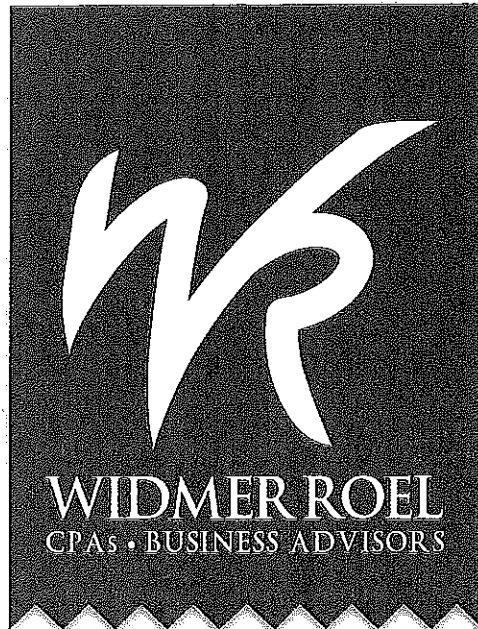




CITY OF HORACE

**FINANCIAL STATEMENTS
DECEMBER 31, 2015 AND 2014**

WITH INDEPENDENT AUDITOR'S REPORT



CITY OF HORACE
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FOR THE YEARS ENDED DECEMBER 31, 2015

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CITY OF HORACE
CITY OFFICIALS
FOR THE YEARS ENDED DECEMBER 31, 2015

Current

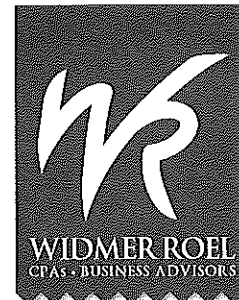
Kory Peterson	Mayor
David Fenelon	Board Member
Bryan Schmidt	Board Member
Sharon May	Board Member
John Koerselman	Board Member
Vance Kemmer	Auditor
Garaas Law Firm	Attorney

December 31, 2015

Shane Walock	Mayor
Sharon May	Board Member
Robert Hoffman	Board Member
John Koerselamn	Board Member
Sharon Hochhalter	Board Member
Vance Kemmer	Auditor
Ohnstad Twichell, P.C.	Attorney

December 31, 2014

Shane Walock	Mayor
Sharon May	Board Member
Robert Hoffman	Board Member
John Koerselamn	Board Member
Sharon Hochhalter	Board Member
Vance Kemmer	Auditor
Ohnstad Twichell, P.C.	Attorney



4334 18th Avenue S.
Ste 101
Fargo, ND 58103-7414

Phone: 701.237.6022
Toll Free: 888.237.6022
Fax: 701.280.1495

INDEPENDENT AUDITOR'S REPORT

City Council
City of Horace
Horace, North Dakota

We have audited the accompanying modified cash financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the **City of Horace** as of and for the years ended December 31, 2015 and 2014, 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 the modified cash basis of accounting described in Note 1; this includes determining that the modified cash basis of accounting is an acceptable basis for the preparation of the financial statements in the circumstances. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to error or fraud.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits 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.

Member of



Basis for Adverse Opinion on Governmental Activities

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 proprietary fund, 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 proprietary fund. The amount by which this departure would affect the assets, net position, and expenses of the governmental activities and the business-type activities is not reasonably determinable.

Adverse Opinion

In our opinion, because of the significance 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 proprietary major fund of **City of Horace** as of December 31, 2015 and 2014, or the changes in financial position for the years then ended.

Unmodified Opinion

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 Horace** as of December 31, 2015 and 2014, and the respective changes in financial position thereof, for the years then ended in accordance with the basis of accounting described in Note 1.

Basis of Accounting

We draw attention to Note 1 of the financial statements, which describes the basis of accounting. The financial statements are prepared on the modified cash basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to these matters.

Other Matters

Disclaimer of Opinion on Supplementary Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the **City of Horace's** basic financial statements. The budgetary comparison information on pages 33-36, which are the responsibility of management, are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

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.

Other Information

Our audits were conducted for the purpose of forming opinions on the financial statements that collectively comprise the **City of Horace's** basic financial statements as a whole. The schedules of fund activity on pages 38-39 are presented for purposes of additional analysis and are not a required part of the basic financial statements. The schedules of fund activity are the responsibility of management and were derived from and relate 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 information is fairly stated in all material respects in relation to the financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated September 19, 2016 on our consideration of the **City of Horace's** internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering **City of Horace's** internal control over financial reporting and compliance.



Fargo, North Dakota
September 19, 2016

CITY OF HORACE

**STATEMENT OF NET POSITION – MODIFIED CASH BASIS
DECEMBER 31, 2015**

	<u>Governmental</u> <u>Activities</u>	<u>Business-type</u> <u>Activities</u>	<u>Total</u>
ASSETS			
Cash and cash equivalents	\$ 3,049,804	\$ -	\$ 3,049,804
Due from enterprise funds	182,688	-	182,688
Note receivable	<u>110,000</u>	<u>-</u>	<u>110,000</u>
Total assets	\$ <u>3,342,492</u>	\$ <u>-</u>	\$ <u>3,342,492</u>
LIABILITIES			
Due to general fund	\$ -	\$ 182,688	\$ 182,688
Long-term liabilities			
Due within one year			
Special assessment bonds payable	326,092	-	326,092
Due after one year			
Special assessment bonds payable	4,400,939	-	4,400,939
Meter deposits	<u>-</u>	<u>20,350</u>	<u>20,350</u>
Total liabilities	<u>4,727,031</u>	<u>203,038</u>	<u>4,930,069</u>
NET POSITION			
Restricted			
Debt service	636,340	-	636,340
Highways maintenance	814,767	-	814,767
Public works	53,172	-	53,172
Special assessments	21,527	-	21,527
Culture and recreation	3,541	-	3,541
Payroll taxes	17,278	-	17,278
Unrestricted	<u>(2,931,164)</u>	<u>(203,038)</u>	<u>(3,134,202)</u>
Total net position	<u>(1,384,539)</u>	<u>(203,038)</u>	<u>(1,587,577)</u>
Total liabilities and net position	\$ <u>3,342,492</u>	\$ <u>-</u>	\$ <u>3,342,492</u>

CITY OF HORACE

**STATEMENT OF ACTIVITIES -- MODIFIED CASH BASIS
FOR THE YEAR ENDED DECEMBER 31, 2015**

	Program Revenues		Net Revenue (Expense) and Changes in Net Position	
	Expenses	Charges for Services	Governmental Activities	Business-type Activities
GOVERNMENTAL ACTIVITIES				
General government	\$ 455,366	\$ 90,916	\$ (364,450)	\$ -
Public safety	30,279	-	(30,279)	-
Public works	2,853,801	167,823	(2,685,978)	-
Bond issuance costs	81,666	-	(81,666)	-
Interest on long-term debt	52,926	-	(52,926)	-
Total governmental activities	<u>3,474,038</u>	<u>90,916</u>	<u>(3,215,299)</u>	<u>-</u>
BUSINESS-TYPE ACTIVITIES				
Water and sewer	441,297	331,035	-	(110,262)
Total	<u>\$ 3,915,335</u>	<u>\$ 421,951</u>	<u>(3,215,299)</u>	<u>(110,262)</u>
GENERAL REVENUES				
Taxes				
Property taxes levied for general purposes			317,751	-
Property taxes levied for special purposes			9,062	-
Special assessments levied for debt service			315,583	-
State revenue sharing			289,462	-
Interest income			617	-
Miscellaneous revenue			165,335	-
Total general revenues			<u>1,097,810</u>	<u>-</u>
Change in net position			<u>(2,117,489)</u>	<u>(110,262)</u>
Net position - January 1			<u>732,950</u>	<u>(92,776)</u>
Net position - December 31			<u>\$ (1,384,539)</u>	<u>\$ (203,038)</u>
				<u>\$ (1,587,577)</u>

CITY OF HORACE

**BALANCE SHEET - MODIFIED CASH BASIS
GOVERNMENTAL FUNDS
DECEMBER 31, 2015**

	<u>General Fund</u>	<u>Highway Fund</u>	<u>Debt Service Funds</u>	<u>Capital Project Funds</u>	<u>Other Government Funds</u>	<u>Total Government Funds</u>
ASSETS						
Cash and cash equivalents	\$ 1,025,347	\$ 814,767	\$ 636,340	\$ 477,832	\$ 95,518	\$ 3,049,804
Due from enterprise funds	<u>182,688</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>182,688</u>
Total assets	<u>\$ 1,208,035</u>	<u>\$ 814,767</u>	<u>\$ 636,340</u>	<u>\$ 477,832</u>	<u>\$ 95,518</u>	<u>\$ 3,232,492</u>
FUND BALANCES						
Restricted for						
Debt service	-	-	636,340	-	-	636,340
Highways maintenance	-	814,767	-	-	-	814,767
Public works	-	-	-	477,832	53,172	531,004
Special assessments	-	-	-	-	21,527	21,527
Culture and recreation	-	-	-	-	3,541	3,541
Payroll taxes	-	-	-	-	17,278	17,278
Unassigned	<u>1,208,035</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,208,035</u>
Total fund balances	<u>\$ 1,208,035</u>	<u>\$ 814,767</u>	<u>\$ 636,340</u>	<u>\$ 477,832</u>	<u>\$ 95,518</u>	<u>\$ 3,232,492</u>

CITY OF HORACE
RECONCILIATION OF GOVERNMENTAL FUNDS BALANCE SHEET
TO THE STATEMENT OF NET POSITION – MODIFIED CASH BASIS
DECEMBER 31, 2015

Total fund balances for governmental funds	\$ 3,232,492
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, 2015 are:	
Special assessment bonds payable	(4,727,031)
Community notes receivable are not available to pay for current period expenditures and thus are not recognized in the governmental funds but are recognized in the statement of net position.	<u>110,000</u>
Total net position of governmental activities	\$ <u>(1,384,539)</u>

CITY OF HORACE

**STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES - MODIFIED CASH BASIS
GOVERNMENTAL FUNDS**

FOR THE YEAR ENDED DECEMBER 31, 2015

	General Fund	Highway Fund	Debt Service Funds	Capital Project Funds	Other Government Funds	Total Government Funds
REVENUES						
Taxes	\$ 317,751	\$ -	\$ -	\$ -	\$ 9,062	\$ 326,813
Special assessments	-	-	315,583	-	-	315,583
Licenses, permits and fees	90,916	-	-	-	-	90,916
Intergovernmental	289,462	167,823	-	-	-	457,285
Interest	617	-	-	-	-	617
Miscellaneous	15,335	-	-	150,000	-	165,335
Total revenues	<u>714,081</u>	<u>167,823</u>	<u>315,583</u>	<u>150,000</u>	<u>9,062</u>	<u>1,356,549</u>
EXPENDITURES						
General government	447,012	-	-	-	8,354	455,366
Public safety	30,279	-	-	-	-	30,279
Public works	-	119,349	-	2,734,452	-	2,853,801
Debt service	-	-	216,804	60,000	-	276,804
Principal	-	-	-	81,666	-	81,666
Bond issuance costs	-	-	38,138	14,788	-	52,926
Interest and fees	-	-	-	-	-	-
Total expenditures	<u>477,291</u>	<u>119,349</u>	<u>254,942</u>	<u>2,890,906</u>	<u>8,354</u>	<u>3,750,842</u>
Excess (deficiency) of revenues over expenditures	<u>236,790</u>	<u>48,474</u>	<u>60,641</u>	<u>(2,740,906)</u>	<u>708</u>	<u>(2,394,293)</u>
OTHER FINANCING SOURCES (USES), INCLUDING TRANSFERS						
Bond proceeds	-	-	-	3,590,000	-	3,590,000
Principal received on loan to park district	20,000	-	-	-	-	20,000
Total other financing sources (uses)	<u>20,000</u>	<u>-</u>	<u>-</u>	<u>3,590,000</u>	<u>-</u>	<u>3,610,000</u>
Net change in fund balances	<u>256,790</u>	<u>48,474</u>	<u>60,641</u>	<u>849,094</u>	<u>708</u>	<u>1,215,707</u>
Fund balances - January 1	<u>951,245</u>	<u>766,293</u>	<u>575,699</u>	<u>(371,262)</u>	<u>94,810</u>	<u>2,016,785</u>
Fund balances - December 31	<u>\$ 1,208,035</u>	<u>\$ 814,767</u>	<u>\$ 636,340</u>	<u>\$ 477,832</u>	<u>\$ 95,518</u>	<u>\$ 3,232,492</u>

See Notes to Financial Statements

CITY OF HORACE

**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, 2015**

Net change in fund balances - total governmental funds \$ 1,215,707

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

The issuance of long-term debt provides current financial resources to governmental funds, but the issuance increases long-term debt in the statement of net position. Also, the 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 special assessment bonds	(3,590,000)
Repayment of special assessment bonds	276,804

The repayment of principal by debtors to the City is considered income in the governmental funds, but the repayment is shown as a reduction of the notes receivable amounts in the statement of net position.

(20,000)

Change in net position of governmental activities \$ (2,117,489)

CITY OF HORACE
STATEMENT OF NET POSITION— MODIFIED CASH BASIS
PROPRIETARY FUNDS
DECEMBER 31, 2015

	<u>Water and Sewer Fund</u>	<u>Other Enterprise Funds</u>	<u>Total Enterprise Funds</u>
ASSETS			
Cash and cash equivalents	\$ <u> -</u>	\$ <u> -</u>	\$ <u> -</u>
LIABILITIES			
Noncurrent liabilities			
Due to general fund	\$ 115,193	\$ 67,495	\$ 182,688
Meter deposits	<u>20,350</u>	<u> -</u>	<u>20,350</u>
Total liabilities	<u>135,543</u>	<u>67,495</u>	<u>203,038</u>
NET POSITION			
Unrestricted	<u>(135,543)</u>	<u>(67,495)</u>	<u>(203,038)</u>
Total liabilities and net position	\$ <u> -</u>	\$ <u> -</u>	\$ <u> -</u>

CITY OF HORACE
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN
FUND NET POSITION – MODIFIED CASH BASIS
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2015

	<u>Water and Sewer Fund</u>	<u>Other Enterprise Funds</u>	<u>Total Enterprise Funds</u>
OPERATING REVENUES			
Water operations	\$ 38,444	\$ -	\$ 38,444
Sanitary sewer operations	67,088	-	67,088
Garbage operations	142,175	-	142,175
Water tower surcharge	41,664	-	41,664
Lagoon surcharge	<u>41,664</u>	<u>-</u>	<u>41,664</u>
Total operating revenues	<u>331,035</u>	<u>-</u>	<u>331,035</u>
OPERATING EXPENSES			
Salaries and wages	109,542	-	109,542
Contracted services	170,571	-	170,571
Maintenance and supplies	148,846	-	148,846
Purchased power costs	<u>12,338</u>	<u>-</u>	<u>12,338</u>
Total operating expenses	<u>441,297</u>	<u>-</u>	<u>441,297</u>
Change in net position	<u>(110,262)</u>	<u>-</u>	<u>(110,262)</u>
Net position - January 1	<u>(25,281)</u>	<u>(67,495)</u>	<u>(92,776)</u>
Net position - December 31	<u>\$ (135,543)</u>	<u>\$ (67,495)</u>	<u>\$ (203,038)</u>

CITY OF HORACE
STATEMENT OF CASH FLOWS -- MODIFIED CASH BASIS
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2015

	Water and Sewer Fund	Other Enterprise Funds	Total Enterprise Funds
CASH FLOWS FROM OPERATING ACTIVITIES			
Receipts from customers	\$ 331,035	\$ -	\$ 331,035
Payments to suppliers	(331,755)	-	(331,755)
Payments to employees	(109,542)	-	(109,542)
Net cash provided by operating activities	(110,262)	-	(110,262)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES			
Interfund loans	110,262	-	110,262
Net increase in cash and cash equivalents	-	-	-
Cash and cash equivalents - January 1	-	-	-
Cash and cash equivalents - December 31	\$ -	\$ -	\$ -

CITY OF HORACE
STATEMENT OF NET POSITION – MODIFIED CASH BASIS
DECEMBER 31, 2014

	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Total</u>
ASSETS			
Cash and cash equivalents	\$ 1,944,359	\$ -	\$ 1,944,359
Due from enterprise funds	72,426	-	72,426
Note receivable	<u>130,000</u>	<u>-</u>	<u>130,000</u>
 Total assets	 <u>\$ 2,146,785</u>	 <u>\$ -</u>	 <u>\$ 2,146,785</u>
LIABILITIES			
Due to general fund	\$ -	\$ 72,426	\$ 72,426
Long-term liabilities			
Due within one year			
Special assessment bonds payable	276,804	-	276,804
Due after one year			
Special assessment bonds payable	1,137,031	-	1,137,031
Meter deposits	<u>-</u>	<u>20,350</u>	<u>20,350</u>
 Total liabilities	 <u>1,413,835</u>	 <u>92,776</u>	 <u>1,506,611</u>
NET POSITION			
Restricted			
Debt service	204,437	-	204,437
Highways	766,293	-	766,293
Public works	53,172	-	53,172
Special Assessments	19,912	-	19,912
Culture and recreation	3,541	-	3,541
Payroll taxes	18,185	-	18,185
Unrestricted	<u>(332,590)</u>	<u>(92,776)</u>	<u>(425,366)</u>
 Total net position	 <u>732,950</u>	 <u>(92,776)</u>	 <u>640,174</u>
 Total liabilities and net position	 <u>\$ 2,146,785</u>	 <u>\$ -</u>	 <u>\$ 2,146,785</u>

CITY OF HORACE

**STATEMENT OF ACTIVITIES – MODIFIED CASH BASIS
FOR THE YEAR ENDED DECEMBER 31, 2014**

	Program Revenues		Net Revenue (Expense) and Changes in Net Position	
	Charges for Services	Capital Grants and Contributions	Governmental Activities	Business-type Activities
GOVERNMENTAL ACTIVITIES				
General government	\$ 261,699	\$ -	\$ (224,755)	\$ (224,755)
Public safety	29,710	-	(29,710)	(29,710)
Public works	126,003	174,226	48,223	48,223
Interest on long-term debt	61,236	-	(61,236)	(61,236)
Total governmental activities	478,648	174,226	(267,478)	(267,478)
BUSINESS-TYPE ACTIVITIES				
Water and sewer	388,507	-	(54,530)	(54,530)
Total	\$ 867,155	\$ 174,226	(267,478)	(322,008)
GENERAL REVENUES				
Taxes				
Property taxes levied for general purposes			304,878	304,878
Property taxes levied for special purposes			9,117	9,117
Special assessments levied for debt service			311,077	311,077
State revenue sharing			279,061	279,061
Interest income			652	652
Miscellaneous revenue			14,237	14,237
Total general revenues			919,022	919,022
Change in net position			(54,530)	597,014
Net position - January 1			81,406	43,160
Net position - December 31			\$ 732,950	\$ 640,174

CITY OF HORACE
BALANCE SHEET – MODIFIED CASH BASIS
GOVERNMENTAL FUNDS
DECEMBER 31, 2014

	General Fund	Highway Fund	Debt Service Funds	Capital Projects Funds	Other Government Funds	Total Government Funds
ASSETS						
Cash and cash equivalents	\$ 507,557	\$ 766,293	\$ 575,699	\$ -	\$ 94,810	\$ 1,944,359
Due from other governmental funds	371,262	-	-	-	-	371,262
Due from enterprise funds	72,426	-	-	-	-	72,426
Total assets	\$ 951,245	\$ 766,293	\$ 575,699	\$ -	\$ 94,810	\$ 2,388,047
LIABILITIES						
Due to other funds	\$ -	\$ -	\$ -	\$ 371,262	\$ -	\$ 371,262
FUND BALANCES						
Restricted for						
Debt service	-	-	575,699	-	-	575,699
Highways maintenance	-	766,293	-	-	-	766,293
Public works	-	-	-	-	53,172	53,172
Special assessments	-	-	-	-	19,912	19,912
Culture and recreation	-	-	-	-	3,541	3,541
Social security taxes	-	-	-	-	18,185	18,185
Unassigned	951,245	-	-	(371,262)	-	579,983
Total fund balances	951,245	766,293	575,699	(371,262)	94,810	2,016,785
Total liabilities and fund balances	\$ 951,245	\$ 766,293	\$ 575,699	\$ -	\$ 94,810	\$ 2,388,047

CITY OF HORACE
RECONCILIATION OF GOVERNMENTAL FUNDS BALANCE SHEET
TO THE STATEMENT OF NET POSITION – MODIFIED CASH BASIS
DECEMBER 31, 2014

Total fund balances for governmental funds	\$ 2,016,785
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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, 2014 are:

Special assessment bonds payable	(1,413,835)
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Community notes receivable are not available to pay for current period expenditures and thus are not recognized in the governmental funds but are recognized in the statement of net position.

	<u>130,000</u>
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Total net position of governmental activities	\$ <u><u>732,950</u></u>
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CITY OF HORACE

**STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCES - MODIFIED CASH BASIS
GOVERNMENTAL FUNDS**

FOR THE YEAR ENDED DECEMBER 31, 2014

	General Fund	Highway Fund	Debt Service Funds	Capital Projects Funds	Other Government Funds	Total Government Funds
REVENUES						
Taxes	\$ 304,878	\$ -	\$ -	\$ -	\$ 9,117	\$ 313,995
Special assessments	-	-	311,077	-	-	311,077
Licenses, permits and fees	36,944	-	-	-	-	36,944
Intergovernmental	279,061	174,226	-	-	-	453,287
Interest	652	-	-	-	-	652
Miscellaneous	14,237	-	-	-	-	14,237
Total revenues	<u>635,772</u>	<u>174,226</u>	<u>311,077</u>	<u>-</u>	<u>9,117</u>	<u>1,130,192</u>
EXPENDITURES						
Current						
General government	253,734	-	-	-	7,965	261,699
Public safety	29,710	-	-	-	-	29,710
Public works	-	126,003	-	-	-	126,003
Debt service	-	-	-	-	-	-
Principal	-	-	215,531	60,000	-	275,531
Interest and fees	-	-	44,642	16,594	-	61,236
Total expenditures	<u>283,444</u>	<u>126,003</u>	<u>260,173</u>	<u>76,594</u>	<u>7,965</u>	<u>754,179</u>
Excess (deficiency) of revenues over expenditures	<u>352,328</u>	<u>48,223</u>	<u>50,904</u>	<u>(76,594)</u>	<u>1,152</u>	<u>376,013</u>
OTHER FINANCING SOURCES (USES), INCLUDING TRANSFERS						
Loans to others	(160,000)	-	-	-	-	(160,000)
Principal received on loans to others	30,000	-	-	-	-	30,000
Total other financing sources (uses)	<u>(130,000)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(130,000)</u>
Net change in fund balances	<u>222,328</u>	<u>48,223</u>	<u>50,904</u>	<u>(76,594)</u>	<u>1,152</u>	<u>246,013</u>
Fund balances - January 1	728,917	718,070	524,795	(294,668)	93,658	1,770,772
Fund balances - December 31	<u>\$ 951,245</u>	<u>\$ 766,293</u>	<u>\$ 575,699</u>	<u>\$ (371,262)</u>	<u>\$ 94,810</u>	<u>\$ 2,016,785</u>

See Notes to Financial Statements

CITY OF HORACE

**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, 2014**

Net change in fund balances - total governmental funds \$ 246,013

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

The issuance of long-term debt provides current financial resources to governmental funds, but the issuance increases long-term debt in the statement of net position. Also, the repayment of debt principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net position.

Repayment of special assessment bonds 275,531

Long-term community development loans (notes receivable) made by the City during the current year are reported as expenditures in the governmental funds but are shown as a notes receivable in the Statement of Net Position. 160,000

The repayment of principal by debtors to the City is considered income in the governmental funds, but the repayment is shown as a reduction of the notes receivable amounts in the Statement of Net Position. (30,000)

Change in net position of governmental activities \$ 651,544

CITY OF HORACE
STATEMENT OF NET POSITION – MODIFIED CASH BASIS
PROPRIETARY FUNDS
DECEMBER 31, 2014

	<u>Water and Sewer Fund</u>	<u>Other Enterprise Fund</u>	<u>Total Enterprise Funds</u>
ASSETS			
Cash and cash equivalents	\$ <u>-</u>	\$ <u>-</u>	\$ <u>-</u>
LIABILITIES			
Noncurrent liabilities			
Due to general fund	\$ 4,931	\$ 67,495	\$ 72,426
Meter deposits	<u>20,350</u>	<u>-</u>	<u>20,350</u>
Total liabilities	<u>25,281</u>	<u>67,495</u>	<u>92,776</u>
NET POSITION			
Unrestricted	<u>(25,281)</u>	<u>(67,495)</u>	<u>(92,776)</u>
Total liabilities and net position	\$ <u>-</u>	\$ <u>-</u>	\$ <u>-</u>

CITY OF HORACE
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN
FUND NET POSITION—MODIFIED CASH BASIS
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2014

	<u>Water and Sewer Fund</u>	<u>Other Enterprise Funds</u>	<u>Total Enterprise Funds</u>
OPERATING REVENUES			
Water operations	\$ 47,296	\$ -	\$ 47,296
Sanitary sewer operations	63,642	-	63,642
Garbage operations	145,021	-	145,021
Water tower surcharge	39,009	-	39,009
Lagoon surcharge	<u>39,009</u>	<u>-</u>	<u>39,009</u>
Total operating revenues	<u>333,977</u>	<u>-</u>	<u>333,977</u>
OPERATING EXPENSES			
Salaries and wages	95,123	-	95,123
Contracted services	167,928	-	167,928
Maintenance and supplies	111,777	-	111,777
Purchased power costs	<u>13,679</u>	<u>-</u>	<u>13,679</u>
Total operating expenses	<u>388,507</u>	<u>-</u>	<u>388,507</u>
Change in net position	<u>(54,530)</u>	<u>-</u>	<u>(54,530)</u>
Net position - January 1	<u>29,249</u>	<u>(67,495)</u>	<u>(38,246)</u>
Net position - December 31	<u>\$ (25,281)</u>	<u>\$ (67,495)</u>	<u>\$ (92,776)</u>

CITY OF HORACE
STATEMENT OF CASH FLOWS – MODIFIED CASH BASIS
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2014

	Water and Sewer Fund	Other Enterprise Funds	Total Enterprise Funds
CASH FLOWS FROM OPERATING ACTIVITIES			
Receipts from customers	\$ 333,977	\$ -	\$ 333,977
Payments to suppliers	(293,384)	-	(293,384)
Payments to employees	(95,123)	-	(95,123)
Net cash used by operating activities	(54,530)	-	(54,530)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES			
Interfund loans	4,931	-	4,931
Net decrease in cash and cash equivalents	(49,599)	-	(49,599)
Cash and cash equivalents - January 1	49,599	-	49,599
Cash and cash equivalents - December 31	\$ -	\$ -	\$ -

CITY OF HORACE
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2015

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

The City of Horace, North Dakota, was incorporated under the laws of the State of North Dakota and operates under a city commission form of government. The accounting policy of the City of Horace, 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. Records are not maintained for capital assets. Since capital asset records are not maintained, depreciation is not recognized and recorded as an expense. 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.

Financial Reporting Entity

The accompanying financial statements present the activities of the City of Horace (“City”). 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 GASB has set forth criteria to be considered in determining financial accountability. This criterion includes appointing a voting majority of an organization’s governing body and (1) the ability of the City of Horace 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 Horace.

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

Basis of Presentation

Government-wide Financial Statements: The statement of net position and the statement of activities report information on all of the non-fiduciary activities of the primary government of the City of Horace. Eliminations have been made to minimize the double counting of internal activities. 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 is 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. 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 non-major funds.

CITY OF HORACE
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2015

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. Non-operating revenues, such as subsidies and investment earnings, result from non-exchange 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 Fund - This fund is used to account for taxes received for streets and highways and for repair and maintenance projects.

Debt Service Funds - This fund includes all of the City's debt service funds aggregated and reported as one major debt service fund. This fund is used to account for the accumulation of resources for, and the payment of, general long-term debt principal, interest and related costs.

Capital Project Funds - This fund includes all of the City's capital project funds aggregated and reported as one major fund. This fund is used to account for financial resources, including special assessments, to be used for the acquisition or construction of major capital facilities, (other than those financed by proprietary funds or trust funds).

The City reports the following major enterprise fund:

Water and Sewer Fund - This fund is used to account for customer receipts and payments for public utilities.

Measurement Focus and Basis of Accounting

In the government-wide statement of net position and the statement of activities, both governmental and business-type 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 funds utilize an economic resources measurement focus. The accounting objectives of this measurement focus are the determination of operating income, changes in net assets (or cost recovery), financial position, and cash flows. All assets and liabilities (whether current or noncurrent, financial, or nonfinancial) associated with their activities are reported. Proprietary fund equity is classified as net assets.

CITY OF HORACE

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 2015

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 with a provision for depreciation 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.

Cash, Cash Equivalents and Investments

Cash and cash equivalents include amounts in demand deposits and certificates of deposit with original maturities less than 90 days, stated at cost.

Investments consist of certificates of deposit, with an original maturity date in excess of 90 days, stated at cost, which approximates market.

Due from (to) other Funds

Due from (to) other Funds arise primarily as a result of a cash deficit in one or more funds. These liabilities are expected to be eliminated within one year through future revenues and transfers.

Fund Balances – Governmental Funds

Fund equity at the governmental fund financial reporting level is classified as “fund balance.” Fund equity for all other reporting is classified as “net position.”

Fund Balance – Generally, the fund balance represents the difference between current assets and current liabilities. In the fund financial statements, the governmental funds report fund classification that comprise a hierarchy based primarily on the extent to which the City is bound to honor constraints on the specific purposes for which amounts in those funds are spent. Fund balances are classified as follows:

Nonspendable – Fund balances that cannot be spent because they are either (a) not in spendable form or (b) legally or contractually required to be maintained intact.

Restricted – Constraints are placed on the use of fund balances which are either (a) Externally imposed by creditors, grantors, contributors, or laws or regulations of other governments or (b) Imposed by law through constitutional provisions or enabling legislation.

Committed – Committed fund balances 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 rescind a fund balance commitment.

(Continued)

CITY OF HORACE

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 2015

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 city's management.

Unassigned – Unassigned fund balances are those that have not been reported in any other classification. The General Fund is the only fund that can report a positive unassigned fund balance.

At December 31, 2015 and 2014, the City only had restricted and unassigned fund balances. Restricted fund balances were constrained by state laws related to specific tax levies and highway tax distributions, as well as provisions of debt covenants.

Net Position – Net position represent the difference between assets and liabilities. Net positions are classified in the following categories:

Net Investment in Capital Assets – This amount consists of capital assets net of accumulated depreciation and reduced by outstanding debt that is attributed to the acquisition, construction, or improvement of the assets.

Restricted Net Position – This amount is restricted by creditors, grantors, contributors, or laws or regulations of other governments.

Unrestricted Net Position – This amount is the net position that does not meet the definition of "net investment in capital assets" or "restricted net position".

As of December 31, 2015 and 2014, the City had \$1,546,625 and \$1,065,540, respectively, in restricted net position, which are restricted by state laws regarding use of tax levies and state revenues.

Flow Assumptions – When both restricted and unrestricted amounts of fund balances are available for use for expenditures incurred, it is the City's policy to use restricted amounts first and then unrestricted amounts as they are needed. For unrestricted amounts of fund balance, it is the City's policy to first use restricted, then committed, then assigned, and then unassigned resources as they are needed.

NOTE 2 – DEPOSITS AND INVESTMENTS

In accordance with North Dakota Statutes, the City of Horace maintains deposits 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 any other state of the United States or such other securities approved by the banking board.

CITY OF HORACE

**NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2015**

At year ended December 31, 2015 and 2014, the City's carrying amount of deposits were \$3,049,804 and \$1,944,359, respectively, and the bank balances were \$3,291,476 and \$2,167,688, respectively. Of the bank balances, \$332,204 was covered by Federal Depository Insurance at December 31, 2015 and \$332,080 was covered by Federal Depository Insurance at December 31, 2014. The remaining bank balances at December 31, 2015 and 2014 were covered by securities pledged by the financial institution in the City's name.

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. Beyond what is stated in the North Dakota Century Code, the City does not have a formal policy to further limit exposure to custodial credit risk. As noted above, the City's deposits were all either fully insured or collateralized.

Investments

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.

As of December 31, 2015 and 2014, the City held certificates of deposit in the amount of \$304,885 and \$304,268, respectively, which are risked as deposits.

NOTE 3 – INTERFUND RECEIVABLES, PAYABLES, AND TRANSFERS

For the years ended December 31, 2015 and 2014, the City had the following interfund receivable/payable balances:

	<u>2015</u>	<u>2014</u>
Due to:	\$ <u>182,688</u>	\$ <u>443,688</u>
General fund		
Due from:		
Capital projects fund	\$ -	\$ 371,262
Water and sewer fund	115,193	4,931
Water meter/chem feed building	67,495	67,495
	\$ <u>182,688</u>	\$ <u>443,688</u>

CITY OF HORACE
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2015

NOTE 4 – NOTE RECEIVABLE

January 1, 2014, the City entered into a promissory note agreement to loan \$160,000 to the Park District of Horace, North Dakota. Under this agreement, the Park District will repay the loan in monthly installments of \$2,500 with a balloon payment due June 1, 2019. The loan carries an interest rate of 1.5%. At December 31, 2015 and 2014, the receivable had a remaining balance of \$110,000 and \$130,000, respectively.

NOTE 5 – LONG-TERM LIABILITIES

The following changes occurred in long-term liabilities of the City:

Governmental Activities

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Special assessment bonds payable					
2015	\$ 1,413,835	\$ 3,590,000	\$ 276,804	\$ 4,727,031	\$ 326,092
2014	\$ 1,689,366	\$ -	\$ 275,531	\$ 1,413,835	\$ 276,804

BUSINESS-TYPE ACTIVITIES (PROPRIETARY FUNDS)

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Meter deposits					
2015	\$ 20,350	\$ -	\$ -	\$ 20,350	\$ -
2014	\$ 20,350	\$ -	\$ -	\$ 20,350	\$ -

Special Assessment Bonds

The City issues special assessment bonds for various construction projects. These bonds will be repaid from debt service or capital projects funds by amounts levied against the property owners benefited by the project.

Special assessment bonds at December 31, 2015 are comprised of the following individual issues:

\$195,330 water stabilization loan from municipal bond bank due in annual installments of \$10,000 to \$15,000 through September 1, 2017; interest at 2.5%	\$ 30,000
\$420,000 of refunding improvement bonds of 2005 due in annual installments of \$30,000 through May 1, 2020; interest at 3.3% to 4.25%	150,000
\$565,000 of refunding improvement bonds of 2007 due in annual installments of \$40,000 to \$45,000 through May 1, 2022; interest at 3.75% to 4.5%	280,000
\$565,000 of refunding improvement bonds of 2008 due in annual installments of \$55,000 to \$60,000 through May 1, 2018; interest at 2.35% to 4.0%	165,000
\$98,000 of refunding improvement bonds of 2008 due in annual installments of \$4,559 to \$8,966 through November 1, 2024; interest at 4.95%	67,031

(Continued)

CITY OF HORACE

**NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2015**

\$750,000 of refunding improvement bonds of 2010 due in annual installments of \$35,000 to \$100,000 through May 1, 2019; interest at 1.00% to 3.25%	260,000
\$300,000 of refunding improvement bonds of 2010 due in annual installments of \$25,000 to \$35,000 through May 1, 2021; interest at 2.00% to 3.00%	185,000
\$3,590,000 of refunding improvement bonds of 2015 due in annual installments of \$55,000 to \$160,000 through May 1, 2040; interest at 1.10% to 4.00%	<u>3,590,000</u>
Total special assessment bonds	\$ <u><u>4,727,031</u></u>

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

	Special Assessments Bonds Payable	
	<u>Principal</u>	<u>Interest</u>
2016	\$ 326,092	\$ 139,006
2017	431,393	128,970
2018	356,710	118,311
2019	302,042	109,367
2020	267,390	101,314
2021-2025	928,406	420,785
2026-2030	735,000	311,919
2031-2035	700,000	196,550
2036-2040	<u>679,998</u>	<u>67,600</u>
	\$ <u><u>4,727,031</u></u>	\$ <u><u>1,593,822</u></u>

Interest paid on special assessment bonds during 2015 and 2014 totaled \$52,926 and \$61,236, respectively, all of which was charged to expense.

Conduit Debt

On October 7, 2013, the City adopted a resolution approving the issuance \$4,960,000 Health Care Revenue Note, Series 2013B and \$1,040,000 Health Care Revenue Note, Series 2013C to finance, in part, the acquisition, construction, and equipping of a 96-bed skilled nursing home. At December 31, 2015 and 2014, the notes had an aggregate outstanding balance of \$4,725,360 and \$50,000, respectively.

On October 1, 2014, the City entered an agreement with the Lutheran Social Services of North Dakota, a North Dakota nonprofit corporation, to issue its First Mortgage Revenue Bonds (Lutheran Social Services Project) Series 2014 in the amount not exceeding \$1,500,000 for the purposes of constructing a 24,000 square foot headquarters office building for the Organization. At December 31, 2015 and 2014, the notes had an aggregate outstanding balance of \$1,491,663 and \$1,500,000, respectively.

CITY OF HORACE

**NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2015**

On April 1, 2015, the City entered an agreement with the YMCA of Cass and Clay Counties, a North Dakota nonprofit corporation, to issue Wellness Facilities Revenue Bonds (YMCA of Cass and Clay Counties Project) Series 2015 in an aggregate amount not exceeding \$3,000,000 for the purposes of (i) renovating and constructing an addition to the aquatic facilities located at 400 1st Avenue South, Fargo, North Dakota, and (ii) paying the cost of issuance. At December 31, 2015, the notes had an aggregate outstanding balance of \$1,326,980. The remaining proceeds were advanced during 2016.

Upon repayment of the notes, ownership of the acquired facilities transfers from the lender to the private-sector entity served by the notes. Neither the City, state, nor any political subdivision thereof is obligated in any manner for repayment of the loans. Accordingly, the notes are not reported as liabilities in the accompanying financial statements.

NOTE 6 – FUND DEFICITS

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

	<u>2015</u>	<u>2014</u>
Debt service funds		
Lagoon expansion 97-98	\$ (76,635)	\$ (60,322)
Water and sewer 02-1/streets 02-2	(347,325)	(283,713)
Improvement district 04-3	(48,823)	(39,413)
Rud's 1st and 2nd addition	(96,945)	(96,945)
Lakeview Heights addition	(4,790)	(4,790)
Street paving 07-1 and 07-2	(56,313)	(2,118)
Sanitary sewer relocate 07-2	(65,388)	(65,388)
Refunding impr bonds 2010 (refi 2003 and 2005)	(625,681)	(515,345)
Capital project funds		
Sparks addition 98-1	(2,126)	(2,126)
Billy Harris street paving	(11,181)	(11,181)
Storm sewer 2000-1	(16,500)	(16,500)
Refunding impr bonds 2004 (refi 1997)	(74,511)	(74,511)
Street paving - post office road	(44,080)	(44,080)
Refunding impr bonds 2005 (refi 1999)	(173,469)	(135,402)
Drainage improvement district 10-01	(124,183)	(87,462)
Enterprise funds		
Water and sewer operating - major	(115,193)	(4,931)
Water meter/chem feed building - nonmajor	(67,495)	(67,495)

These deficits are anticipated to be remediated by future transfers.

NOTE 7 – 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

CITY OF HORACE

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 2015

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 8 – PENSION PLAN

The City of Horace provides a retirement plan for City employees. The plan is a SIMPLE IRA defined contribution plan in which the City contributes an amount established by the governing board, currently 3% of gross salaries for each eligible employee. Employees are immediately 100% vested in all employer contributions. An employee's contribution can be any amount less than or equal to the maximum amount allowed by law. Contributions are determined on base salary and exclude any overtime or bonuses earned by employees. To initially be eligible for the plan, the employee must have earned at least \$5,000 per year during any two preceding years and are expected to earn at least \$5,000 in the current year. Once eligibility requirements are met for plan participation, an employee begins actual participation in the plan on the first day of the first plan year after he/she has met the eligibility requirements. A deduction is made monthly and forwarded to the plan account, which is maintained by Alerus Financial. 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, 2015 and 2014 were \$3,812 and \$3,175, respectively.

NOTE 9 – RISK MANAGEMENT

The City of Horace 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 (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 to \$242,261 million for public assets coverage.

The City of Horace 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 one million dollars per occurrence during a 12-month period. The State Bonding Fund currently provides the City of Horace with blanket fidelity bond coverage in the amount of \$843,000 for the City employees.

The City has workers compensation with the North Dakota Workforce Safety and Insurance. The City provides single 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.

CITY OF HORACE

**NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2015**

NOTE 10 – CONTINGENT LIABILITIES

On September 7, 1976, the City entered into a contract with a developer for installation of water and sewer lines and related infrastructure. The developer's rights under the contract were later assigned to a third party. On August 11, 2009, the City was served with legal papers regarding a civil lawsuit initiated against the City by the above-mentioned assignee to the contract. The lawsuit alleges that the City failed to perform under the September 7, 1976 contract. The litigation is currently in the discovery phase and the City's potential liability under the lawsuit cannot be reasonably estimated. The City's legal counsel intends to vigorously contest the lawsuit.

In October 2014, the City approved the development of the Dream Fields 2014-1 addition. Subsequent to inception of the project, a dispute occurred between the project developer and an outside party over ownership of the southern portion of land included in the development. Currently the parties to the land ownership dispute are working on a resolution. The City completed the development project in 2015.

CITY OF HORACE

**SUPPLEMENTAL SCHEDULES
DECEMBER 31, 2015 AND 2014**

CITY OF HORACE
BUDGETARY COMPARISON SCHEDULE – MODIFIED CASH BASIS
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2015

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>	<u>Over (Under) Final Budget</u>
REVENUES				
Taxes	\$ 308,308	\$ 308,308	\$ 317,751	\$ 9,443
Licenses, permits and fees	9,300	9,300	90,916	81,616
Intergovernmental	87,500	87,500	289,462	201,962
Interest	950	950	617	(333)
Miscellaneous	<u>46,000</u>	<u>46,000</u>	<u>15,335</u>	<u>(30,665)</u>
Total revenues	<u>452,058</u>	<u>452,058</u>	<u>714,081</u>	<u>262,023</u>
EXPENDITURES				
Current				
General government	452,058	452,058	447,012	(5,046)
Public safety	<u>-</u>	<u>-</u>	<u>30,279</u>	<u>30,279</u>
Total expenditures	<u>452,058</u>	<u>452,058</u>	<u>477,291</u>	<u>25,233</u>
Excess of revenues over expenditures	<u>-</u>	<u>-</u>	<u>236,790</u>	<u>236,790</u>
OTHER FINANCING SOURCES (USES)				
Principal received on loan to park district	<u>-</u>	<u>-</u>	<u>20,000</u>	<u>20,000</u>
Net change in fund balance	<u>-</u>	<u>-</u>	<u>256,790</u>	<u>236,790</u>
Fund balances - Beginning of year	<u>951,245</u>	<u>951,245</u>	<u>951,245</u>	<u>-</u>
Fund balances - End of year	<u>\$ 951,245</u>	<u>\$ 951,245</u>	<u>\$ 1,208,035</u>	<u>\$ 236,790</u>

CITY OF HORACE
BUDGETARY COMPARISON SCHEDULE – MODIFIED CASH BASIS
HIGHWAY FUND
FOR THE YEAR ENDED DECEMBER 31, 2015

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>	<u>Variance with Final Budget</u>
REVENUES				
Intergovernmental	\$ <u>-</u>	\$ <u>-</u>	\$ <u>167,823</u>	\$ <u>167,823</u>
EXPENDITURES				
Current				
Public works	<u>80,000</u>	<u>80,000</u>	<u>119,349</u>	<u>39,349</u>
Excess (deficiency) of revenues over expenditures	<u>(80,000)</u>	<u>(80,000)</u>	<u>48,474</u>	<u>128,474</u>
Fund balances - January 1	<u>766,293</u>	<u>766,293</u>	<u>766,293</u>	<u>-</u>
Fund balances - December 31	\$ <u><u>686,293</u></u>	\$ <u><u>686,293</u></u>	\$ <u><u>814,767</u></u>	\$ <u><u>128,474</u></u>

CITY OF HORACE
BUDGETARY COMPARISON SCHEDULE – MODIFIED CASH BASIS
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2014

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>	<u>Over (Under) Final Budget</u>
REVENUES				
Taxes	\$ 275,626	\$ 275,626	\$ 304,878	\$ 29,252
Licenses, permits and fees	20,600	20,600	36,944	16,344
Intergovernmental	56,000	56,000	279,061	223,061
Interest	2,500	2,500	652	(1,848)
Miscellaneous	<u>22,000</u>	<u>22,000</u>	<u>14,237</u>	<u>(7,763)</u>
Total revenues	<u>376,726</u>	<u>376,726</u>	<u>635,772</u>	<u>259,046</u>
EXPENDITURES				
Current				
General government	333,626	333,626	253,734	(79,892)
Public safety	<u>32,000</u>	<u>32,000</u>	<u>29,710</u>	<u>(2,290)</u>
Total expenditures	<u>365,626</u>	<u>365,626</u>	<u>283,444</u>	<u>(82,182)</u>
Excess of revenues over expenditures	<u>11,100</u>	<u>11,100</u>	<u>352,328</u>	<u>341,228</u>
OTHER FINANCING SOURCES (USES)				
Loan to park district	-	-	(160,000)	(160,000)
Principal received on loan to park district	<u>-</u>	<u>-</u>	<u>30,000</u>	<u>30,000</u>
Total other financing sources (uses)	<u>-</u>	<u>-</u>	<u>(130,000)</u>	<u>(130,000)</u>
Net change in fund balances	<u>11,100</u>	<u>11,100</u>	<u>222,328</u>	<u>211,228</u>
Fund balances - January 1	<u>728,917</u>	<u>728,917</u>	<u>728,917</u>	<u>-</u>
Fund balances - December 31	<u>\$ 740,017</u>	<u>\$ 740,017</u>	<u>\$ 951,245</u>	<u>\$ 211,228</u>

CITY OF HORACE
BUDGETARY COMPARISON SCHEDULE – MODIFIED CASH BASIS
HIGHWAY FUND
FOR THE YEAR ENDED DECEMBER 31, 2014

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>	<u>Over (Under) Final Budget</u>
REVENUES				
Intergovernmental	\$ <u>135,000</u>	\$ <u>135,000</u>	\$ <u>174,226</u>	\$ <u>39,226</u>
EXPENDITURES				
Current				
Public works	<u>75,000</u>	<u>75,000</u>	<u>126,003</u>	<u>51,003</u>
Excess of revenues over expenditures	<u>60,000</u>	<u>60,000</u>	<u>48,223</u>	<u>(11,777)</u>
Fund balances - January 1	<u>718,070</u>	<u>718,070</u>	<u>718,070</u>	<u>-</u>
Fund balances - December 31	\$ <u><u>778,070</u></u>	\$ <u><u>778,070</u></u>	\$ <u><u>766,293</u></u>	\$ <u><u>(11,777)</u></u>

CITY OF HORACE

**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
FOR THE YEARS ENDED DECEMBER 31, 2015**

NOTE 1 – STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

Budgetary Information:

- a) The City commission adopts an appropriated budget on the modified cash basis of accounting.
- b) Annually on or before September 10th the City prepares a preliminary budget. NDCC Section 40-40-04
- c) 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 Section 40-40-05
- d) 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 Section 40-40-08
- e) The City commission, on or before October 7th, completes the final budget. NDCC Section 40-40-09
- f) Each budget is controlled by the City auditor at the revenue and expenditure function/object level.
- g) 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 Section 57-15-31.1
- h) All appropriations lapse at year-end.

NOTE 2 – LEGAL COMPLIANCE – BUDGETS

Expenditures exceeded budget years ended December 31 by the following amounts:

	<u>2015</u>	<u>2014</u>
General fund	\$ 25,233	\$ -
Highway fund	\$ 39,349	\$ 51,003

No remedial action is anticipated or required by the City regarding these excess expenditures.

CITY OF HORACE

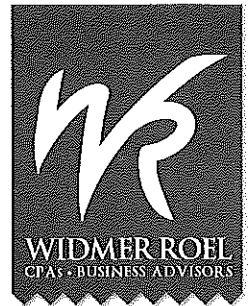
**SCHEDULE OF FUND ACTIVITY ARISING FROM CASH TRANSACTIONS
FOR THE YEAR ENDED DECEMBER 31, 2015**

	Balance 12/31/14	Receipts	Transfers In	Financing Sources	Transfers Out	Disbursements	Balance 12/31/15
MAJOR GOVERNMENTAL FUNDS							
General fund	\$ 951,245	\$ 714,081	\$ -	\$ 20,000	\$ -	\$ 477,291	\$ 1,208,035
Highway fund	766,293	167,823	-	-	-	119,349	814,767
<u>Total debt service funds - major fund</u>	1,643,733	315,583	-	-	-	1,076	1,958,240
Street improvements 93-1	(60,322)	-	-	-	-	16,313	(76,635)
Lagoon expansion 97-98	(283,713)	-	-	-	-	63,612	(347,325)
Water and sewer 02-1/streets 02-2	(39,413)	-	-	-	-	9,410	(48,823)
Improvement district 04-3	(96,945)	-	-	-	-	-	(96,945)
Rud's 1st and 2nd addition	(4,790)	-	-	-	-	-	(4,790)
Lakeview Heights addition	(2,118)	-	-	-	-	54,195	(56,313)
Street paving 07-1 and 07-2	(65,388)	-	-	-	-	-	(65,388)
Sanitary sewer relocate 07-2	(515,345)	-	-	-	-	110,336	(625,681)
Refunding impr bonds 2010 (refi 2003 and 2005)							
Total	575,699	315,583	-	-	-	254,942	636,340
<u>Total capital projects funds - major fund</u>	(2,126)	-	-	-	-	-	(2,126)
Sparks addition 98-1	(11,181)	-	-	-	-	-	(11,181)
Billy Harris street paving	(16,500)	-	-	-	-	-	(16,500)
Storm sewer 2000-1	(74,511)	-	-	-	-	-	(74,511)
Refunding impr bonds 2004 (refi 1997)	(44,080)	-	-	-	-	-	(44,080)
Street paving - post office road	(135,402)	-	-	-	-	38,067	(173,469)
Refunding impr bonds 2005 (refi 1999)	(87,462)	-	-	-	-	36,721	(124,183)
Drainage improvement district 10-01	-	150,000	-	-	-	1,041,700	247,141
Dream Fields 2014-1	-	-	-	1,138,841	-	-	61,268
Street improvement district 2015-1/52nd	-	-	-	75,000	-	13,732	-
Prairie Way 2015-2	-	-	-	2,376,159	-	1,760,686	615,473
Total	(371,262)	150,000	-	3,590,000	-	2,890,906	477,832
NONMAJOR GOVERNMENTAL FUNDS							
Social security	18,185	7,447	-	-	-	8,354	17,278
City's share of specials	19,912	1,615	-	-	-	-	21,527
Gaming fund	3,541	-	-	-	-	-	3,541
Sleepy Hollow	12,397	-	-	-	-	-	12,397
Riverdale	40,775	-	-	-	-	-	40,775
Total	94,810	9,062	-	-	-	8,354	95,518
TOTAL GOVERNMENTAL FUNDS	2,016,785	1,356,549	-	3,610,000	-	3,750,842	3,232,492
ENTERPRISE FUNDS							
Water and sewer operating - major	(4,931)	331,035	-	-	-	441,297	(115,193)
Water meter/chem feed building - nonmajor	(67,495)	-	-	-	-	-	(67,495)
TOTAL ENTERPRISE FUNDS	(72,426)	331,035	-	-	-	441,297	(182,688)
TOTAL REPORTING ENTITY	\$ 1,944,359	\$ 1,687,584	\$ -	\$ 3,610,000	\$ -	\$ 4,192,139	\$ 3,049,804

CITY OF HORACE

**SCHEDULE OF FUND ACTIVITY ARISING FROM CASH TRANSACTIONS
FOR THE YEAR ENDED DECEMBER 31, 2014**

	<u>Balance 12/31/13</u>	<u>Receipts</u>	<u>Transfers In</u>	<u>Financing Sources (Uses)</u>	<u>Transfers Out</u>	<u>Disbursements</u>	<u>Balance 12/31/14</u>
MAJOR GOVERNMENTAL FUNDS							
General fund	\$ 728,917	\$ 635,772	\$ -	\$ (130,000)	\$ -	\$ 283,444	\$ 951,245
Highway fund	718,070	174,226	-	-	-	126,003	766,293
<u>Total debt service funds - major fund</u>	1,332,656	311,077	-	-	-	-	1,643,733
Street improvements 93-1	(43,559)	-	-	-	-	16,763	(60,322)
Lagoon expansion 97-98	(218,166)	-	-	-	-	65,547	(283,713)
Water and sewer 02-1/streets 02-2	(30,003)	-	-	-	-	9,410	(89,413)
Improvement district 04-3	(96,945)	-	-	-	-	-	(96,945)
Rud's 1st and 2nd addition	(4,790)	-	-	-	-	-	(4,790)
Lakeview heights addition	53,720	-	-	-	-	55,838	(2,118)
Street paving 07-1 and 07-2	(65,388)	-	-	-	-	-	(65,388)
Sanitary sewer relocates 07-3	(402,730)	-	-	-	-	112,615	(515,345)
Refunding impr bonds 2010 (refi 2003 and 2005)	524,795	311,077	-	-	-	260,173	575,699
<u>Total</u>							
<u>Total capital projects funds - major fund</u>	(2,126)	-	-	-	-	-	(2,126)
Sparks addition 98-1	(11,181)	-	-	-	-	-	(11,181)
Billy Harris street paving	(16,500)	-	-	-	-	-	(16,500)
Storm sewer 2000-1	(74,511)	-	-	-	-	-	(74,511)
Refunding impr bonds 2004 (refi 1997)	(44,080)	-	-	-	-	-	(44,080)
Street paving - post office road	(96,131)	-	-	-	-	39,271	(135,402)
Refunding impr bonds 2005 (refi 1999)	(50,139)	-	-	-	-	37,323	(87,462)
Drainage improvement district 10-01	(294,668)	-	-	-	-	76,594	(371,262)
<u>Total</u>							
NONMAJOR GOVERNMENTAL FUNDS							
Social security	18,595	7,555	-	-	-	7,965	18,185
City's share of specials	18,350	1,562	-	-	-	-	19,912
Gaming fund	3,541	-	-	-	-	-	3,541
Sleepy Hollow	12,397	-	-	-	-	-	12,397
Riverdale	40,775	-	-	-	-	-	40,775
<u>Total</u>	93,658	9,117	-	-	-	7,965	94,810
TOTAL GOVERNMENTAL FUNDS	1,770,772	1,130,192	-	(130,000)	-	754,179	2,016,785
ENTERPRISE FUNDS							
Water and sewer operating - major	49,599	333,977	-	-	-	388,507	(4,931)
Water meter/chem feed building - nonmajor	(67,495)	-	-	-	-	-	(67,495)
<u>TOTAL ENTERPRISE FUNDS</u>	(17,896)	333,977	-	-	-	388,507	(72,426)
TOTAL REPORTING ENTITY	1,752,876	1,464,169	-	(130,000)	-	1,142,686	1,944,359



4334 18th Avenue S.
Ste 101
Fargo, ND 58103-7414

Phone: 701.237.6022
Toll Free: 888.237.6022
Fax: 701.280.1495

INDEPENDENT AUDITOR'S 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

To the City Council
City of Horace
Horace, North Dakota

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the modified cash financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of **City of Horace (City)** as of and for the years ended December 31, 2015 and 2014, and the related notes to the financial statements, which collectively comprise the **City of Horace's** basic financial statements and have issued our report thereon dated September 19, 2016.

Internal Control over Financial Reporting

In planning and performing our audits, we considered **City of Horace'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 opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of **City of Horace's** internal control. Accordingly, we do not express an opinion on the effectiveness of the City'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 weakness or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings and responses, we identified certain deficiencies in internal control that we consider to be material weaknesses and significant deficiencies.

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 statement will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and responses to be material weaknesses: 2015-001, and 2015-005.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiency described in the accompanying schedule of findings and responses to be a significant deficiency: 2015-006.

Compliance and Other Matters


As part of obtaining reasonable assurance about whether **City of Horace'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 audits and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standard* and which are described in the accompanying schedule of findings and responses as items 2015-002, 2015-003, and 2015-004.

City of Horace's Response to Findings

City of Horace's response to the findings identified in our audits is described in the accompanying schedule of findings and responses. **City of Horace's** response was not subjected to the auditing procedures applied in the audits of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is intended solely to describe the scope of our testing of internal control and compliance and the results 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.


Fargo, North Dakota
September 19, 2016

CITY OF HORACE
SCHEDULE OF FINDINGS AND RESPONSES
DECEMBER 31, 2015

SECTION I - SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued:

Governmental activities	Adverse – modified cash basis
Business-type activities	Adverse – modified cash basis
Major governmental funds	Unmodified – modified cash basis
Major proprietary fund	Adverse – modified cash basis
Aggregate remaining fund information	Unmodified – modified cash basis

Internal control over financial reporting:

Material weakness(es) identified?	<u> X </u> yes	<u> </u> no
Significant deficiency(ies) identified that are not considered to be material weakness(es)?	<u> X </u> yes	<u> </u> none reported

Noncompliance material to financial statements noted?

<u> X </u> yes	<u> </u> no
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CITY OF HORACE
SCHEDULE OF FINDINGS AND RESPONSES
DECEMBER 31, 2015

SECTION II – FINANCIAL STATEMENT FINDINGS

FINDING 2015-001 (MATERIAL WEAKNESS) - CAPITAL ASSET RECORDS

Condition

The City of Horace does not maintain capital asset records sufficient for financial reporting purposes under *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments* ("GASB 34"). Furthermore, the City does not have a capital asset policy which includes a capitalization threshold, useful lives and depreciation methods.

Criteria

Accounting principles generally accepted in the United States of America require the financial statements include the capital assets, net of accumulated depreciation. GASB 34 requires that capital asset records include infrastructure constructed after January 1, 2004.

Effect

The omission of capital assets from the financial statements results in an incomplete presentation of the City of Horace's financial statements and an adverse audit opinion on the governmental activities, the business-type activities and the major proprietary fund.

Recommendation

We recommend that the City adopt a capital asset policy, which serves as a guideline for financial reporting of capital assets. We further recommend that the City prepare a schedule of capital assets, complete with accumulated depreciation, in accordance with the City's policies. This is a repeat recommendation.

Views of Responsible Officials

The City Auditor will take steps to prepare a depreciation schedule.

FINDING 2015-002 (MATERIAL NONCOMPLIANCE) – BUDGETS

Condition

The City does not include budgeted amounts for debt service funds in its budget-to-actual financial statements. Moreover, the City's expenditures exceeded the final budget for the general fund in 2015 and the highway fund in 2015 and 2014.

Criteria

NDCC 40-40-05 requires municipalities to budget for the general fund, each special revenue fund, and each debt service fund. Furthermore, NDCC 40-40-15 provides for joint and several liabilities for city council members for overspent budgets.

CITY OF HORACE
SCHEDULE OF FINDINGS AND RESPONSES
DECEMBER 31, 2015

Effect

The City may be in violation of NDCC 40-40-15, and the City Council exposes itself to potential joint and several liabilities for any overspent budgets. Finally, the City's financial statements are exposed to an increased risk of errors and fraud related to expenditures.

Recommendation

We recommend that the City budget for all funds required by NDCC 40-40-05, including all inter-fund transfers. We recommend that the budgetary information for all funds be provided with the City's financial statements for review and approval of responsible officials. We further recommend that the governing board amend the budget for any funds to be overspent. This is a repeat recommendation.

Views of Responsible Officials

The City will begin to budget for all funds and inter-fund transfers.

FINDING 2015-003 (MATERIAL NONCOMPLIANCE) – POSTING OF SPECIAL ASSESSMENTS

Condition

When the City receives special assessments from the county, the assessments are posted to the Street Improvements 93-1 fund. However, payments are paid out of the individual debt service funds. This has resulted in a surplus in the Streets Improvements 93-1 fund and deficit balance in the other debt service funds.

Criteria

The City's bond covenants and NDCC 21-03 require special assessments levied for debt service purposes to be used for that purpose.

Effect

There is a risk of non-compliance with debt covenants and with NDCC 21-03. Also, if the special assessments are used for purposes other than retirement of the related bond issue, the City runs the risk of running out of cash later in the bond repayment process.

Recommendation

We recommend that the City obtain information enabling it to determine the special assessments by special assessment district. We further recommend that the correct amounts of special assessments by district be allocated to the individual debt service funds. This is a repeat recommendation.

Views of Responsible Officials

The City Auditor has begun the process of working with the City's Assessor in an attempt to resolve. Some progress has been made, but still work in process.

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FINDING 2015-004 (MATERIAL NONCOMPLIANCE) – USE OF CAPITAL PROJECTS FUNDS

Condition

It was noted that some of the City's capital projects funds are being utilized to make debt service payments.

Criteria

Bond covenants and NDCC 21-03-08 require bond proceeds to be kept in a fund "separate and distinct from all other funds, to be used for the purpose for which it was borrowed." Bond covenants and NDCC 21-03 refer to the creation of a bond fund or sinking fund, "separate and apart from all other funds of the issuer," to which special assessments should be deposited and from which bond principal and interest payments should be made.

Effect

Special assessments may be improperly used for purposes other than those for which they were levied. Furthermore, the City may be out of compliance with NDCC 21-03-08 and various debt covenants.

Recommendation

We recommend that, for each new improvement project, the City establish both a separate capital projects fund and a separate debt service fund. The bond proceeds should be deposited in the capital projects fund and used only for the purposes for which it was borrowed (i.e., construction and related costs). When the project is complete, any remaining funds should be transferred into the debt service fund.

All special assessments levied for the specific project should be deposited into the debt service fund, and all debt principal and interest payments should be made from the debt service fund.

We further recommend that the City evaluate its current existing funds. It is likely that some of the funds currently classified as capital projects funds are more accurately described as debt service funds for financial reporting purposes. This is a repeat recommendation.

Views of Responsible Officials

The City is implementing this process going forward.

FINDING 2015-005 (MATERIAL WEAKNESS) - SEGREGATION OF DUTIES

Condition

We believe the limited number of personnel prevents a proper segregation of duties to ensure adequate internal control.

Criteria

To ensure adequate internal control over financial reporting and prevent material misstatements due to errors or fraud, there should be a segregation of the functions of approval, custody of assets, posting and reconciliation.

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Effect

The financial statements are susceptible to misstatements due to errors or fraud.

Recommendation

We recommend that management be aware of the lack of segregation of duties and implement controls wherever possible to mitigate this risk. This is a repeat recommendation.

Views of Responsible Officials

The City is aware of this weakness, however, it is not practical at this time to hire sufficient staff to segregate duties. The Auditor will discuss with the Council moving forward.

FINDING 2015-006 (SIGNIFICANT DEFICIENCY) – FINANCIAL STATEMENT PREPARATION

Condition

Widmer Roel PC assists management in preparing financial statements that are presented, including note disclosures, on the modified cash basis of accounting.

Criteria

As a matter of internal control, management should be responsible and capable of preparing financial statements in conformity with generally accepted accounting principles, or as applicable, another comprehensive basis of accounting.

Effect

Without the assistance of the auditors, the financial statements could be materially misstated or omit material financial statement disclosures.

Recommendation

We recommend that management be aware of this condition and be prepared and able to provide all necessary information and schedules to complete the financial statements and disclosures. We further recommend that a responsible official review a current appropriate disclosure checklist or other guidance to ensure the financial statements contain all necessary disclosures. This is a repeat recommendation.

Views of Responsible Officials

The City has noted this as a control weakness.