



City of Hillsboro
Hillsboro, North Dakota

Audit Report

For the Year Ended December 31, 2016

JOSHUA C. GALLION
STATE AUDITOR

Office of the State Auditor
Division of Local Government

CITY OF HILLSBORO
Hillsboro, North Dakota

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CITY OF HILLSBORO
Hillsboro, North Dakota

December 31, 2016

CITY OFFICIALS

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

INDEPENDENT AUDITOR'S 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, 2016, 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, 2016, 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, 2016 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 and notes to the required supplementary information* on pages 24-28 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.

CITY OF HILLSBORO

Independent Auditor's Report - Continued

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 *Title 2 U.S. Code of Federal Regulations (CFR) Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, 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 February 8, 2018, 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.

/s/

Joshua C. Gallion
State Auditor

Fargo, North Dakota
February 8, 2018

CITY OF HILLSBORO
Hillsboro, North Dakota

STATEMENT OF NET POSITION - MODIFIED CASH BASIS
December 31, 2016

	Primary Government		
	Governmental Activities	Business-Type Activities	Total
ASSETS:			
Cash	\$ 1,537,934	\$ 388,256	\$ 1,926,190
Investments	324,504	941,830	1,266,334
Total Assets	\$ 1,862,438	\$ 1,330,086	\$ 3,192,524
LIABILITIES:			
Benefits Payable	\$ 1,930	\$ 215	\$ 2,145
Long-Term Liabilities:			
Due Within One Year:			
Special Assessment Bonds Payable	540,000	-	540,000
Revenue Bonds Payable	-	120,000	120,000
State Revolving Loan Fund Payable	87,000	-	87,000
Due After One Year:			
Special Assessment Bonds Payable	2,880,000	-	2,880,000
Revenue Bonds Payable	-	2,595,000	2,595,000
State Revolving Loan Fund Payable	663,000	-	663,000
Total Liabilities	\$ 4,171,930	\$ 2,715,215	\$ 6,887,145
NET POSITION:			
Restricted for:			
Public Works	\$ 172,988	\$ -	\$ 172,988
Economic/Job Development	530,784	-	530,784
Capital Improvements	115,521	-	115,521
Emergency	33,710	-	33,710
General Government	30,340	-	30,340
Unrestricted	(3,192,835)	(1,385,129)	(4,577,964)
Total Net Position	\$ (2,309,492)	\$ (1,385,129)	\$ (3,694,621)

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, 2016

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	\$ 373,947	\$ 26,258	\$ -	\$ (347,689)	\$ -	\$ (347,689)
Public Safety	135,267	-	-	(135,267)	-	(135,267)
Public Works/Infrastructure	184,709	5,330	93,578	(85,801)	-	(85,801)
Culture and Recreation	109,511	19,145	-	(90,366)	-	(90,366)
Economic Development	41,637	-	-	(41,637)	-	(41,637)
Miscellaneous	10,808	-	-	(10,808)	-	(10,808)
Capital Outlay	132,947	-	-	(132,947)	-	(132,947)
Interest & Fees on Long-Term Debt	115,744	-	-	(115,744)	-	(115,744)
Total Governmental Activities	\$ 1,104,570	\$ 50,733	\$ 93,578	\$ (960,259)	\$ -	\$ (960,259)
<u>Business-Type Activities:</u>						
Water Funds	\$ 515,628	\$ 601,213	\$ -	\$ -	\$ 85,585	\$ 85,585
Electric Funds	1,916,157	2,210,454	-	-	294,297	294,297
Sewer Funds	86,932	110,763	-	-	23,831	23,831
Sanitation	234,340	236,853	-	-	2,513	2,513
Total Business-Type Activities	\$ 2,753,057	\$ 3,159,283	\$ -	\$ -	\$ 406,226	\$ 406,226
Total Primary Government	\$ 3,857,627	\$ 3,210,016	\$ 93,578	\$ (960,259)	\$ 406,226	\$ (554,033)
<u>General Revenues:</u>						
Taxes:						
Property taxes levied for general purposes	\$ 177,776	\$ -	\$ 177,776			
Property taxes levied for special purposes	103,011	-	103,011			
Property taxes levied for debt service	586,109	-	586,109			
Sales taxes	359,931	-	359,931			
State Aid Distribution	125,687	-	125,687			
Interest Income	1,661	1,548	3,209			
Miscellaneous Revenue	94,498	216,600	311,098			
Transfers	95,000	(95,000)	-			
Total General Revenues and Transfers	\$ 1,543,673	\$ 123,148	\$ 1,666,821			
Change in Net Position	\$ 583,414	\$ 529,374	\$ 1,112,788			
Net Position - January 1	\$ (2,892,906)	\$ (1,914,503)	\$ (4,807,409)			
Net Position - December 31	\$ (2,309,492)	\$ (1,385,129)	\$ (3,694,621)			

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
December 31, 2016

	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	\$ 132,394	\$ 78,493	\$ 354,935	\$ 97,122	\$ 722,511	\$ 152,479	\$ 1,537,934
Investments	-	-	175,849	18,399	123,690	6,566	324,504
Due from Other Funds	3,537	-	-	-	-	-	3,537
Total Assets	\$ 135,931	\$ 78,493	\$ 530,784	\$ 115,521	\$ 846,201	\$ 159,045	\$ 1,865,975
LIABILITIES AND FUND BALANCES							
Liabilities:							
Benefits Payable	\$ 1,430	\$ -	\$ -	\$ -	\$ -	\$ 500	\$ 1,930
Due to Other Funds	-	-	-	-	-	3,537	3,537
Total Liabilities	\$ 1,430	\$ -	\$ -	\$ -	\$ -	\$ 4,037	\$ 5,467
Fund Balances:							
Committed:							
General Government	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 8,440	\$ 8,440
Restricted:							
Debt Service	-	-	-	-	846,201	-	846,201
Public Works	-	78,493	-	-	-	94,495	172,988
Economic Development	-	-	530,784	-	-	-	530,784
Capital Improvements	-	-	-	115,521	-	-	115,521
Emergency	-	-	-	-	-	33,710	33,710
General Government	-	-	-	-	-	21,900	21,900
Unassigned							
General Fund	134,501	-	-	-	-	-	134,501
Negative Fund Balances	-	-	-	-	-	(3,537)	(3,537)
Total Fund Balances	\$ 134,501	\$ 78,493	\$ 530,784	\$ 115,521	\$ 846,201	\$ 155,008	\$ 1,860,508
Total Liabilities and Fund Balances	\$ 135,931	\$ 78,493	\$ 530,784	\$ 115,521	\$ 846,201	\$ 159,045	\$ 1,865,975

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, 2016

Total *Fund Balances* for Governmental Funds \$ 1,860,508

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, 2016 are:

Special Assessment Bonds Payable	\$ (3,420,000)	
Loans Payable	<u>(750,000)</u>	<u>(4,170,000)</u>
Total Net Position of Governmental Activities		<u>\$ (2,309,492)</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, 2016

	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	\$ 177,776	\$ -	\$ -	\$ -	\$ 89,521	\$ 13,490	\$ 280,787
Sales Taxes	-	-	359,931	-	-	-	359,931
Special Assessments	-	-	-	-	586,109	-	586,109
Licenses, Permits and Fees	45,403	-	-	-	-	-	45,403
Intergovernmental	125,687	93,578	-	-	-	-	219,265
Charges for Services	-	-	-	-	-	5,330	5,330
Interest Income	1,135	-	294	37	185	10	1,661
Miscellaneous	19,174	2,302	-	-	25,163	47,859	94,498
Total Revenues	\$ 369,175	\$ 95,880	\$ 360,225	\$ 37	\$ 700,978	\$ 66,689	\$ 1,592,984
Expenditures:							
Current:							
General Government	\$ 204,055	\$ -	\$ -	\$ -	\$ -	\$ 169,892	\$ 373,947
Public Safety	135,267	-	-	-	-	-	135,267
Public Works	-	166,579	-	-	-	18,130	184,709
Culture and Recreation	109,511	-	-	-	-	-	109,511
Economic Development	-	-	23,086	-	-	18,551	41,637
Other	10,808	-	-	-	-	-	10,808
Capital Outlay	-	-	-	132,947	-	-	132,947
Dept Service:							
Principal	-	15,984	-	-	635,000	-	650,984
Interest	-	703	-	-	83,498	-	84,201
Fees	-	-	-	-	31,543	-	31,543
Total Expenditures	\$ 459,641	\$ 183,266	\$ 23,086	\$ 132,947	\$ 750,041	\$ 206,573	\$ 1,755,554
Excess (Deficiency) of Revenues Over Expenditures	\$ (90,466)	\$ (87,386)	\$ 337,139	\$ (132,910)	\$ (49,063)	\$ (139,884)	\$ (162,570)
Other Financing Sources (Uses):							
Transfers In	\$ 85,141	\$ 70,000	\$ -	\$ 135,000	\$ 331,293	\$ 190,766	\$ 812,200
Transfers Out	(31,766)	(5,000)	(490,293)	-	(185,000)	(5,141)	(717,200)
Total Other Financing Sources and Uses	\$ 53,375	\$ 65,000	\$ (490,293)	\$ 135,000	\$ 146,293	\$ 185,625	\$ 95,000
Net Change in Fund Balances	\$ (37,091)	\$ (22,386)	\$ (153,154)	\$ 2,090	\$ 97,230	\$ 45,741	\$ (67,570)
Fund Balances - January 1	\$ 171,592	\$ 100,879	\$ 683,938	\$ 113,431	\$ 748,971	\$ 109,267	\$ 1,928,078
Fund Balance - December 31	\$ 134,501	\$ 78,493	\$ 530,784	\$ 115,521	\$ 846,201	\$ 155,008	\$ 1,860,508

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, 2016

Net Change in *Fund Balances* - Total Governmental Funds \$ (67,570)

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.

Repayment of Special Assessment Bonds	\$ 530,000	
Repayment of State Revolving Fund Loans	105,000	
Repayment of Capital Leases	15,984	650,984
	<hr/>	<hr/>

Change in Net Position of Governmental Activities \$ 583,414

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, 2016

	Business-Type Activities - Enterprise Funds				
	Water Funds	Electric Funds	Sewer Funds	Sanitation Fund	Total Enterprise Funds
<u>ASSETS</u>					
Cash and Cash Equivalents	\$ 201,366	\$ 20,655	\$ 102,032	\$ 64,203	\$ 388,256
Investments	303,920	587,649	50,261	-	941,830
Total Assets	\$ 505,286	\$ 608,304	\$ 152,293	\$ 64,203	\$ 1,330,086
<u>LIABILITIES</u>					
<u>Current Liabilities:</u>					
Benefits Payable	\$ -	\$ 215	\$ -	\$ -	\$ 215
Bonds Payable	120,000	-	-	-	120,000
Total Current Liabilities	\$ 120,000	\$ 215	\$ -	\$ -	\$ 120,215
<u>Noncurrent Liabilities:</u>					
Bonds Payable	\$ 2,595,000	\$ -	\$ -	\$ -	\$ 2,595,000
Total Liabilities	\$ 2,715,000	\$ 215	\$ -	\$ -	\$ 2,715,215
<u>NET POSITION</u>					
Unrestricted	\$ (2,209,714)	\$ 608,089	\$ 152,293	\$ 64,203	\$ (1,385,129)
Total Net Position	\$ (2,209,714)	\$ 608,089	\$ 152,293	\$ 64,203	\$ (1,385,129)

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, 2016

	Business-Type Activities - Enterprise Funds				
	Water Funds	Electric Funds	Sewer Funds	Sanitation Fund	Total Enterprise Funds
<u>Operating Revenues:</u>					
Charges for Sales and Services	\$ 601,213	\$ 2,210,454	\$ 110,763	\$ 236,853	\$ 3,159,283
<u>Operating Expenses:</u>					
Salaries and Benefits	\$ 112,957	\$ 105,982	\$ 29,823	\$ -	\$ 248,762
Professional Services (Legal, Engineering, etc)	42,785	45,099	7,002	205,757	300,643
Maintenance & Supplies	165,641	132,087	49,377	6,904	354,009
Recycling Costs	-	-	-	12,756	12,756
Raw Water Costs	54,723	-	-	-	54,723
Purchased Power Costs	-	1,626,603	-	-	1,626,603
Machinery and Equipment	630	630	630	8,605	10,495
Miscellaneous	-	4,211	100	318	4,629
Total Operating Disbursements	\$ 376,736	\$ 1,914,612	\$ 86,932	\$ 234,340	\$ 2,612,620
Operating Income (Loss)	\$ 224,477	\$ 295,842	\$ 23,831	\$ 2,513	\$ 546,663
<u>Nonoperating Revenues (Expenses):</u>					
Interest on Investments	\$ 554	\$ 860	\$ 134	\$ -	\$ 1,548
Miscellaneous Receipts	181,497	6,937	27,551	615	216,600
Retirement of Debt - Interest	(50,950)	(788)	-	-	(51,738)
Retirement of Debt - Fees	(15,350)	(757)	-	-	(16,107)
Operating Lease Payments	(72,592)	-	-	-	(72,592)
Total Nonoperating Revenues (Expenses)	\$ 43,159	\$ 6,252	\$ 27,685	\$ 615	\$ 77,711
Income Before Transfers	\$ 267,636	\$ 302,094	\$ 51,516	\$ 3,128	\$ 624,374
Transfers In	\$ 185,000	\$ -	\$ -	\$ -	\$ 185,000
Transfers Out	(62,500)	(212,500)	(5,000)	-	(280,000)
Total Transfers	\$ 122,500	\$ (212,500)	\$ (5,000)	\$ -	\$ (95,000)
Change in Net Position	\$ 390,136	\$ 89,594	\$ 46,516	\$ 3,128	\$ 529,374
Total Net Position - January 1	\$ (2,599,850)	\$ 518,495	\$ 105,777	\$ 61,075	\$ (1,914,503)
Total Net Position - December 31	\$ (2,209,714)	\$ 608,089	\$ 152,293	\$ 64,203	\$ (1,385,129)

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, 2016

	Business-Type Activities - Enterprise Funds				
	Water Funds	Electric Funds	Sewer Funds	Sanitation Fund	Total Enterprise Funds
<u>Cash Flows from Operating Activities:</u>					
Receipts from Customers and Users	\$ 601,213	\$ 2,210,454	\$ 110,763	\$ 236,853	\$ 3,159,283
Payments to Suppliers	(263,779)	(1,808,630)	(57,109)	(234,340)	(2,363,858)
Payments to Employees	(112,957)	(105,982)	(29,823)	-	(248,762)
Net Cash Provided (Used) by Operating Activities	<u>\$ 224,477</u>	<u>\$ 295,842</u>	<u>\$ 23,831</u>	<u>\$ 2,513</u>	<u>\$ 546,663</u>
<u>Cash Flows from Noncapital Financing Activities:</u>					
Miscellaneous Revenue (Expense)	\$ 181,497	\$ 6,937	\$ 27,551	\$ 615	\$ 216,600
Transfers from Other Funds	185,000	-	-	-	185,000
Transfers to Other Funds	(62,500)	(212,500)	(5,000)	-	(280,000)
Net Cash Provided (Used) by Noncapital Financing Activities	<u>\$ 303,997</u>	<u>\$ (205,563)</u>	<u>\$ 22,551</u>	<u>\$ 615</u>	<u>\$ 121,600</u>
<u>Cash Flows from Capital and Related Financing Activities:</u>					
Principal Paid on Capital Debt	\$ (355,000)	\$ (35,000)	\$ -	\$ -	\$ (390,000)
Operating Lease Payments	(72,592)	-	-	-	(72,592)
Interest & Fees Paid on Capital Debt	(66,300)	(1,545)	-	-	(67,845)
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>\$ (493,892)</u>	<u>\$ (36,545)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (530,437)</u>
<u>Cash Flows from Investing Activities:</u>					
Purchases, Sales & Maturities of Investments	\$ (358)	\$ (131,628)	\$ (17)	\$ -	\$ (132,003)
Interest Income	554	860	134	-	1,548
Net Cash Provided (Used) by Investing Activities	<u>\$ 196</u>	<u>\$ (130,768)</u>	<u>\$ 117</u>	<u>\$ -</u>	<u>\$ (130,455)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	<u>\$ 34,778</u>	<u>\$ (77,034)</u>	<u>\$ 46,499</u>	<u>\$ 3,128</u>	<u>\$ 7,371</u>
Cash and Cash Equivalents, January 1	<u>\$ 166,588</u>	<u>\$ 97,689</u>	<u>\$ 55,533</u>	<u>\$ 61,075</u>	<u>\$ 380,885</u>
Cash and Cash Equivalents, December 31	<u>\$ 201,366</u>	<u>\$ 20,655</u>	<u>\$ 102,032</u>	<u>\$ 64,203</u>	<u>\$ 388,256</u>
Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities					
Operating Income (Loss)	<u>\$ 224,477</u>	<u>\$ 295,842</u>	<u>\$ 23,831</u>	<u>\$ 2,513</u>	<u>\$ 546,663</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, 2016

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 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 items a) and 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 funds primarily utilize a “current financial resources measurement focus” within the confines of the modified cash basis of accounting, except that long term debt is reported. 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 resulting from cash transactions. Assets and liabilities are reported for cash transactions and also long-term debt (current and noncurrent) associated with those 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, and proprietary fund 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, 2016 consist of certificates of deposit stated at cost with maturities in excess of three months.

E. Fund Balances / Net Position

Fund Balance

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.

Major Special Revenue Fund Purposes & Revenue Sources

Purposes and major revenue sources of the major special revenue funds (city sales tax fund, and highway tax fund) are disclosed in more detail in Note 1B in the discussion of major funds.

CITY OF HILLSBORO

Notes to the Financial Statements – Continued

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, 2016.

Restricted Fund Balances – consist of the following items at December 31, 2016

Restricted fund balances are shown by primary function on the balance sheet for debt service, public works, sales tax/economic development, capital improvements, emergency, and general government (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 reported in the armory operations and CDLF wholesale food funds.

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.

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, economic/job development, emergency, and general government.

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

F. 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.

NOTE 2: 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.

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, 2016, the city's carrying amount of deposits was \$3,192,778 and the bank balances totaled \$3,243,283. Of the bank balances, \$883,492 was covered by Federal Depository Insurance. The remaining balances were collateralized with securities held by the pledging financial institution's agent in the government's name.

CITY OF HILLSBORO

Notes to the Financial Statements – Continued

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, 2016, 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 3: 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.

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 4: DUE TO / FROM OTHER FUNDS

The composition of due to and due from other funds as of December 31, 2016 are as follows:

	Due To	Due From
Governmental Funds		
Major Fund		
General Fund	\$ -	\$ 3,537
Nonmajor Fund		
Recreation District	3,537	-
Total	\$ 3,537	\$ 3,537

The composition of due to and due from other funds is related to negative cash fund balances in the social security fund and the recreation district fund covered by the general fund.

CITY OF HILLSBORO

Notes to the Financial Statements – Continued

NOTE 5: 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, 2016:

Fund	Transfers In	Transfers Out
Governmental Funds		
<u>Major Funds</u>		
General Fund	\$ 85,141	\$ 31,766
Highway Tax/Streets	70,000	5,000
City Sales Tax Fund	-	490,293
Equipment	20,000	-
AMR Meter Replacement	115,000	-
<u>Debt Service Funds</u>		
Kingman Sewer	35,000	-
City Debt Retirement	296,293	185,000
<u>Nonmajor Funds</u>		
Social Security	5,216	1,815
City Share of Specials	115,000	-
Planning and Zoning	722	33
Cemetery	4,000	-
Armory Operations	20,000	-
Main Street Community Center	45,000	-
Forestry	828	3,293
Business-Type Funds		
<u>Major Funds</u>		
Water Funds	185,000	62,500
Electric Funds	-	212,500
Sewer Funds	-	5,000
Total Transfers	\$ 997,200	\$ 997,200

NOTE 6: LONG-TERM LIABILITIES

During the years ended December 31, 2016, the following changes occurred in long-term liabilities of the city:

Governmental Activities

Governmental Activities	Balance January 1	Increases	Decreases	Balance December 31	Due Within One Year
Special Assessment Bonds	\$ 3,950,000	\$ -	\$ 530,000	\$ 3,420,000	\$ 540,000
Revolving Loan Payable	855,000	-	105,000	750,000	87,000
Capital Lease Payable	15,984	-	15,984	-	-
Total Governmental Activities	\$ 4,820,984	\$ -	\$ 650,984	\$ 4,170,000	\$ 627,000

Special Assessment Bonds

\$550,000 Special Assessment Bonds of 2015 due in annual installments of \$55,000 to \$65,000 through May 1, 2024; interest at 4.25% to 4.75%. \$ 495,000

\$605,000 Special Assessment Bonds of 2015 due in annual installments of \$85,000 to \$90,000 through May 2019; interest at 1.5%. 265,000

CITY OF HILLSBORO

Notes to the Financial Statements – Continued

Special Assessment Bonds - Continued

\$3,075,000 Refunding Improvement Bonds of 2015 due in annual installments of \$335,000 to \$350,000 through May 2022; interest at 1.15% to 2.1% \$ 2,045,000

\$735,000 Refunding Improvement bonds of 2015-B due in annual installments of \$40,000 to \$60,000 to May 2028 with interest of 1.0% to 2.75%. 615,000

Total Special Assessment Bonds \$ 3,420,000

State Revolving Fund Loans

\$1,150,563 Drinking Water Revolving Improvement Bonds of 2007 due in annual installments of \$87,000 to \$95,000 through September 2021; interest at 2.5%. \$ 455,000

\$127,489 Drawdown for the wastewater treatment project, issued in 2010. No set payment schedule, interest at 2.5% with a .5% administrative fee. 90,000

\$299,413 Drawdown for the water treatment project, issued in 2011. No set payment schedule, interest at 2.5% with a .5% administrative fee. 205,000

Total State Revolving Fund Loans \$ 750,000

Total Governmental Activities \$ 4,170,000

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 Assess. Payable		SRF Loan Payable	
	Principal	Interest	Principal	Interest
2017	\$ 540,000	\$ 56,042	\$ 107,000	\$ 18,750
2018	535,000	49,064	109,000	16,075
2019	535,000	41,275	111,000	13,350
2020	450,000	33,278	113,000	10,575
2021	445,000	25,075	95,000	2,375
2022 - 2026	795,000	43,281	100,000	21,875
2027 - 2031	120,000	3,300	115,000	6,875
Totals	\$ 3,420,000	\$ 251,315	\$ 750,000	\$ 89,875

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

Business-Type Activities	Balance January 1	Increases	Decreases	Balance December 31	Due Within One Year
Water Fund	\$ 3,070,000	\$ -	\$ 355,000	\$ 2,715,000	\$ 120,000
Electric Fund	35,000	-	35,000	-	-
Total Business-Type Activities	\$ 3,105,000	\$ -	\$ 390,000	\$ 2,715,000	\$ 120,000

CITY OF HILLSBORO

Notes to the Financial Statements – Continued

Business-Type Activities:

\$1,310,679 Drawdown for the Water Treatment Plant, issued in 2011. No set payment schedule, interest at 2.5% with a .5% administrative fee.	\$ 755,000
\$2,609,722 Drawdown for the Water Treatment Plant, issued in 2015. No set payment schedule.	<u>\$ 1,960,000</u>
Total Business-Type Activities	<u>\$ 2,715,000</u>

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

NOTE 7: PENSION PLAN

The City of Hillsboro provides a retirement plan for City employees. The profit-sharing plan is a 401a 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 Bank. 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, 2016, 2015 and 2014 were \$31,199, \$25,462, and \$25,169, respectively.

NOTE 8: 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.

As of December 31, 2016, there were two Community Development Block Grants outstanding, with an aggregate principal amount payable of \$142,970.

NOTE 9: 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.

CITY OF HILLSBORO

Notes to the Financial Statements – Continued

In 1986, state agencies and political subdivisions of the State of North Dakota joined together to form the North Dakota Insurance Reserve Fund (NDIRF), 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 NDIRF for its general liability, auto, and public assets insurance coverage. The coverage by NDIRF is limited to losses of two million dollars per occurrence for general liability and automobile coverage and \$1,406,782 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 \$2,000,000 for the city employees. The State Bonding Fund does not currently charge any premium for this coverage.

The City has worker's 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 10: FUND DEFICITS

The following funds were in a deficit position at December 31, 2016:

Fund Name	Balance
Governmental Funds	
<u>Nonmajor Funds:</u>	
Recreation District	\$ (3,537)

CITY OF HILLSBORO
Hillsboro, North Dakota

BUDGETARY COMPARISON SCHEDULE - MODIFIED CASH BASIS
GENERAL FUND
For the Year Ended December 31, 2016

	Original Budget	Final Budget	Actual	Variance with Final Budget
<u>Revenues:</u>				
Taxes	\$ 171,240	\$ 171,240	\$ 177,776	\$ 6,536
Licenses, Permits and Fees	42,960	42,960	45,403	2,443
Intergovernmental	183,000	183,000	125,687	(57,313)
Fines, Forfeitures and Penalties	150	150	-	(150)
Interest	1,000	1,000	1,135	135
Miscellaneous	34,000	34,000	19,174	(14,826)
Total Revenues	\$ 432,350	\$ 432,350	\$ 369,175	\$ (63,175)
<u>Expenditures:</u>				
Current:				
General Government	\$ 211,250	\$ 211,250	\$ 204,055	\$ 7,195
Public Safety	163,400	163,400	135,267	28,133
Culture and Recreation	104,100	104,100	109,511	(5,411)
Other	10,000	10,000	10,808	(808)
Total Expenditures	\$ 488,750	\$ 488,750	\$ 459,641	\$ 29,109
Excess (Deficiency) of Revenues Over Expenditures	\$ (56,400)	\$ (56,400)	\$ (90,466)	\$ (34,066)
<u>Other Financing Sources (Uses):</u>				
Transfers In	\$ 80,000	\$ 80,000	\$ 85,141	\$ 5,141
Transfers Out	(65,240)	(65,240)	(31,766)	33,474
Total Other Financing Sources and Uses	\$ 14,760	\$ 14,760	\$ 53,375	\$ 38,615
Net Change in Fund Balances	\$ (41,640)	\$ (41,640)	\$ (37,091)	\$ 4,549
Fund Balances - January 1	\$ 171,592	\$ 171,592	\$ 171,592	\$ -
Fund Balances - December 31	\$ 129,952	\$ 129,952	\$ 134,501	\$ 4,549

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, 2016

	Original Budget	Final Budget	Actual	Variance with Final Budget
<u>Revenues:</u>				
Intergovernmental	\$ 119,500	\$ 119,500	\$ 93,578	\$ (25,922)
Miscellaneous Revenue	500	500	2,302	1,802
Total Revenues	\$ 120,000	\$ 120,000	\$ 95,880	\$ (24,120)
<u>Expenditures:</u>				
Current:				
Public Works	\$ 209,887	\$ 209,887	\$ 166,579	\$ 43,308
Debt Service:				
Principal	15,984	15,984	15,984	-
Interest	703	703	703	-
Total Expenditures	\$ 226,574	\$ 226,574	\$ 183,266	\$ 43,308
Excess (Deficiency) of Revenues Over Expenditures	\$ (106,574)	\$ (106,574)	\$ (87,386)	\$ 19,188
<u>Other Financing Sources (Uses):</u>				
Transfers In	\$ 70,000	\$ 70,000	\$ 70,000	\$ -
Transfers Out	(5,000)	(5,000)	(5,000)	-
Total Other Financing Sources and Uses	\$ 65,000	\$ 65,000	\$ 65,000	\$ -
Net Change in Fund Balances	\$ (41,574)	\$ (41,574)	\$ (22,386)	\$ 19,188
Fund Balances - January 1	\$ 100,879	\$ 100,879	\$ 100,879	\$ -
Fund Balances - December 31	\$ 59,305	\$ 59,305	\$ 78,493	\$ 19,188

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, 2016

	Original Budget	Final Budget	Actual	Variance with Final Budget
<u>Revenues:</u>				
Taxes	\$ 370,000	\$ 370,000	\$ 359,931	\$ (10,069)
Interest income	400	400	294	(106)
Total Revenues	\$ 370,400	\$ 370,400	\$ 360,225	\$ (10,175)
<u>Expenditures:</u>				
Current:				
Economic Development	\$ 313,100	\$ 313,100	\$ 23,086	\$ 290,014
Excess (Deficiency) of Revenues Over Expenditures	\$ 57,300	\$ 57,300	\$ 337,139	\$ 279,839
<u>Other Financing Sources (Uses):</u>				
Transfers Out	\$ (124,000)	\$ (124,000)	\$ (490,293)	\$ (366,293)
Net Change in Fund Balances	\$ (66,700)	\$ (66,700)	\$ (153,154)	\$ (86,454)
Fund Balances - January 1	\$ 683,938	\$ 683,938	\$ 683,938	\$ -
Fund Balances - December 31	\$ 617,238	\$ 617,238	\$ 530,784	\$ (86,454)

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, 2016

NOTE 1: STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Budgetary Information:

The governing board adopts an annual budget on a basis consistent with GAAP, and state law as outlined in various sections of North Dakota Century Code (NDCC) Chapter 40-40 for the general fund, each special revenue fund and each debt service fund of the municipality. The city is required to present the adopted and final amended revenues and expenditures for each of these funds.

The following procedures are followed in establishing the budgetary data reflected in the financial statements:

- The city commission adopts an “appropriated budget” on the modified cash basis of accounting.
- The governing body of each municipality, annually or before September tenth, shall make an itemized statement known as the preliminary budget statement showing the amounts of money which, in the opinion of the governing body, will be required for the proper maintenance, expansion, or improvement of the municipality during the year (NDCC 40-40-04).
- The preliminary budget must include a detailed breakdown of the estimated revenues and appropriations requested for the ensuing year for the general fund, each special revenue fund, and each debt service fund of the municipality. The revenue and expenditure items for the preceding year and estimates of the revenue and expenditures for the current year must be included for each fund to assist in determining the estimated revenues and appropriation requested for the ensuing year. The budget must also include any transfers in or out and the beginning and ending fund balance for each of the funds. The budget must be prepared on the same basis of accounting used by the municipality for its annual financial reports (NDCC 40-40-05).
- After the governing body has prepared the preliminary budget statement, the auditor of the municipality shall give notice that: the preliminary budget is on file in the office of the auditor and may be examined by anyone upon request; the governing body shall meet no later than October 7th at the time and place specified in the notice for the purpose of adopting the final budget and making the annual tax levy; and, the governing shall hold a public session at the time and place designated in the notice of the hearing at which any taxpayer may appear and discuss with the body any item of proposed expenditure or may object to any item or amount (NDCC 40-40-06).
- After the budget hearing, the final budget must be prepared on or before October 7th in accordance with provisions outlined in detail in NDCC 40-40-08.
- After completing the final budget on or before October 7th, the governing body shall proceed to make the annual tax levy in an amount sufficient to meet the expenses for the ensuing year as determined at the budget meeting (NDCC 40-40-09).

CITY OF HILLSBORO

Notes to the Required Supplementary Information – Continued

- Immediately after completion of the final budget and adoption of the annual tax levy by the governing body of a municipality in accordance with provisions, and in no case later than October 10th, the auditor of the municipality shall send to the county auditor a certified copy of the final budget (NDCC 40-40-10).
- No municipal expenditure may be made nor liability incurred, and no bill may be paid for any purposes in excess of the appropriation made therefor in the final budget. Expenditures made liabilities incurred, or warrants issued in excess of the appropriations are a joint and several liability the members of the governing body (NDCC 40-40-15).
- At the end of the fiscal year, the balance to credit of each annual appropriation becomes a part of the general unappropriated balance in the municipal treasury, but no special appropriation lapses until the work for which it was made has been completed, the bills paid, and the accounts closed. He governing body of a city may elect, at the end of the fiscal year, to carry over the unencumbered cash balance in the general fund or other budgeted funds and designate the balances for subsequent years (NDCC 40-40-21).

NOTE 2: LEGAL COMPLIANCE - BUDGETS

OVERSPENT FUNDS

The following funds were overspent for the year ended December 31, 2016:

Fund	Budget	Actual	Overspent
Governmental Funds			
<u>Nonmajor Funds</u>			
Planning and Zoning	\$ -	\$ 740	\$ (740)
Armory	30,000	31,274	(1,274)
Main Street Community Center	2,000	28,662	(26,662)
Forestry	-	848	(848)

CITY OF HILLSBORO
Hillsboro, North Dakota

SCHEDULE OF FUND ACTIVITY
ARISING FROM CASH TRANSACTIONS-Cash Amounts by Fund
For the Year Ended December 31, 2016

	Balance 1-1-16	Receipts	Transfers In	Transfers Out	Disbursements	Balance 12-31-16
Major Governmental Funds:						
General Fund	\$ 171,591.59	\$ 369,175.58	\$ 85,141.38	\$ 31,766.37	\$ 459,641.38	\$ 134,500.80
Special Revenue Funds						
Highway Tax/Streets	\$ 100,878.74	\$ 95,879.88	\$ 70,000.00	\$ 5,000.00	\$ 183,265.56	\$ 78,493.06
City Sales Tax Fund	683,937.73	360,224.93	-	490,292.80	23,085.94	530,783.92
Total Major Special Revenue Funds	\$ 784,816.47	\$ 456,104.81	\$ 70,000.00	\$ 495,292.80	\$ 206,351.50	\$ 609,276.98
Capital Project Funds						
Capital Projects	\$ 50,469.21	\$ 36.67	\$ -	\$ -	\$ 1,000.00	\$ 49,505.88
Equipment	38,500.00	-	20,000.00	-	17,000.00	41,500.00
AMR Meter Replacement	20,019.41	-	115,000.00	-	114,931.47	20,087.94
BNSF Caboose Restoration	4,443.00	-	-	-	15.92	4,427.08
Total Major Capital Project Funds	\$ 113,431.62	\$ 36.67	\$ 135,000.00	\$ -	\$ 132,947.39	\$ 115,520.90
Debt Service Funds						
Riverbend Debt Service	\$ 149,256.83	\$ 78,377.09	\$ -	\$ -	\$ 95,464.00	\$ 132,169.92
Project 2006 Water Main	82,232.91	90,005.69	-	-	100,987.50	71,251.10
Highway 200 Debt Service	274,798.05	118,917.04	-	-	95,261.90	298,453.19
2007 Streets Debt Service	362,670.72	264,503.20	-	-	266,920.56	360,253.36
Prairieview Debt Service	(246,375.28)	149,174.10	-	-	136,618.83	(233,820.01)
Kingman Sewer	126,387.89	-	35,000.00	-	54,787.50	106,600.39
City Debt Retirement	-	-	296,292.80	185,000.00	-	111,292.80
Total Major Debt Service Funds	\$ 748,971.12	\$ 700,977.12	\$ 331,292.80	\$ 185,000.00	\$ 750,040.29	\$ 846,200.75
Total Major Governmental Funds	\$ 1,818,810.80	\$ 1,526,294.18	\$ 621,434.18	\$ 712,059.17	\$ 1,548,980.56	\$ 1,705,499.43
Nonmajor Governmental Funds:						
Special Revenue Funds						
Social Security	\$ (5,355.95)	\$ 1,954.95	\$ 5,216.44	\$ 1,815.44	\$ -	\$ -
City's Share of Specials	(1,568.97)	4,733.87	115,000.00	-	97,224.34	20,940.56
Emergency	33,699.89	9.85	-	-	-	33,709.74
Planning and Zoning	30.52	20.40	722.36	33.28	740.00	-
Cemetery	836.86	7,266.48	4,000.00	-	11,144.36	958.98
Armory Operations	651.18	16,250.00	20,000.00	-	31,273.74	5,627.44
Main Street Community Center	(17,346.08)	1,100.00	45,000.00	-	28,661.79	92.13
Forestry	3,287.04	26.20	827.57	3,292.66	848.15	-
CDLF - Wholesale Foods	2,284.57	18,987.48	-	-	18,551.38	2,720.67
Mosquito Control	97,095.60	5,330.44	-	-	7,930.38	94,495.66
Recreation District	(4,347.75)	11,010.39	-	-	10,200.00	(3,537.36)
Total Special Revenue Funds	\$ 109,266.91	\$ 66,690.06	\$ 190,766.37	\$ 5,141.38	\$ 206,574.14	\$ 155,007.82
Total Governmental Funds	\$ 1,928,077.71	\$ 1,592,984.24	\$ 812,200.55	\$ 717,200.55	\$ 1,755,554.70	\$ 1,860,507.25
Major Enterprise Funds:						
Water Fund						
Water Department	\$ 470,149.54	\$ 783,264.11	\$ 185,000.00	\$ 62,500.00	\$ 870,627.62	\$ 505,286.03
Electric Funds						
Generation Project - Debt	\$ 39,639.83	\$ 131,513.59	\$ -	\$ -	\$ 36,544.50	\$ 134,608.92
Electric Department	471,069.42	2,110,613.73	-	212,500.00	1,937,739.09	431,444.06
Meter Deposits	42,785.79	3,460.21	-	-	4,209.77	42,036.23
Total Electric Funds	\$ 553,495.04	\$ 2,245,587.53	\$ -	\$ 212,500.00	\$ 1,978,493.36	\$ 608,089.21
Sewer Fund						
Sewer Department	\$ 105,776.73	\$ 138,448.33	\$ -	\$ 5,000.00	\$ 86,932.02	\$ 152,293.04
Sanitation Fund						
Sanitation Department	\$ 61,075.41	\$ 237,467.94	\$ -	\$ -	\$ 234,340.85	\$ 64,202.50
Total Major Enterprise Funds	\$ 1,190,496.72	\$ 3,404,767.91	\$ 185,000.00	\$ 280,000.00	\$ 3,170,393.85	\$ 1,329,870.78
Agency Fund:						
Airport	\$ -	\$ 10,643.07	\$ -	\$ -	\$ 10,643.07	\$ -
Total Reporting Entity	\$ 3,118,574.43	\$ 5,008,395.22	\$ 997,200.55	\$ 997,200.55	\$ 4,936,591.62	\$ 3,190,378.03



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, 2016, 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 February 8, 2018.

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 [2016-001 and 2016-002].

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.

/s/

Joshua C. Gallion
State Auditor

Fargo, North Dakota
February 8, 2018

CITY OF HILLSBORO
Hillsboro, North Dakota

SCHEDULE OF FINDINGS AND RESPONSES
For the Year Ended December 31, 2016

Section I - Summary of Auditor's Results

Financial Statements

Type of Auditor's Reports 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 weaknesses identified X Yes None noted

Significant deficiencies identified not considered to be material weaknesses?

Yes X None noted

Noncompliance material to financial statements noted?

Yes X None noted

Section II - Financial Statement Findings

2016-001 - 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.

Auditor Response

Regarding the establishment of capital asset records, while management agrees that capital asset records should be established to be in conformity with accounting principles generally accepted in the United States of America, management and the board feel that it is not cost effective to set up and maintain capital asset records as outlined in the recommendation. The lack of capital asset records is a significant financial accounting matter material to the financial statements and note disclosures that results in modified opinions on the financial statements. Capital asset records should be established and maintained so the City is in conformity with accounting principles generally accepted in the United States of America.

2016-002 - 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.

You may obtain audit reports on the internet at:

www.nd.gov/auditor/

or by contacting the
Division of Local Government Audit

Office of the State Auditor
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