YEAR ENDED DECEMBER 31, 2013



CITY OF HILLSBORO
Hillsboro, North Dakota

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CITY OF HILLSBORO
Hillsboro, North Dakota

CITY OFFICIALS

December 31, 2013

Mark Forseth	President
Curt Kaufman	Vice-President
Lorraine Tibert	Board Member
Mike Kress	Board Member
Dave Sather	Board Member
Lesley Connelly	Auditor
Julie Bjorklund	Deputy Auditor
John Juelson	Attorney

STATE AUDITOR

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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 AUDITORS REPORT

Independent Auditor's Opinion

City Commission
City of Hillsboro
Hillsboro, North Dakota

Report on the Financial Statements

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, 2013, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Summary of Opinions

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

Basis for Adverse Opinions Governmental Activities, Business-Type Activities, and Major Business-Type Funds

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 position 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 position and expenses of the governmental activities, the business-type activities and the business-type funds is not reasonably determinable.

Adverse Opinions

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, 2013, and the changes in financial position thereof for the year then ended.

Basis for Unmodified Opinion of Modified Cash Basis for Major Governmental Funds and Aggregate Remaining Fund Information

As discussed in Note 1 to the financial statements, 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.

Unmodified Opinions

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 of the City of Hillsboro, North Dakota, as of December 31, 2013 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.

Other Matters

Required Supplementary Information

Management has omitted the management's discussion and analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

Accounting principles generally accepted in the United States of America require that the *budgetary comparison information* on pages 26-28 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

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 arising from cash transactions* and *schedule of expenditures of federal awards*, as required by 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 is not a required part of the basic financial statements.

The *schedule of fund activity arising from cash transactions and schedule of expenditures of federal awards* are the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the *schedule of fund activity arising from cash transactions and the schedule of expenditures of federal awards* are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Report on Other Legal and Regulatory Requirements

In accordance with Government Auditing Standards, we have also issued our report dated August 22, 2014, 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the City of Hillsboro's internal control over financial reporting and compliance.



Robert R. Peterson
State Auditor

Fargo, North Dakota
August 22, 2014

CITY OF HILLSBORO
Hillsboro, North Dakota

STATEMENT OF NET POSITION - MODIFIED CASH BASIS
December 31, 2013

	Primary Government		
	Governmental Activities	Business-Type Activities	Total
ASSETS:			
Cash	\$ 1,356,959	\$ 560,974	\$ 1,917,933
Investments	175,152	557,194	732,346
Total Assets	\$ 1,532,111	\$ 1,118,168	\$ 2,650,279
LIABILITIES:			
Benefits Payable	\$ 1,839	\$ 215	\$ 2,054
Long-Term Liabilities:			
Due Within One Year:			
Special Assessment Bonds Payable	745,000	-	745,000
Revenue Bonds Payable	-	170,000	170,000
State Revolving Loan Fund Payable	101,000	-	101,000
Due After One Year:			
Special Assessment Bonds Payable	3,470,000	-	3,470,000
Revenue Bonds Payable	-	4,029,087	4,029,087
State Revolving Loan Fund Payable	948,000	-	948,000
Capital Leases Payable	31,294	-	31,294
Total Liabilities	\$ 5,297,133	\$ 4,199,302	\$ 9,496,435
NET POSITION:			
Restricted for:			
Public Works	\$ 233,144	\$ -	\$ 233,144
Economic/Job Development	462,942	-	462,942
Capital Improvements	91,196	-	91,196
Emergency	33,680	-	33,680
Other Purposes	27,023	-	27,023
Unrestricted	(4,613,007)	(3,081,134)	(7,694,141)
Total Net Position	\$ (3,765,022)	\$ (3,081,134)	\$ (6,846,156)

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, 2013

Functions/Programs	Program Revenues			Net (Expense) Revenue and Changes in Net Position		
	Expenses	Charges for Services	Operating Grants and Contributions	Primary Government		Total
				Governmental Activities	Business-Type Activities	
<u>Governmental Activities:</u>						
General Government	\$ 262,796	\$ 57,250	\$ 4,988	\$ (200,558)	\$ -	\$ (200,558)
Public Safety	192,343	-	-	(192,343)	-	(192,343)
Public Works/Infrastructure	393,262	-	188,790	(204,472)	-	(204,472)
Culture and Recreation	80,744	-	-	(80,744)	-	(80,744)
Miscellaneous	4,428	-	-	(4,428)	-	(4,428)
Capital Outlay	2,000	-	-	(2,000)	-	(2,000)
Interest on Long-Term Debt	313,272	-	-	(313,272)	-	(313,272)
Total Governmental Activities	\$ 1,484,134	\$ 57,250	\$ 193,778	\$ (1,233,106)	\$ -	\$ (1,233,106)
<u>Business-Type Activities:</u>						
Water Funds	\$ 4,054,208	\$ 496,169	\$ 2,782,035	\$ -	\$ (776,004)	\$ (776,004)
Electric Funds	2,035,570	2,156,407	-	-	120,837	120,837
Sewer Funds	172,158	108,474	-	-	(63,684)	(63,684)
Sanitation	196,524	193,325	-	-	(3,199)	(3,199)
Total Business-Type Activities	\$ 6,458,460	\$ 2,954,375	\$ 2,782,035	\$ -	\$ (722,050)	\$ (722,050)
Total Primary Government	\$ 7,942,594	\$ 3,011,625	\$ 2,975,813	\$ (1,233,106)	\$ (722,050)	\$ (1,955,156)
<u>General Revenues:</u>						
Taxes:						
Property taxes levied for general purposes	\$ 101,175	\$ -	\$ 101,175			
Property taxes levied for special purposes	161,413	-	161,413			
Property taxes levied for debt service	660,824	-	660,824			
Sales taxes	361,161	-	361,161			
State Aid Distribution	167,723	-	167,723			
Interest Income	4,710	1,517	6,227			
Miscellaneous Revenue	116,272	129,181	245,453			
Loan Forgiveness	-	243,000	243,000			
Transfers	200,000	(200,000)	-			
Total General Revenues and Transfers	\$ 1,773,278	\$ 173,698	\$ 1,946,976			
Change in Net Position	\$ 540,172	\$ (548,352)	\$ (8,180)			
Net Position - January 1	\$ (4,305,194)	\$ (2,532,782)	\$ (6,837,976)			
Net Position - December 31	\$ (3,765,022)	\$ (3,081,134)	\$ (6,846,156)			

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, 2013

	Major Funds						Total Governmental Funds
	General Fund	Highway Tax Fund	City Sales Tax Fund	Capital Project Funds	Debt Service Funds	Other Governmental Funds	
ASSETS							
Cash and Cash Equivalents	\$ 174,366	\$ 153,776	\$ 287,790	\$ 91,196	\$ 509,760	\$ 140,071	\$ 1,356,959
Investments	-	-	175,152	-	-	-	175,152
Due from Other Funds	5,242	-	-	-	-	-	5,242
Total Assets	\$ 179,608	\$ 153,776	\$ 462,942	\$ 91,196	\$ 509,760	\$ 140,071	\$ 1,537,353
LIABILITIES AND FUND BALANCES							
<u>Liabilities:</u>							
Benefits Payable	\$ 1,639	\$ -	\$ -	\$ -	\$ -	\$ 200	\$ 1,839
Due to Other Funds	-	-	-	-	-	5,242	5,242
Total Liabilities	\$ 1,639	\$ -	\$ -	\$ -	\$ -	\$ 5,442	\$ 7,081
<u>Fund Balances:</u>							
Committed:							
General Government	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 13,671	\$ 13,671
Restricted:							
Debt Service	-	-	-	-	509,760	-	509,760
Public Works	-	153,776	-	-	-	79,368	233,144
Economic Development	-	-	462,942	-	-	-	462,942
Capital Improvements	-	-	-	91,196	-	-	91,196
Emergency	-	-	-	-	-	33,680	33,680
General Government	-	-	-	-	-	13,352	13,352
Unassigned							
General Fund	177,969	-	-	-	-	-	177,969
Negative Fund Balances	-	-	-	-	-	(5,442)	(5,442)
Total Fund Balances	\$ 177,969	\$ 153,776	\$ 462,942	\$ 91,196	\$ 509,760	\$ 134,629	\$ 1,530,272
Total Liabilities and Fund Balances	\$ 179,608	\$ 153,776	\$ 462,942	\$ 91,196	\$ 509,760	\$ 140,071	\$ 1,537,353

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

CITY OF HILLSBORO
Hillsboro, North Dakota

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET
TO THE STATEMENT OF NET POSITION - MODIFIED CASH BASIS
GOVERNMENTAL FUNDS
December 31, 2013

Total *Fund Balances* for Governmental Funds \$ 1,530,272

Total *net position* reported for governmental activities in the statement of net position 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 position. Balances at December 31, 2013 are:

Special Assessment Bonds Payable	\$ (4,215,000)	
Loans Payable	(1,049,000)	
Capital Leases Payable	<u>(31,294)</u>	
Total Long-Term Liabilities		<u>(5,295,294)</u>
Total Net Position of Governmental Activities		<u>\$ (3,765,022)</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, 2013

	Major Funds						Total Governmental Funds
	General Fund	Highway Tax Fund	City Sales Tax Fund	Capital Project Funds	Debt Service Funds	Other Governmental Funds	
Revenues:							
Property Taxes	\$ 101,175	\$ -	\$ -	\$ -	\$ 92,461	\$ 68,952	\$ 262,588
Sales Taxes	-	-	361,161	-	-	-	361,161
Special Assessments	-	-	-	-	660,824	-	660,824
Licenses, Permits and Fees	38,318	-	-	-	-	-	38,318
Intergovernmental	172,711	188,790	-	-	-	-	361,501
Charges for Services	-	-	-	-	-	18,752	18,752
Fines and Forfeits	180	-	-	-	-	-	180
Interest Income	750	-	294	-	3,656	10	4,710
Miscellaneous	36,800	385	-	37	52,087	26,963	116,272
Total Revenues	\$ 349,934	\$ 189,175	\$ 361,455	\$ 37	\$ 809,028	\$ 114,677	\$ 1,824,306
Expenditures:							
Current:							
General Government	\$ 159,130	\$ -	\$ -	\$ -	\$ -	\$ 103,666	\$ 262,796
Public Safety	192,343	-	-	-	-	-	192,343
Public Works	-	381,911	-	-	-	11,351	393,262
Culture and Recreation	80,744	-	-	-	-	-	80,744
Economic Development	-	-	217,106	-	-	18,183	235,289
Other	4,428	-	-	-	-	-	4,428
Capital Outlay	-	-	-	2,000	-	-	2,000
Dept Service:							
Principal	-	65,287	-	48,955	3,404,225	-	3,518,467
Interest	-	1,400	-	1,045	234,527	-	236,972
Fees	-	-	-	-	24,309	-	24,309
Total Expenditures	\$ 436,645	\$ 448,598	\$ 217,106	\$ 52,000	\$ 3,663,061	\$ 133,200	\$ 4,950,610
Excess (Deficiency) of Revenues Over Expenditures	\$ (86,711)	\$ (259,423)	\$ 144,349	\$ (51,963)	\$ (2,854,033)	\$ (18,523)	\$ (3,126,304)
Other Financing Sources (Uses):							
Transfers In	\$ 124,000	\$ 85,000	\$ -	\$ 130,688	\$ 357,447	\$ 19,800	\$ 716,935
Lease Financing	-	145,536	-	-	-	-	145,536
Bonds Proceeds	-	-	-	28,747	3,075,000	-	3,103,747
Bond Discount	-	-	-	-	(51,991)	-	(51,991)
Transfers Out	-	(5,000)	(62,000)	(1,800)	(448,135)	-	(516,935)
Total Other Financing Sources and Uses	\$ 124,000	\$ 225,536	\$ (62,000)	\$ 157,635	\$ 2,932,321	\$ 19,800	\$ 3,397,292
Net Change in Fund Balances	\$ 37,289	\$ (33,887)	\$ 82,349	\$ 105,672	\$ 78,288	\$ 1,277	\$ 270,988
Fund Balances - January 1	\$ 140,680	\$ 187,663	\$ 380,593	\$ (14,476)	\$ 431,472	\$ 133,352	\$ 1,259,284
Fund Balance - December 31	\$ 177,969	\$ 153,776	\$ 462,942	\$ 91,196	\$ 509,760	\$ 134,629	\$ 1,530,272

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

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, 2013

Net Change in *Fund Balances* - Total Governmental Funds \$ 270,988

The change in net position 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 position. Issuance of long-term debt decreases net position. This is the amount by which debt repayment exceeded debt proceeds.

Issuance of Special Assessment Bonds	\$ (3,075,000)	
Issuance of Loans	(28,747)	
Issuance of Capital Leases	(145,536)	
Repayment of Special Assessment Bonds	3,305,000	
Repayment of Loans	99,225	
Repayment of Capital Leases	<u>114,242</u>	<u>269,184</u>

Change in Net Position of Governmental Activities \$ 540,172

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

CITY OF HILLSBORO
Hillsboro, North Dakota

STATEMENT OF NET POSITION - MODIFIED CASH BASIS
PROPRIETARY FUNDS
December 31, 2013

	Business-Type Activities - Enterprise Funds				
	Water Funds	Electric Funds	Sewer Funds	Sanitation	Total Enterprise Funds
ASSETS					
Cash and Cash Equivalents	\$ -	\$ 337,700	\$ 189,607	\$ 33,667	\$ 560,974
Investments	89,306	417,677	50,211	-	557,194
Total Assets	\$ 89,306	\$ 755,377	\$ 239,818	\$ 33,667	\$ 1,118,168
LIABILITIES					
Current Liabilities:					
Benefits Payable	\$ -	\$ 215	\$ -	\$ -	\$ 215
Bonds Payable	-	130,000	40,000	-	170,000
Total Current Liabilities	\$ -	\$ 130,215	\$ 40,000	\$ -	\$ 170,215
Noncurrent Liabilities:					
Bonds Payable	\$ 3,164,087	\$ 170,000	\$ 695,000	\$ -	\$ 4,029,087
Total Liabilities	\$ 3,164,087	\$ 300,215	\$ 735,000	\$ -	\$ 4,199,302
NET POSITION					
Unrestricted	\$ (3,074,781)	\$ 455,162	\$ (495,182)	\$ 33,667	\$ (3,081,134)
Total Net Position	\$ (3,074,781)	\$ 455,162	\$ (495,182)	\$ 33,667	\$ (3,081,134)

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 POSITION - MODIFIED CASH BASIS
PROPRIETARY FUNDS

For the Year Ended December 31, 2013

	Business-Type Activities - Enterprise Funds				
	Water Funds	Electric Funds	Sewer Funds	Sanitation	Total Enterprise Funds
<u>Operating Revenues:</u>					
Charges for Sales and Services:	\$ 496,169	\$ 2,156,407	\$ 108,474	\$ 193,325	\$ 2,954,375
<u>Operating Expenses:</u>					
Salaries and Wages	\$ 114,035	\$ 90,085	\$ 36,202	\$ -	\$ 240,322
Professional Services (Legal, Engineering, etc)	328,946	63,721	12,579	180,727	585,973
Maintenance & Supplies	82,386	81,972	26,131	-	190,489
Purchased Power Costs	-	1,626,503	-	-	1,626,503
Machinery and Equipment	37,786	127,365	92,467	4,162	261,780
Clearing	-	23,716	-	-	23,716
Miscellaneous	10,813	5,691	4,674	11,593	32,771
Total Operating Disbursements	\$ 573,966	\$ 2,019,053	\$ 172,053	\$ 196,482	\$ 2,961,554
Operating Income (Loss)	\$ (77,797)	\$ 137,354	\$ (63,579)	\$ (3,157)	\$ (7,179)
<u>Nonoperating Revenues (Expenses):</u>					
Interest on Investments	\$ 478	\$ 905	\$ 134	\$ -	\$ 1,517
Grants	2,782,035	-	-	-	2,782,035
Loan Forgiveness	243,000	-	-	-	243,000
Plant and Equipment	(3,434,058)	-	-	-	(3,434,058)
Miscellaneous	18,079	110,105	-	-	128,184
Retirement of Debt - Interest & Fees	(40,661)	(16,517)	(105)	(42)	(57,325)
Other Nonoperating Revenues (Expenses)	(5,523)	-	-	997	(4,526)
Total Nonoperating Revenues (Expenses)	\$ (436,650)	\$ 94,493	\$ 29	\$ 955	\$ (341,173)
Income Before Transfers	\$ (514,447)	\$ 231,847	\$ (63,550)	\$ (2,202)	\$ (348,352)
Transfers In	\$ -	\$ 138,000	\$ -	\$ -	\$ 138,000
Transfers Out	(5,000)	(328,000)	(5,000)	-	(338,000)
Total Transfers	\$ (5,000)	\$ (190,000)	\$ (5,000)	\$ -	\$ (200,000)
Change in Net Position	\$ (519,447)	\$ 41,847	\$ (68,550)	\$ (2,202)	\$ (548,352)
Total Net Position - January 1	\$ (2,555,334)	\$ 413,315	\$ (426,632)	\$ 35,869	\$ (2,532,782)
Total Net Position - December 31	\$ (3,074,781)	\$ 455,162	\$ (495,182)	\$ 33,667	\$ (3,081,134)

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, 2013

	Business-Type Activities - Enterprise Funds				Total Enterprise Funds
	Water Funds	Electric Funds	Sewer Funds	Sanitation	
<u>Cash Flows from Operating Activities:</u>					
Receipts from Customers and Users	\$ 496,169	\$ 2,156,407	\$ 108,474	\$ 193,325	\$ 2,954,375
Payments to Suppliers	(459,931)	(1,928,968)	(135,851)	(196,482)	(2,721,232)
Payments to Employees	(114,694)	(89,870)	(36,202)	-	(240,766)
Net Cash Provided (Used) by Operating Activities	<u>\$ (78,456)</u>	<u>\$ 137,569</u>	<u>\$ (63,579)</u>	<u>\$ (3,157)</u>	<u>\$ (7,623)</u>
<u>Cash Flows from Noncapital Financing Activities:</u>					
Miscellaneous Revenue (Expense)	\$ 18,079	\$ 110,105	\$ -	\$ -	\$ 128,184
Grants	2,782,035	-	-	-	2,782,035
Transfers from Other Funds	-	138,000	-	-	138,000
Transfers to Other Funds	(5,000)	(328,000)	(5,000)	-	(338,000)
Other	(5,523)	98	718	997	(3,710)
Net Cash Provided (Used) by Noncapital Financing Activities	<u>\$ 2,789,591</u>	<u>\$ (79,797)</u>	<u>\$ (4,282)</u>	<u>\$ 997</u>	<u>\$ 2,706,509</u>
<u>Cash Flows from Capital and Related Financing Activities:</u>					
Purchases and Construction of Capital Assets	\$ (3,434,058)	\$ -	\$ -	\$ -	\$ (3,434,058)
Issuance of Capital Debt	2,369,087	-	-	-	2,369,087
Principal Paid on Capital Debt	(170,000)	(120,000)	-	-	(290,000)
Interest Paid on Capital Debt	(40,661)	(16,517)	(105)	(42)	(57,325)
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>\$ (1,275,632)</u>	<u>\$ (136,517)</u>	<u>\$ (105)</u>	<u>\$ (42)</u>	<u>\$ (1,412,296)</u>
<u>Cash Flows from Investing Activities:</u>					
Purchases, Sales & Maturities of Investments	\$ (1,435,981)	\$ 415,540	\$ 257,439	\$ 35,869	\$ (727,133)
Interest Income	478	905	134	-	1,517
Net Cash Provided (Used) by Investing Activities	<u>\$ (1,435,503)</u>	<u>\$ 416,445</u>	<u>\$ 257,573</u>	<u>\$ 35,869</u>	<u>\$ (725,616)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	<u>\$ -</u>	<u>\$ 337,700</u>	<u>\$ 189,607</u>	<u>\$ 33,667</u>	<u>\$ 560,974</u>
Cash and Cash Equivalents, January 1	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Cash and Cash Equivalents, December 31	<u>\$ -</u>	<u>\$ 337,700</u>	<u>\$ 189,607</u>	<u>\$ 33,667</u>	<u>\$ 560,974</u>
Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities					
Operating Income (Loss)	<u>\$ (77,797)</u>	<u>\$ 137,354</u>	<u>\$ (63,579)</u>	<u>\$ (3,157)</u>	<u>\$ (7,179)</u>
<u>Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities:</u>					
Change in Assets and Liabilities:					
Benefits Payable	<u>\$ (659)</u>	<u>\$ 215</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (444)</u>
Net Cash Provided (Used) by Operating Activities	<u>\$ (78,456)</u>	<u>\$ 137,569</u>	<u>\$ (63,579)</u>	<u>\$ (3,157)</u>	<u>\$ (7,623)</u>

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, 2013

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 position 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 Fund. This fund is used to account for taxes received for streets and highways and for repair and maintenance projects on them. The primary revenue source in this fund is restricted grants.

City Sales Tax Fund. This fund accounts for sales tax money for the city. The primary revenue source in this fund includes restricted sales tax dollars.

Capital Projects Funds. This fund accounts for the accumulation of funds for various capital improvements to city properties. The primary revenue source in this fund is restricted grants.

Debt Service Funds. Debt service funds are used to account for the accumulation of resources for, and the payment of, long-term debt principal, interest, and related costs.

The City reports the following major enterprise funds:

Water Funds. This fund is used to account for customer receipts and payments for water fees and construction costs of various water projects.

Electric Funds. This fund is used to account for customer receipts and payments for electric fees, as well as the payment of long-term debt principal, interest, and related costs for electrical purposes.

Sewer Funds. This fund is used to account for customer receipts and payments for sewer fees and costs related to Kingman Sewer Addition.

Sanitation Fund. This fund is used to account for customer receipts and payments for sanitation 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 position 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 position (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 position.

Basis of Accounting

In the government-wide Statement of Net Position 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 position/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.

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.

The investments of the City at December 31, 2013 consist of certificates of deposit stated at cost with maturities in excess of three months.

E. Fund Balances / Net Position

Prior to GASB Statement No. 54, in the fund financial statements, the governmental funds reported reservations of fund balances for amounts that were not available for appropriation or were legally restricted by outside parties for use for a specific purpose. Designations of fund balances represented tentative management plans that were subject to change. GASB Statement No. 54 established new fund balance classifications that comprise a hierarchy based on the extent to which the government is bound to honor constraints (restrictions or limitations) imposed upon the use of the resources reported in governmental funds.

Fund Balance Spending Policy:

It is the policy of the City of Hillsboro to spend restricted resources first, followed by unrestricted resources. It is also the policy of the Board to spend unrestricted resources of funds in the following order: committed, assigned and then unassigned.

CITY OF HILLSBORO

Notes to the Financial Statements – Continued

Major Special Revenue Fund Purposes & Revenue Sources:

Purposes and major revenue sources of the major special revenue funds (capital improvements funds, sales tax economic development fund, and revolving loan fund) are disclosed in more detail in Note 1B in the discussion of major funds.

GASB Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions

GASB 54 requires the fund balance amounts to be properly reported within one of the fund balance categories listed below.

CLASSIFICATION	DEFINITION	EXAMPLES
Nonspendable	Amounts that cannot be spent because they are either (a) not in spendable form or (b) legally or contractually required to be maintained intact.	Inventories, prepaid amounts (expenses), long-term receivables (loans), endowment funds.
Restricted	Fund balance is reported as restricted when constraints are placed on the use of resources that are either (a) Externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments. (b) Imposed by law through constitutional provisions or enabling legislation.	Funds restricted by State Statute, unspent bond proceeds, grants earned but not spent, debt covenants, taxes raised for a specific purpose.
Committed	A committed fund balance includes amounts that can only be used for specific purposes pursuant to constraints imposed by formal action of the government's highest level of decision-making authority, the governing board. Formal action is required to be taken to establish, modify or rescind a fund balance commitment.	By board action, construction, claims and judgments, retirements of loans and notes payable, capital expenditures and self-insurance.
Assigned	Assigned fund balances are amounts that are constrained by the government's intent to be used for specific purposes, but are under the direction of the board and the business manager.	By board action, construction, claims and judgments, retirements of loans and notes payable, capital expenditures and self-insurance.
Unassigned	Unassigned fund balance is the lowest classification for the General Fund. This is fund balance that has not been reported in any other classification. (a) The General Fund is the only fund that can report a positive unassigned fund balance.	Available for any remaining general fund expenditure.

City of Hillsboro had restricted, committed, and unassigned fund balances reported in the balance sheet at December 31, 2013.

Restricted Fund Balances – consist of the following items at December 31, 2013:

Restricted fund balances are shown by primary function on the balance sheet for debt service, public works, sales tax/economic development, culture & recreation, capital improvements, emergency, and other purposes (reported in the other governmental funds). Restricted fund balances are restricted by enabling legislation (primarily state law for various tax levies) and by outside 3rd parties (State & Federal governments for various grants & reimbursements and bond indentures).

Special Revenue Funds – Restricted & Committed Fund Balances:

- (a) Restricted by specified tax levies and/or restricted Federal & State grants/reimbursements:
 - Restricted tax levies – includes fund balances for various tax levies other than the general fund.
 - Restricted grants/reimbursements – primarily includes disaster type grants in various special revenue funds, and other grant funds.
- (b) Committed fund balances (special revenue funds) – committed by governing board city council action;
 - Committed in special revenue funds for various armory operations, MSCC rental, CDLF – wholesale foods, and recreation district;

Net Position:

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.

Prior to GASB 63, amounts were reported as equity on the statement of net assets in two primary categories (restricted and unrestricted). Subsequent to GASB 63, the statement of net assets was changed to the statement of net position, and net assets equity was changed to net position. Net position is shown in two primary categories (restricted and unrestricted), outlined in further detail as follows:

Restrictions of net position shown in the statement of net position are due to restricted tax levies, restricted Federal & State grants/reimbursements, and restricted amounts for unspent bond proceeds reported in debt service and capital projects funds. Additionally, restricted net position is shown in the statement of net position by primary function as fund balances are shown in the balance sheet, and is restricted for debt service, public works, job/economic development, culture & recreation, emergency, and other purposes.

Unrestricted net position consists of activity primarily related to the general fund and negative capital projects fund amounts at year-end. The unrestricted net position is available to meet the City's ongoing obligations

I. Interfund Transactions

In the governmental fund statements, transactions that constitute reimbursements to a fund for expenditures initially made from it that are properly applicable to another fund, are recorded as expenditures in the reimbursing fund and as reductions of expenditures in the fund that is reimbursed.

All other interfund transactions, except reimbursements, are reported as transfers.

In the government-wide financial statements, interfund transactions have been eliminated.

CITY OF HILLSBORO

Notes to the Financial Statements – Continued

NOTE 2: LEGAL COMPLIANCE - BUDGETS

BUDGET AMENDMENTS

The city's governing board approved the following amendments to the city budget in 2013:

	REVENUES/TRANSFERS/FINANCING SOURCES		
	Original Budget	Amendment	Amended Budget
Governmental Funds:			
<u>Major Funds</u>			
General Fund	\$409,788	\$ 40,146	\$449,934
Highway Tax Fund	234,500	39,674	274,174
Sales Tax	251,000	110,454	361,454
<u>Capital Project Funds</u>			
2008 Highway 200	-	139,435	139,435
<u>Debt Service Funds</u>			
Project 2006 Water Main	102,400	3,534	105,934
Highway 200 Debt Service	135,500	13,391	148,891
2007 Streets Debt Service	312,000	12,057	324,057
Kingman Sewer	-	67,694	67,694
<u>Nonmajor Funds</u>			
Social Security	30,000	455	30,455
Cemetery	8,550	3,395	11,945
CDLF - Wholesale Foods	-	18,987	18,987

	EXPENDITURES AND TRANSFERS OUT		
	Original Budget	Amendment	Amended Budget
Governmental Funds:			
<u>Major Funds</u>			
General Fund	\$387,479	\$ 47,900	\$435,379
Highway Tax Fund	244,685	63,376	308,061
Sales Tax	233,000	46,106	279,106
<u>Debt Service Funds</u>			
Riverbend Debt Service	92,121	359	92,480
Highway 200 Debt Service	103,300	116,855	220,155
Kingman Sewer	-	15,798	15,798
<u>Nonmajor Funds</u>			
Social Security	30,000	5,107	35,107
CDLF - Wholesale Foods	-	18,182	18,182
Recreation District	9,550	150	9,700

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, 2013, the city's carrying amount of deposits was \$2,590,543 and the bank balances totaled \$2,597,510. Of the bank balances, \$786,019 was covered by Federal Depository Insurance. The remaining balances totaling \$1,811,491 were collateralized with securities held by the pledging financial institution's agent in the government's name.

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, 2013, the City held certificates of deposit with maturities in excess of 3 months in the amount of \$300,000, respectively, 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, 2013 are as follows:

	Due To	Due From
<u>Major Fund</u>		
General Fund	\$5,242	\$ -
<u>Nonmajor Funds</u>		
Social Security	-	4,750
Armory Operations	-	155
Recreation District	-	337
Total	\$5,242	\$5,242

The composition of due to and due from other funds is related to negative cash fund balances in various non-major governmental funds covered by the general fund.

NOTE 6: TRANSFERS

The following is a summary of transfers in and transfers out as reported in the basic financial statements for the year ended December 31, 2013:

Fund	Transfers In	Transfers Out
Governmental Funds		
<u>Major Funds</u>		
General Fund	\$124,000	\$ -
Highway Tax/Streets	85,000	5,000
City Sales Tax Fund	-	62,000
Capital Projects	130,688	1,800
Debt Service	357,446	448,134
<u>Nonmajor Funds:</u>		
Cemetery	3,800	-
Armory Operations	11,000	-
Main Street Community Center	5,000	-
Enterprise Funds		
<u>Major Funds</u>		
Water Funds	-	5,000
Electric Funds	138,000	328,000
Sewer Funds	-	5,000
Total Transfers	\$854,934	\$854,934

CITY OF HILLSBORO

Notes to the Financial Statements – Continued

NOTE 7: LONG-TERM LIABILITIES

During the years ended December 31, 2013, the following changes occurred in long-term liabilities of the city:

Governmental Activities:

Governmental Activities:	Balance 1-1-13	Increases	Decreases	Balance 12-31-13	Due Within One Year
Special Assessment Bonds	\$4,445,000	\$3,075,000	\$3,305,000	\$4,215,000	\$745,000
Revolving Loan Payable	1,119,478	28,747	99,225	1,049,000	101,000
Capital Lease Payable	-	145,536	114,242	31,294	-
Total Governmental Activities	\$5,564,478	\$3,249,283	\$3,518,467	\$5,295,294	\$846,000

Business-Type Activities (Proprietary Funds)

Business-Type Activities:	Balance 1-1-13	Increases	Decreases	Balance 12-31-13	Due Within One Year
Revenue Bonds Payable	\$2,120,000	\$2,369,087	\$290,000	\$4,199,087	\$170,000
Capital Lease Payable	-	6,854	6,854	-	-
Total Business-Type Activities	\$2,120,000	\$2,375,941	\$296,854	\$4,199,087	\$170,000

SPECIAL ASSESSMENT BONDS

\$785,000 Special Assessment Bonds of 2011 due in annual installments of \$40,000 to \$65,000 through May 2024; interest at 3.5% to 4.75% \$ 620,000

\$605,000 Special Assessment Bonds of 2013 due in annual installments of \$85,000 to \$90,000 through May 2019; interest at 0.65% to 1.5% 520,000

\$3,075,000 Refunding Improvement Bonds of 2013 due in annual installments of \$335,000 to \$350,000 through May 2022; interest at 0.65% to 2.1% 3,075,000

Total Special Assessment Bonds \$4,215,000

Advanced Refunding – Lease Revenue Bonds 2005:

In 2013, the Special Assessment Bonds of 2007 and Special Assessment Bonds of 2007-B in the amounts of \$1,980,000 and \$925,000 were advance refunded. Refunding Improvement Bonds of 2013 were issued with a principal amount of \$3,075,000 with interest rates ranging from 0.65% to 2.10% was issued to acquire a net present value cash flow savings of \$545,690.

STATE REVOLVING FUND LOANS

\$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% \$ 704,000

CITY OF HILLSBORO

Notes to the Financial Statements – Continued

STATE REVOLVING FUND LOANS - CONTINUED

\$417,225 Drawdown for the Highway 200 project, issued in 2011. No set payment schedule, interest at .5 to 2.5%. Note: the IRS is subsidizing part of each interest payment.	<u>\$ 345,000</u>
Total State Revolving Fund Loans	<u>\$1,049,000</u>
Total Governmental Activities	<u>\$5,264,000</u>

Special assessment bond and Drinking Water Improvement Bonds of 2007 debt service requirements to maturity are as follows:

GOVERNMENTAL ACTIVITIES						
Year Ending December 31	Special Assessment Payable		SRF Loan Payable		Capital Lease Payable	
	Principal	Interest	Principal	Interest	Principal	Interest
2014	\$ 460,000	\$ 72,856	\$ 96,000	\$ 26,225	\$ -	\$ -
2015	480,000	67,883	98,000	23,825	15,310	1,377
2016	485,000	61,943	105,000	21,375	15,984	703
2017	495,000	54,894	107,000	18,750	-	-
2018	485,000	46,903	109,000	16,075	-	-
2019 - 2023	1,810,000	106,149	379,000	40,925	-	-
2024 - 2028	-	-	130,000	13,500	-	-
2029 - 2033	-	-	25,000	625	-	-
Totals	<u>\$4,215,000</u>	<u>\$410,626</u>	<u>\$1,049,000</u>	<u>\$161,300</u>	<u>\$31,294</u>	<u>\$2,080</u>

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%.	<u>\$ 300,000</u>
\$1,310,679 Drawdown for the Water Treatment Plant, issued in 2011. No set payment schedule, interest at .5 to 2.5%.	915,000
\$2,369,087 Drawdown for the Water Treatment Plant, issued in 2013. No set payment schedule.	2,249,087
\$735,000 Refunding Improvement bonds of 2013-B due in annual installments of \$40,000 to \$60,000 to May 2028 with interest of 1.0% to 2.75%.	<u>735,000</u>
Total Business-Type Activities	<u>\$4,199,087</u>

Revenue bond debt service requirements to maturity are as follows:

BUSINESS-TYPE ACTIVITIES		
Year Ending December 31	Special Assessment Payable	
	Principal	Interest
2014	\$ 170,000	\$ 24,603
2015	175,000	18,504
2016	75,000	14,380
2017	40,000	13,193
2018	45,000	12,768
2019 - 2023	240,000	50,428
2024 - 2028	290,000	19,939
Totals	\$1,035,000	\$153,813

The Water Treatment Plant issuances do not have a set payment schedule.

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 Bell State Bank & 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, 2013, 2012 and 2011 were \$24,859, \$24,543, and \$22,249, 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 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.

CITY OF HILLSBORO

Notes to the Financial Statements – Continued

As of December 31, 2013, there were two Community Development Block Grants outstanding, with an aggregate principal amount payable of \$235,831.

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 \$1,552,413 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, 2013:

Fund Name	Balance
Governmental Funds	
<u>Nonmajor Funds:</u>	
Social Security	\$(4,750)
Armory Operations	(355)
Recreation District	(337)

CITY OF HILLSBORO
Hillsboro, North Dakota

BUDGETARY COMPARISON SCHEDULE - MODIFIED CASH BASIS
GENERAL FUND

For the Year Ended December 31, 2013

	Original Budget	Final Budget	Actual	Variance with Final Budget
<u>Revenues:</u>				
Taxes	\$ 98,600	\$ 101,175	\$ 101,175	\$ -
Licenses, Permits and Fees	35,693	38,318	38,318	-
Intergovernmental	149,600	172,711	172,711	-
Fines, Forfeitures and Penalties	150	180	180	-
Interest	500	750	750	-
Miscellaneous	25,245	36,800	36,800	-
Total Revenues	\$ 309,788	\$ 349,934	\$ 349,934	\$ -
<u>Expenditures:</u>				
Current:				
General Government	\$ 147,480	\$ 159,130	\$ 159,130	\$ -
Public Safety	170,000	192,350	192,343	7
Culture and Recreation	65,000	78,900	80,744	(1,844)
Other	5,000	5,000	4,428	572
Total Expenditures	\$ 387,480	\$ 435,380	\$ 436,645	\$ (1,265)
Excess (Deficiency) of Revenues Over Expenditures	\$ (77,692)	\$ (85,446)	\$ (86,711)	\$ (1,265)
<u>Other Financing Sources (Uses):</u>				
Transfers In	\$ 100,000	\$ 100,000	\$ 124,000	\$ 24,000
Net Change in Fund Balances	\$ 22,308	\$ 14,554	\$ 37,289	\$ 22,735
Fund Balances - January 1	\$ 140,680	\$ 140,680	\$ 140,680	\$ -
Fund Balances - December 31	\$ 162,988	\$ 155,234	\$ 177,969	\$ 22,735

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, 2013

	Original Budget	Final Budget	Actual	Variance with Final Budget
<u>Revenues:</u>				
Intergovernmental	\$ 149,000	\$ 188,789	\$ 188,790	\$ 1
Miscellaneous Revenue	500	385	385	-
Total Revenues	\$ 149,500	\$ 189,174	\$ 189,175	\$ 1
<u>Expenditures:</u>				
Current:				
Public Works	\$ 239,685	\$ 303,061	\$ 236,375	\$ 66,686
Excess (Deficiency) of Revenues Over Expenditures	\$ (90,185)	\$ (113,887)	\$ (113,887)	\$ -
<u>Other Financing Sources (Uses):</u>				
Transfers In	\$ 85,000	\$ 85,000	\$ 85,000	\$ -
Transfers Out	(5,000)	(5,000)	(5,000)	-
Total Other Financing Sources and Uses	\$ 80,000	\$ 80,000	\$ 80,000	\$ -
Net Change in Fund Balances	\$ (10,185)	\$ (33,887)	\$ (33,887)	\$ -
Fund Balances - January 1	\$ 187,663	\$ 187,663	\$ 187,663	\$ -
Fund Balances - December 31	\$ 177,478	\$ 153,776	\$ 153,776	\$ -

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 Years Ended December 31, 2013

	Original Budget	Final Budget	Actual	Variance with Final Budget
<u>Revenues:</u>				
Taxes	\$ 250,000	\$ 361,161	\$ 361,161	\$ -
Interest income	1,000	294	294	-
Total Revenues	<u>\$ 251,000</u>	<u>\$ 361,455</u>	<u>\$ 361,455</u>	<u>\$ -</u>
<u>Expenditures:</u>				
Current:				
Economic Development	\$ 191,000	\$ 217,106	\$ 217,106	\$ -
Excess (Deficiency) of Revenues Over Expenditures	<u>\$ 60,000</u>	<u>\$ 144,349</u>	<u>\$ 144,349</u>	<u>\$ -</u>
<u>Other Financing Sources (Uses):</u>				
Transfers Out	\$ (42,000)	\$ (62,000)	\$ (62,000)	\$ -
Net Change in Fund Balances	<u>\$ 18,000</u>	<u>\$ 82,349</u>	<u>\$ 82,349</u>	<u>\$ -</u>
Fund Balances - January 1	<u>\$ 380,593</u>	<u>\$ 380,593</u>	<u>\$ 380,593</u>	<u>\$ -</u>
Fund Balances - December 31	<u><u>\$ 398,593</u></u>	<u><u>\$ 462,942</u></u>	<u><u>\$ 462,942</u></u>	<u><u>\$ -</u></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, 2013

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 2013, City of Hillsboro had the following fund expenditures in excess of budgeted amounts:

	Budget	Actual	Excess
Special Revenue Fund:			
General Fund	\$435,379	\$436,645	\$ 1,266
Capital Project Funds	2,000	52,000	50,000

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

CITY OF HILLSBORO
Hillsboro, North Dakota

SCHEDULE OF FUND ACTIVITY
ARISING FROM CASH TRANSACTIONS-Cash Amounts by Fund
For the Year Ended December 31, 2013

	Balance 1-1-13	Receipts	Transfers In	Debt Proceeds	Transfers Out	Disbursements	Balance 12-31-13
Major Governmental Funds:							
General Fund	\$ 140,679.79	\$ 349,933.57	\$ 124,000.00	\$ -	\$ -	\$ 436,644.91	\$ 177,968.45
Special Revenue Funds							
Highway Tax/Streets	\$ 187,662.99	\$ 189,174.19	\$ 85,000.00	-	\$ 5,000.00	\$ 303,061.49	\$ 153,775.69
City Sales Tax Fund	380,593.39	361,454.03	-	-	62,000.00	217,105.68	462,941.74
Total Major Special Revenue Funds	\$ 568,256.38	\$ 550,628.22	\$ 85,000.00	\$ -	\$ 67,000.00	\$ 520,167.17	\$ 616,717.43
Capital Project Funds							
Capital Projects	\$ 64,959.71	\$ 36.59	\$ -	\$ -	\$ 1,800.00	\$ 2,000.00	\$ 61,196.30
2008 Hwy 200 Project	(139,435.32)	-	110,688.32	28,747.00	-	-	-
Equipment	60,000.00	-	20,000.00	-	-	50,000.00	30,000.00
Total Major Capital Project Funds	\$ (14,475.61)	\$ 36.59	\$ 130,688.32	\$ 28,747.00	\$ 1,800.00	\$ 52,000.00	\$ 91,196.30
Debt Service Funds							
Riverbend Debt Service	\$ 160,726.92	\$ 93,437.37	\$ -	\$ -	\$ -	\$ 92,480.25	\$ 161,684.04
Project 2006 Water Main	86,490.28	105,934.04	-	-	-	102,292.50	90,131.82
Highway 200 Debt Service	228,706.95	148,890.86	20,000.00	-	110,688.32	109,466.57	177,442.92
2007 Streets Debt Service	198,717.65	324,056.79	-	-	231,363.75	20,907.59	270,503.10
Prairieview Debt Service	(243,169.41)	65,543.69	-	-	106,082.50	17,670.19	(301,378.41)
Kingman Sewer	-	67,694.42	-	-	-	15,797.50	51,896.92
Advanced Refunding	-	3,470.86	337,446.25	3,023,009.39	-	3,304,446.25	59,480.25
Total Major Debt Service Funds	\$ 431,472.39	\$ 809,028.03	\$ 357,446.25	\$ 3,023,009.39	\$ 448,134.57	\$ 3,663,060.85	\$ 509,760.64
Total Major Governmental Funds	\$ 1,125,932.95	\$ 1,709,626.41	\$ 697,134.57	\$ 3,051,756.39	\$ 516,934.57	\$ 4,671,872.93	\$ 1,395,642.82
Nonmajor Governmental Funds:							
Special Revenue Funds:							
Social Security	\$ (97.59)	\$ 30,454.97	\$ -	\$ -	\$ -	\$ 35,107.23	\$ (4,749.85)
City's Share of Specials	3,661.87	26,382.12	-	-	-	23,614.22	6,429.77
Emergency	33,670.52	9.84	-	-	-	-	33,680.36
Planning and Zoning	234.28	682.84	-	-	-	740.00	177.12
Cemetery	2,981.13	11,944.91	3,800.00	-	-	11,803.90	6,922.14
Armory Operations	5,948.80	2,410.00	11,000.00	-	-	19,713.67	(354.87)
Main Street Community Center	17,934.30	900.00	5,000.00	-	-	11,200.00	12,634.30
Forestry	3,231.97	1,342.40	-	-	-	1,487.25	3,087.12
CDLF - Wholesale Foods	231.44	18,987.48	-	-	-	18,182.04	1,036.88
Mosquito Control	62,313.56	15,441.53	-	-	-	1,651.38	76,103.71
Recreation District	3,241.94	6,120.44	-	-	-	9,700.00	(337.62)
Total Special Revenue Funds	\$ 133,352.22	\$ 114,676.53	\$ 19,800.00	\$ -	\$ -	\$ 133,199.69	\$ 134,629.06
Total Nonmajor Gov't Funds	\$ 133,352.22	\$ 114,676.53	\$ 19,800.00	\$ -	\$ -	\$ 133,199.69	\$ 134,629.06
Total Governmental Funds	\$ 1,259,285.17	\$ 1,824,302.94	\$ 716,934.57	\$ 3,051,756.39	\$ 516,934.57	\$ 4,805,072.62	\$ 1,530,271.88
Major Enterprise Funds:							
Water Funds							
Water Projects	\$ 156,826.09	\$ 266.58	\$ -	\$ -	\$ -	\$ 94,948.80	\$ 62,143.87
Regional Water Treatment Plant	(2,023,845.52)	2,800,114.40	-	2,369,087.00	-	3,710,622.51	(565,266.63)
Water Department	519,685.25	496,380.27	-	-	5,000.00	418,637.21	592,428.31
Total Water Funds	\$ (1,347,334.18)	\$ 3,296,761.25	\$ -	\$ 2,369,087.00	\$ 5,000.00	\$ 4,224,208.52	\$ 89,305.55

Continued on next page....

CITY OF HILLSBORO
Hillsboro, North Dakota

SCHEDULE OF FUND ACTIVITY
ARISING FROM CASH TRANSACTIONS-Cash Amounts by Fund
For the Year Ended December 31, 2013

	Balance 1-1-13	Receipts	Transfers In	Debt Proceeds	Transfers Out	Disbursements	Balance 12-31-13
CONTINUED....							
Major Enterprise Funds (Major):							
<u>Electric Funds</u>							
Generation Project - Debt	\$ 78,514.03	\$ 125,266.63	\$ 138,000.00	\$ -	\$ 138,000.00	\$ 138,119.84	\$ 65,660.82
Electric Department	711,693.61	2,141,878.54	-	-	190,000.00	2,017,449.98	646,122.17
Meter Deposits	43,106.67	60.05	-	-	-	-	43,166.72
Total Electric Funds	\$ 833,314.31	\$ 2,267,205.22	\$ 138,000.00	\$ -	\$ 328,000.00	\$ 2,155,569.82	\$ 754,949.71
<u>Sewer Funds</u>							
Kingman Addition Sewer Constr.	\$ 188,274.54	\$ -	\$ -	\$ -	\$ -	\$ 99,286.47	\$ 88,988.07
Sewer Department	120,092.92	108,609.19	-	-	5,000.00	72,872.35	150,829.76
Total Sewer Funds	\$ 308,367.46	\$ 108,609.19	\$ -	\$ -	\$ 5,000.00	\$ 172,158.82	\$ 239,817.83
<u>Sanitation</u>							
Sanitation Department	\$ 35,868.73	\$ 194,322.09	\$ -	\$ -	\$ -	\$ 196,524.16	\$ 33,666.66
Total Major Enterprise Funds	\$ (169,783.68)	\$ 5,866,897.75	\$ 138,000.00	\$ 2,369,087.00	\$ 338,000.00	\$ 6,748,461.32	\$ 1,117,739.75
<u>Agency Funds</u>							
Airport	\$ -	\$ 9,398.97	\$ -	\$ -	\$ -	\$ 9,398.97	\$ -
Total Reporting Entity	\$ 1,089,501.49	\$ 7,700,599.66	\$ 854,934.57	\$ 5,420,843.39	\$ 854,934.57	\$ 11,562,932.91	\$ 2,648,011.63

CITY OF HILLSBORO
Hillsboro, North Dakota

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Year Ended December 31, 2013

Federal Grantor/ Pass-Through Grantor/ Program Title	Federal CFDA Number		Federal Expenditures
<u>DEPARTMENT OF DEFENSE</u>			
<u>Passed through Trill Rural Water District:</u> North Dakota Environmental Infrastructure (Section 594) - ARRA	12.118	*	<u>\$ 2,782,035</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, 2013. 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 position 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

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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 INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON
COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

Independent Auditor's Report

City Commission
City of Hillsboro
Hillsboro, North Dakota

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of the City of Hillsboro as of and for the year ended December 31, 2013, and the related notes to the financial statements, which collectively comprise the City of Hillsboro's basic financial statements, and have issued our report thereon dated August 22, 2014.

Internal Control Over Financial Reporting

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

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying *schedule of findings and questioned costs*, we identified certain deficiencies in internal control 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 a 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* to be material weaknesses [2013-01 and 2013-02].

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the 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*.

CITY OF HILLSBORO

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 – Material Weaknesses Identified - Continued

The City of Hillsboro's Response to Findings

The City of Hillsboro's responses to the findings identified in our audit are described in the accompanying *schedule of findings and questioned costs*. The City of Hillsboro's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Robert R. Peterson
State Auditor

Fargo, North Dakota
August 22, 2014

STATE AUDITOR

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STATE CAPITOL
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BISMARCK, NORTH DAKOTA 58505

REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM; REPORT ON INTERNAL CONTROL OVER COMPLIANCE; AND REPORT ON THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS REQUIRED BY OMB CIRCULAR A-133

Independent Auditor's Report

Board of County Commissioners
City of Hillsboro
Hillsboro, North Dakota

Report on Compliance for Each Major Federal Program

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, 2013. The 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.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for the City of Hillsboro's major federal program based on our audit of the types of compliance requirements referred to above. 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, *Audits of States, Local Governments, and Non-Profit Organizations*. 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 the 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 on compliance for the major federal program. However, our audit does not provide a legal determination of the City of Hillsboro's compliance.

Opinion on Each Major Federal Program

In our opinion, the City of Hillsboro complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended December 31, 2013.

CITY OF HILLSBORO

Report on Compliance for Each Major Federal Program; Report on Internal Control Over Compliance; and
Report on Schedule of Expenditures of Federal Awards Required by OMB Circular A-133 - Continued

Report on Internal Control Over Compliance

Management of the City of Hillsboro is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the City of Hillsboro's internal control over compliance with the types of requirements that could have a direct and material effect on the major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the major federal program 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. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

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 material weakness or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Report on Schedule of Expenditures of Federal Awards Required by OMB Circular A-133

We have audited the financial statements of the City of Hillsboro as of and for the year ended December 31, 2013, and have issued our report thereon dated August 22, 2014, which contained unmodified opinions on those financial statements for the major governmental funds and aggregate remaining fund information, and modified (adverse) opinions for major business-type funds, governmental activities, and business type activities. Our audit was conducted for the purpose of forming opinions on the financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the financial statements as a whole.



Robert R. Peterson
State Auditor

Fargo, North Dakota
August 22, 2014

CITY OF HILLSBORO
Hillsboro, North Dakota

SCHEDULE OF FINDINGS AND RESPONSES
For the Year Ended December 31, 2013

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	Unmodified on modified cash basis
Major Business-Type Funds	Adverse
Aggregate Remaining Fund Information	Unmodified on modified cash basis

Internal Control over financial reporting:

Material weakness(es) identified?	<u> X </u> Yes	<u> </u> None noted
Significant deficiencies identified?	<u> </u> Yes	<u> X </u> None noted
Noncompliance material to financial statements noted?	<u> </u> Yes	<u> X </u> None noted

Federal Awards

Internal control over major programs:

Material weakness identified?	<u> </u> Yes	<u> X </u> None noted
Significant deficiencies identified not considered to be material weaknesses?	<u> </u> Yes	<u> X </u> None noted
Type of auditor's report issued on compliance for major programs?	Unmodified	
Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?	<u> </u> Yes	<u> X </u> None noted

Identification of Major Programs:

CFDA Numbers	Name of Federal Program
12.118	North Dakota Environmental Infrastructure (Section 594) – 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

2013-01 - 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.

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 it is cost effective to establish capital asset records at this time according to Auditor recommendation.

2013-02 - 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. It 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 Findings and Questioned Costs

No matters were reported.