



CITY OF STURGIS

FINANCIAL STATEMENTS AND INDEPENDENT AUDITOR'S REPORT
DECEMBER 31, 2017

DRAFT



Ketel Thorstenson, LLP

Certified Public Accountants/Business & Personal Consultants

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CITY OF STURGIS

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INDEPENDENT AUDITOR'S REPORT

City Council
City of Sturgis
Sturgis, South 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 STURGIS** (the City), as of and for the year ended December 31, 2017, 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 and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information as of December 31, 2017, and the respective changes in financial position and cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Report on Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 6 through 15, budgetary comparison information on pages 53 through 56, pension information on pages 57 through 58, and notes to required supplementary information on page 59 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 regarding 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.

Report on Supplementary Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's basic financial statements as a whole. The combining nonmajor fund financial statements and schedule of rally activities on pages 61 through 63 are presented for purposes of additional analysis and are not a required part of the financial statements. The combining nonmajor fund financial statements are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. The combining nonmajor fund financial statements have 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 information is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

The schedule of rally activities on page 63 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.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated _____, 2018, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, 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 the City's internal control over financial reporting and compliance.

KETEL THORSTENSON, LLP
Certified Public Accountants

_____, 2018

CITY OF STURGIS

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) DECEMBER 31, 2017

This section of the City of Sturgis' annual financial report presents management's discussion and analysis of the City's financial performance during the fiscal year ended on December 31, 2017. Please read it in conjunction with the City's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

- During the year, the City's revenues generated from charges for services, taxes and other revenues of the governmental programs were \$2,964,610 more than the \$9,501,052 governmental program expenditures. This includes any transfers in/out. The increase is due to an increase in Taxes and in Capital and Operating Grants and Contributions and a decrease in expenditures. Taxes were up 3.80 percent compared to 2016. Capital Grants and Contributions were up 58 percent compared to 2016 primarily because of the Main Street Reconstruction project. The City continues to see growth in construction of homes and businesses during 2017.
- In the City's business-type activities, revenues exceeded expenses by \$1,947,463, which includes transfers and any activity due to the disposal of fixed assets. The increase is due to a 3 percent increase in wastewater fees and the surcharge that was added in July 2017 for the new wastewater project. There were slight decreases in revenue in the Sanitation Fund (landfill fees and rubble site tickets), Ambulance Fund, and Liquor Fund compared to 2016. The Water Fund had very little change in revenue from 2016. Expenses were higher in Wastewater and Sanitation, but down in Liquor Fund, Water Fund, and Ambulance Fund. Overall expenses in the business-type activities were lower by 4 percent compared to 2016.

OVERVIEW OF THE FINANCIAL STATEMENTS

The financial report is presented in a format consistent with the presentation requirements of the Governmental Accounting Standards Board (GASB) Statement 34.

This annual report consists of three parts – management's discussion and analysis (this section), the basic financial statements (including related notes), and required supplementary information. The basic financial statements include two kinds of statements that present different views of the City:

- The first two statements are government-wide financial statements that provide both long-term and short-term information about the City's overall financial status.
- The remaining statements are fund financial statements that focus on individual parts of the City government, reporting the City's operations in more detail than the government-wide statements.
- The governmental funds statements tell how general government services like public safety were financed in the short-term, as well as what remains for future spending.
- Proprietary fund statements offer short-term and long-term financial information about the activities that the City operates like businesses. The City has five proprietary funds – the Liquor Fund, Water Fund, Wastewater Fund, Sanitation Fund and Ambulance Fund.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of required supplementary information that further explains and supports the information in the financial statements. In addition to the required elements, we have included a section with combining statements that provide details about our non-major governmental funds, each of which are added together and presented in a single column in the basic financial statements.

CITY OF STURGIS

**MANAGEMENT’S DISCUSSION AND ANALYSIS (UNAUDITED) (CONTINUED)
DECEMBER 31, 2017**

OVERVIEW OF THE FINANCIAL STATEMENTS (CONTINUED)

Figure A-1 summarizes the major features of the City’s financial statements, including the portion of the City government they cover and the types of information they contain. The remainder of the overview section of the management’s discussion and analysis explains the structure and contents of each of the statements.

Figure A-1

	Government-wide Statements	Fund Statements	
		Governmental Funds	Proprietary Funds
Scope	Entire City government (except fiduciary funds and the fiduciary component units)	The activities of the City that are not proprietary or fiduciary, such as finance office, police, fire and parks	Activities the City operates similar to private businesses, such as the water and sewer systems
Required Financial Statements	Statement of Net Position and Statement of Activities	Balance Sheet and Statement of Revenues, Expenditures, and Changes in Fund Balances	Statement of Net Position; Statement of Revenues, Expenses, and Changes in Net Position; and Statement of Cash Flows
Accounting Basis and Measurement Focus	Accrual accounting and economic resources focus	Modified accrual accounting and current financial resources focus	Accrual accounting and economic resources focus
Type of Asset/Liability Information	All assets and liabilities, both financial and capital, and short-term and long-term	Only assets expected to be used up and liabilities that come due during the year or soon thereafter, no capital assets included	All assets and liabilities, both financial and capital, and short-term and long-term
Type of Inflow/Outflow Information	All revenues and expenses during year, regardless of when cash is received or paid	Revenues for which cash is received during or soon after the end of the year; expenditures when goods or services have been received and payment is due during the year or soon thereafter	All revenues and expenses during year, regardless of when cash is received or paid

Government-wide Statements

The government-wide statements report information about the City as a whole using accounting methods similar to those used by private-sector companies. The statement of net position includes all of the government’s assets and liabilities. All of the current year’s revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

CITY OF STURGIS

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) (CONTINUED) DECEMBER 31, 2017

OVERVIEW OF THE FINANCIAL STATEMENTS (CONCLUDED)

Government-wide Statements (Continued)

The two government-wide statements report the City's net position and how they have changed. Net position – the difference between the City's assets and liabilities – is one way to measure the City's financial health or position.

- Increases or decreases in the City's net position are an indicator of whether its financial health is improving or deteriorating, respectively.
- To assess the overall health of the City you need to consider additional non-financial factors such as changes in the City's property tax base and changes in the sales tax revenue base.

The government-wide financial statements of the City are reported in two categories:

- **Governmental Activities** -- This category includes most of the City's basic services, such as police, fire, public works, parks department and general administration. Property taxes, sales taxes, charges for services, state and federal grants, and interest earnings finance most of these activities.
- **Business-type Activities** -- The City charges a fee to customers to help cover the costs of certain services it provides. The City's liquor, water, wastewater, sanitation, and ambulance funds are included here.

Fund Financial Statements

The fund financial statements provide more detailed information about the City's most significant funds – not the City as a whole. Funds are accounting devices that the City uses to keep track of specific sources of funding and spending for particular purposes. State law requires some of the funds. The City Council establishes other funds to control and manage money for particular purposes or to show that it is properly using certain taxes and grants.

The City has two kinds of funds:

- **Governmental Funds** – Most of the City's basic services are included in the governmental funds, which focus on (1) how cash and other financial assets that can readily be converted to cash flow in and out and (2) the balances left at the year-end that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs. Because this information does not encompass the additional long-term focus of the government-wide statements, we provide additional information at the bottom of the governmental funds' statements, or on the subsequent page, that explains the relationship (or differences) between them.
- **Proprietary Funds** – Services for which the City charges customers a fee are generally reported in proprietary funds. Proprietary funds, like the government-wide statements, provide both short-term and long-term financial information. The City's enterprise funds are the same as its business-type activities, but provide more detail and additional information, such as cash flows.

CITY OF STURGIS

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) (CONTINUED)
DECEMBER 31, 2017**

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

Net Position

The City's combined net position increased nine percent between fiscal year 2016 and 2017. (See Table A-1).

Table A-1 Summarized Statement of Net Position						
	Governmental Activities		Business-Type Activities		Total	
	<u>2017</u>	<u>2016</u>	<u>2017</u>	<u>2016</u>	<u>2017</u>	<u>2016</u>
Current and Other Assets	\$ 4,936,508	\$ 4,019,885	\$ 4,148,552	\$ 3,601,786	\$ 9,085,060	\$ 7,621,671
Capital Assets	42,006,046	37,809,133	26,673,658	24,410,309	68,679,704	62,219,442
Total Assets	\$46,942,554	\$ 41,829,018	\$ 30,822,210	\$ 28,012,095	\$ 77,764,764	\$ 69,841,113
Pension Related Deferred Outflows	\$ 1,203,184	\$ 1,247,194	\$ 654,739	\$ 671,694	\$ 1,857,923	\$ 1,918,888
Long-Term Debt	\$ 7,053,789	\$ 5,583,087	\$ 8,828,880	\$ 7,536,523	\$ 15,882,669	\$ 13,119,610
Other Liabilities	1,576,125	941,911	668,670	1,115,330	2,244,795	2,057,241
Total Liabilities	\$ 8,629,914	\$ 6,524,998	\$ 9,497,550	\$ 8,651,853	\$ 18,127,464	\$ 15,176,851
<i>Net Position:</i>						
Net Investment in Capital Assets	\$35,166,804	\$ 32,442,911	\$ 17,958,805	\$ 16,977,996	\$ 53,125,609	\$ 49,420,907
Restricted	3,384,401	3,689,900	703,828	415,095	4,088,229	4,104,995
Unrestricted	964,619	418,403	3,316,766	2,638,845	4,281,385	3,057,248
Total Net Position	\$39,515,824	\$ 36,551,214	\$ 21,979,399	\$ 20,031,936	\$ 61,495,223	\$ 56,583,150
Beginning Net Position	\$36,551,214	\$ 37,149,938	\$ 20,031,936	\$ 18,741,690	\$ 56,583,150	\$ 55,891,628
Increase in Net Position	\$ 2,964,610	\$ (598,724)	\$ 1,947,463	\$ 1,290,246	\$ 4,912,073	\$ 691,522
Percentage of Increase in Net Position	8%	-2%	10%	7%	9%	1%

The Statement of Net Position reports all financial and capital resources. The statement presents the assets and liabilities in order of relative liquidity. The liabilities with average maturities greater than one year are reported in two components – the amount due within one year and the amount due in more than one year. The difference between the City's assets and liabilities is its net position.

CITY OF STURGIS

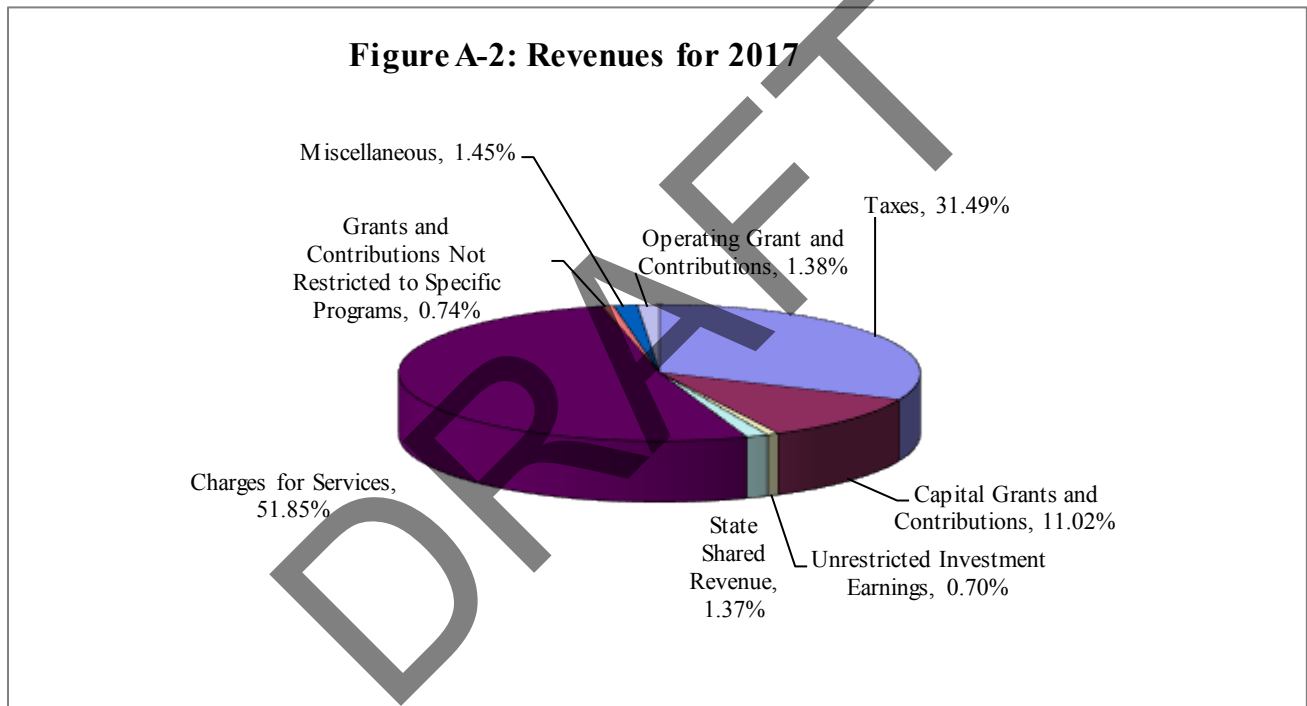
**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) (CONTINUED)
DECEMBER 31, 2017**

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONTINUED)

Changes in Net Position

The City's revenues totaled \$21,375,629 (See Table A-2). Well over half of the City's revenue comes from charges for services and taxes, with 52 cents of every dollar raised coming from charges for services (primarily liquor and water operations) and 31 cents of every dollar raised coming from some type of tax (See Figure A-2). The other seventeen percent of the City's total revenue comes from state and federal grants for capital purposes, operating grants, contributions, state shared revenue, interest and miscellaneous.

The total cost of all programs and services was \$16,463,556 (See Table A-2). The City's expenses cover a range of services, including road maintenance, parks and recreation services and sewer system services. (See Figure A-3).

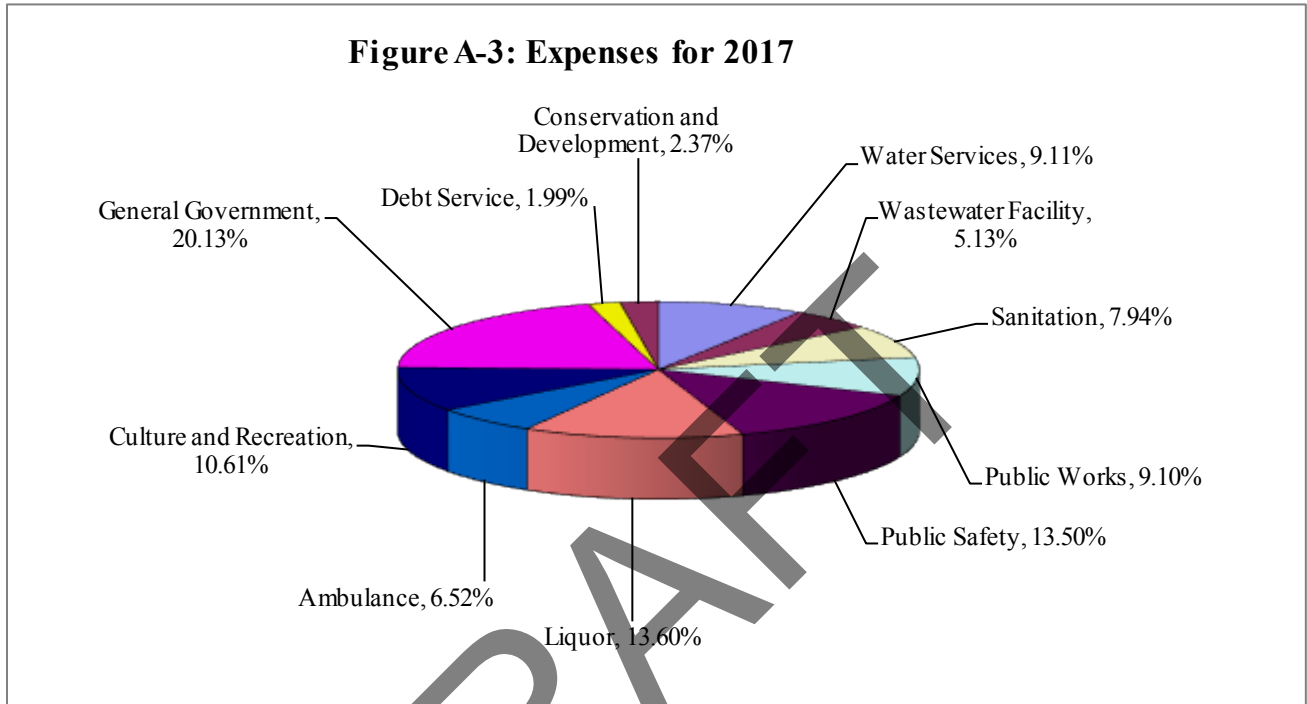


CITY OF STURGIS

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) (CONTINUED)
DECEMBER 31, 2017**

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONTINUED)

Changes in Net Position (Continued)



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CITY OF STURGIS

MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) (CONTINUED)
DECEMBER 31, 2017

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONTINUED)

Changes in Net Position (Concluded)

Table A-2 and the narrative that follows consider the operations of the governmental and business - type activities.

Table A-2 Changes in Net Position						
	Governmental Activities		Business - Type Activities		Total	
	2017	2016	2017	2016	2017	2016
Revenues						
Program Revenues						
Charges for Services	\$ 2,808,904	\$ 2,731,165	\$ 8,274,299	\$ 7,904,216	\$ 11,083,203	\$ 10,635,381
Operating Grants and Contributions	295,846	29,513	-	-	295,846	29,513
Capital Grants and Contributions	2,354,491	25,212	-	-	2,354,491	25,212
General Revenues						
Taxes	6,731,027	6,479,143	-	-	6,731,027	6,479,143
State Shared Revenue	292,636	281,111	-	-	292,636	281,111
Grants and Contributions not Program Specific	158,463	21,320	-	34,385	158,463	55,705
Unrestricted Investment Earnings	140,532	161,869	9,821	10,724	150,353	172,593
Miscellaneous	143,968	127,301	165,642	93,667	309,610	220,968
Total Revenues	12,925,867	9,856,634	8,449,762	8,042,992	21,375,629	17,899,626
Expenses						
General Government	3,314,816	3,513,661	-	-	3,314,816	3,513,661
Public Safety	2,222,402	2,435,561	-	-	2,222,402	2,435,561
Public Works	1,497,735	1,530,814	-	-	1,497,735	1,530,814
Culture and Recreation	1,747,229	2,023,419	-	-	1,747,229	2,023,419
Conservation and Development	390,772	273,209	-	-	390,772	273,209
Debt Service	328,098	250,158	-	-	328,098	250,158
Liquor	-	-	2,238,959	2,256,085	2,238,959	2,256,085
Water Services	-	-	1,499,234	1,551,409	1,499,234	1,551,409
Wastewater Services	-	-	844,215	794,859	844,215	794,859
Sanitation Services	-	-	1,306,410	1,273,133	1,306,410	1,273,133
Ambulance	-	-	1,073,686	1,305,796	1,073,686	1,305,796
Total Expenses	9,501,052	10,026,822	6,962,504	7,181,282	16,463,556	17,208,104
Excess Before Transfers	3,424,815	(170,188)	1,487,258	861,710	4,912,073	691,522
Transfers	(460,205)	(428,536)	460,205	428,536	-	-
Increase (Decrease) in Net Position	2,964,610	(598,724)	1,947,463	1,290,246	4,912,073	691,522
Ending Net Position	\$ 39,515,824	\$ 36,551,214	\$ 21,979,399	\$ 20,031,936	\$ 61,495,223	\$ 56,583,150

CITY OF STURGIS

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) (CONTINUED)
DECEMBER 31, 2017**

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONCLUDED)

Governmental Activities

Total revenues of the governmental activities for the City increased 31 percent compared to the prior year, while total expenses decreased by 5 percent. The City is seeing growth in sales tax and in Rally sponsorships, while the expenses decrease in many of the departments. Overall, 2017 was a good year and continue to see growth in tourism, construction, and economic development.

Business-Type Activities

Operating revenues of the City's business-type activities increased by 5 percent compared to the prior year, while expenses decreased by 3 percent. The overall increase in revenues is due to the increase in fees, the economic growth, and the surcharge in the Wastewater Fund. Decrease in expenses is also due to better liquor store inventory management and decreased wages in the Ambulance Fund.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

The financial analysis of the City's funds mirror those highlighted in the analysis of governmental and business-type activities presented above. The City maintains governmental fund types - General, Special Revenue Funds (including the Capital Improvement, Revolving Loan, and Business Improvement District Funds), Debt Service Funds, Capital Projects Funds and Permanent Funds. The City also maintains five business type funds - Liquor, Water, Wastewater, Sanitation and Ambulance Funds.

BUDGETARY HIGHLIGHTS

Over the course of the year, the City Council revised the City budget three times. These amendments fall into two categories:

- Move contingency money to funds to prevent budget overruns
- Supplemental appropriations to increase the budget to prevent budget overruns

CITY OF STURGIS

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) (CONTINUED)
DECEMBER 31, 2017**

CAPITAL ASSET ADMINISTRATION

By the end of 2017, the City had invested \$68,679,704 in a broad range of capital assets, including, land, buildings, and various machinery and equipment. (See Table A-3). This amount represents a net increase (including additions and deductions) of \$6,460,262, primarily due to the completion of TIF #12, Dolan Creek Housing project; the completion of the Main Street Project; completion of the Wastewater Screen project, improvements to the Community Center; completion of Ft. Meade Trail and the Stone Shelter.

	Governmental Activities		Business-type Activities	
	2017	2016	2017	2016
Land	\$ 2,923,815	\$ 2,923,815	\$ 738,681	\$ 738,681
Construction Work in Progress	3,895,047	382,541	2,269,008	1,578,765
Buildings	8,546,120	8,707,116	1,450,389	1,511,024
Improvements Other Than Buildings	24,683,864	23,924,056	21,176,565	19,435,066
Machinery and Equipment	1,957,200	1,871,605	1,039,015	1,146,773
Total Capital Assets	\$ 42,006,046	\$ 37,809,133	\$ 26,673,658	\$ 24,410,309

LONG-TERM DEBT

At year-end the City had \$15,882,669 in Sales Tax Revenue Bonds, Contract Payable, General Obligation Bonds and other long-term obligations. This is an increase of \$2,763,059 as shown on Table A-4 below.

	Governmental Activities		Business-type Activities	
	2017	2016	2017	2016
Compensated Absences	\$ 214,547	\$ 216,865	\$ 77,536	\$ 86,676
Tax Increment Financing Obligations	1,750,000	1,548,801	-	-
Notes Payable	5,089,242	997,421	2,819,929	712,501
Sales Tax Revenue Bonds	-	2,820,000	5,931,415	6,137,346
General Obligation Bonds	-	-	-	600,000
Total Outstanding Debt and Obligations	\$ 7,053,789	\$ 5,583,087	\$ 8,828,880	\$ 7,536,523

During the current year, the City obtained additional financing through a Pioneer Bank and will begin making regular payments in 2018. The additional financing was for the Wastewater Screen Project and the East Annex sewer line. The City paid off the 2010 general obligation bonds for the Wastewater and Water Funds. The City received an additional loan from Pioneer Bank for the Main Street Project and several other governmental capital improvement projects. The City will make interest only payments until the projects are completed. The City made schedule payments throughout the year on other debt balances.

CITY OF STURGIS

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED) (CONCLUDED)
DECEMBER 31, 2017**

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The City's current economic position has remained strong and is growing. There was an increase in total property valuation of \$3,348,753. The City requested a 6% increase in property tax for the year of 2017 payable in 2018. The growth factor of 2016 taxes payable in 2017 was 3.33%. The growth factor for 2017 taxes payable in 2018 was 2.4%.

The adopted 2018 general fund expenditures budget increased by 4%. The increase is primarily due to wage increases.

The City's business-type activities, sanitation fees will not increase in 2018. The Liquor Fund anticipates an 8 to 10 percent increase in revenue over 2017. The Ambulance Fund anticipates revenue to remain comparable to recent years.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the City's finances and to demonstrate the City's accountability for the money it receives. If you have questions about this report or need additional information, contact the City of Sturgis' Finance Office, 1040 Harley-Davidson Way, Suite 103, Sturgis, SD 57785.

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CITY OF STURGIS

STATEMENT OF NET POSITION
DECEMBER 31, 2017

	GOVERNMENTAL		BUSINESS-TYPE	
	ACTIVITIES	ACTIVITIES		TOTAL
Assets				
Cash and Cash Equivalents (Note 2)	\$ 3,476,908	\$ 2,272,484	\$	5,749,392
Receivables, Net	913,513	698,610		1,612,123
Notes Receivable (Note 10)	413,390	-		413,390
Internal Balances (Note 6)	(666,368)	666,368		-
Inventories	-	447,223		447,223
Other Assets	38,591	14,778		53,369
Investment Real Estate Held for Sale	608,100	-		608,100
Restricted Assets:				
Cash with Fiscal Agent (Note 5)	-	42,720		42,720
Deposits (Note 9)	135,844	-		135,844
Net Pension Asset (Note 8)	16,530	6,369		22,899
Capital Assets (Note 4)				
Land and Construction Work in Progress	6,818,862	3,007,689		9,826,551
Other Capital Assets, Net of Depreciation	35,187,184	23,665,969		58,853,153
Total Assets	46,942,554	30,822,210		77,764,764
Deferred Outflows of Resources				
Pension Related Deferred Outflows of Resources (Note 8)	1,203,184	654,739		1,857,923
Total Assets and Deferred Outflows of Resources	\$ 48,145,738	\$ 31,476,949	\$	79,622,687
Liabilities				
Accounts Payable	\$ 1,430,180	\$ 423,983	\$	1,854,163
Other Current Liabilities	145,945	244,687		390,632
Noncurrent Liabilities (Note 5):				
Due Within One Year	458,142	412,699		870,841
Due in More Than One Year	6,595,647	8,416,181		15,011,828
Total Liabilities	8,629,914	9,497,550		18,127,464
Net Position				
Net Investment in Capital Assets	35,166,804	17,958,805		53,125,609
Restricted for:				
Debt Service	-	42,720		42,720
SDPAA (Note 9)	135,844	-		135,844
Revolving Loans	496,231	-		496,231
BID Tax	201	-		201
BBB Tax	753,869	-		753,869
Library Purposes	269,987	-		269,987
SDRS Pension (Note 8)	1,219,714	661,108		1,880,822
Permanently Restricted Purposes:				
Expendable	131,020	-		131,020
Nonexpendable	377,535	-		377,535
Unrestricted	964,619	3,316,766		4,281,385
Total Net Position	39,515,824	21,979,399		61,495,223
Total Liabilities and Net Position	\$ 48,145,738	\$ 31,476,949	\$	79,622,687

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2017

	Program Revenues				Net (Expense) Revenue and		Total
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Changes in Net Position		
					Governmental Activities	Business-Type Activities	
Functions/Programs							
Primary Government							
Governmental Activities:							
General Government	\$ 3,314,816	\$ 2,444,718	\$ 7,209	\$ 875,300	\$ 12,411	\$ -	\$ 12,411
Public Safety	2,222,402	53,010	38,637	-	(2,130,755)	-	(2,130,755)
Public Works	1,497,735	39,934	-	1,435,203	(22,598)	-	(22,598)
Health and Welfare	-	7,981	-	-	7,981	-	7,981
Culture and Recreation	1,747,229	263,261	250,000	18,631	(1,215,337)	-	(1,215,337)
Conservation and Development	390,772	-	-	25,357	(365,415)	-	(365,415)
Interest on Long-Term Debt	328,098	-	-	-	(328,098)	-	(328,098)
Total Governmental Activities	9,501,052	2,808,904	295,846	2,354,491	(4,041,811)	-	(4,041,811)
Business-Type Activities:							
Liquor	2,238,959	2,358,673	-	-	-	119,714	119,714
Water	1,499,234	1,850,678	-	-	-	351,444	351,444
Wastewater	844,215	1,741,488	-	-	-	897,273	897,273
Sanitation	1,306,410	1,364,324	-	-	-	57,914	57,914
Ambulance	1,073,686	959,136	-	-	-	(114,550)	(114,550)
Total Business-Type Activities	6,962,504	8,274,299	-	-	-	1,311,795	1,311,795
Total Primary Government	\$ 16,463,556	\$ 11,083,203	\$ 295,846	\$ 2,354,491	(4,041,811)	1,311,795	(2,730,016)
General Revenues:							
Taxes:							
Property Taxes					2,902,537	-	2,902,537
Sales Taxes					3,828,490	-	3,828,490
State Shared Revenue					292,636	-	292,636
Grants and Contributions Not Restricted to Specific Programs							
					158,463	-	158,463
Unrestricted Investment Earnings					140,532	9,821	150,353
Miscellaneous Revenue					143,968	165,642	309,610
Transfers					(460,205)	460,205	-
Total General Revenues and Transfers					7,006,421	635,668	7,642,089
Change in Net Position					2,964,610	1,947,463	4,912,073
Net Position, Beginning					36,551,214	20,031,936	56,583,150
Net Position, Ending					\$ 39,515,824	\$ 21,979,399	\$ 61,495,223

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

BALANCE SHEET - GOVERNMENTAL FUNDS
DECEMBER 31, 2017

	General Fund	Capital Improvement Fund	Revolving Loan Fund
Assets			
101 Cash (Note 2)	\$ 170,953	\$ 219,201	\$ 201,008
105 Savings Certificates (Note 2)	718,691	546,172	229,323
108 Property Taxes Receivable	99,694	-	-
108 Sales Tax Receivable	183,676	138,562	-
115 Accounts Receivable, Net	46,593	-	65,900
121 Special Assessments Receivable	-	-	-
128 Notes Receivable (Note 10)	-	1,804	411,586
131 Due from Other Funds (Note 6)	633,599	259,625	-
132 Due from Federal/State Government	91,609	235,507	-
133 Advance to Other Funds (Note 6)	1,092,484	-	400,000
151 Investment Held for Sale	-	-	-
154.1 Restricted Deposits (Note 9)	135,844	-	-
155 Prepaid Expense	38,591	-	-
Total Assets	\$ 3,211,734	\$ 1,400,871	\$ 1,307,817
Liabilities, Deferred Inflows of Resources and Fund Balances			
<i>Liabilities</i>			
202 Accounts Payable	\$ 201,522	\$ 1,223,415	\$ -
208 Due to Other Funds (Note 6)	-	-	-
216 Accrued Wages Payable	80,114	-	-
217 Accrued Taxes Payable	2,144	-	-
220 Deposits	2,700	-	-
236 Advance from Other Funds (Note 6)	-	810,000	-
Total Liabilities	286,480	2,033,415	-
<i>Deferred Inflows of Resources</i>			
245 Unavailable Revenue - Property Taxes	84,107	-	-
246 Unavailable Revenue - Special Assessments	-	-	-
Total Deferred Inflows of Resources	84,107	-	-
<i>Fund Balances (Deficits) (Note 1)</i>			
263 Nonspendable	1,266,919	1,804	811,586
264 Restricted	-	-	496,231
265 Committed	134,742	-	-
266 Assigned	89,201	-	-
267 Unassigned	1,350,285	(634,348)	-
Total Fund Balances (Deficits)	2,841,147	(632,544)	1,307,817
Total Liabilities, Deferred Inflows of Resources and Fund Balances	\$ 3,211,734	\$ 1,400,871	\$ 1,307,817

The accompanying notes are an integral part of the financial statements.

<u>TIF Funds</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
\$ 491,614	\$ 472,411	\$ 1,555,187
-	427,535	1,921,721
-	-	99,694
-	22,929	345,167
-	4,631	117,124
-	24,412	24,412
-	-	413,390
-	-	893,224
-	-	327,116
-	-	1,492,484
-	608,100	608,100
-	-	135,844
-	-	38,591
\$ 491,614	\$ 1,560,018	\$ 7,972,054

\$ 3,365	\$ 1,878	\$ 1,430,180
167,841	-	167,841
-	962	81,076
-	154	2,298
-	-	2,700
2,074,235	-	2,884,235
2,245,441	2,994	4,568,330

-	-	84,107
-	24,412	24,412
-	24,412	108,519

-	377,535	2,457,844
-	1,155,077	1,651,308
-	-	134,742
-	-	89,201
(1,753,827)	-	(1,037,890)
(1,753,827)	1,532,612	3,295,205

\$ 491,614	\$ 1,560,018	\$ 7,972,054
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CITY OF STURGIS

**RECONCILIATION OF GOVERNMENTAL FUNDS BALANCE SHEET
TO GOVERNMENT-WIDE STATEMENT OF NET POSITION
DECEMBER 31, 2017**

Total Fund Balances - Governmental Funds \$ 3,295,205

Amounts reported for governmental activities in the Statement of Net Position are different because:

Capital assets used in governmental activities are not current financial resources and therefore are not reported in the funds. 42,006,046

Net pension asset reported in governmental activities is not an available financial resource and therefore is not reported in the funds. 16,530

Pension related deferred outflows are components of pension asset and therefore are not reported in the funds. 1,203,184

Long-term liabilities, including bonds payable, tax increment financing obligations, and compensated absences are not due and payable in the current period and therefore not reported in the funds. (7,053,789)

Accrued interest on long-term debt is not due and payable in the current period and therefore is not reported in the funds. (59,871)

Assets such as delinquent taxes receivable, special assessments, and grants are not available to pay for current period expenditures and therefore are deferred in the funds. 108,519

Total Net Position - Governmental Activities \$ 39,515,824

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
 GOVERNMENTAL FUNDS
 FOR THE YEAR ENDED DECEMBER 31, 2017

		<u>General</u> <u>Fund</u>	<u>Capital</u> <u>Improvement</u> <u>Fund</u>	<u>Revolving</u> <u>Loan</u> <u>Fund</u>	<u>TIF</u> <u>Funds</u>	<u>Other</u> <u>Governmental</u> <u>Funds</u>	<u>Total</u> <u>Governmental</u> <u>Funds</u>
Revenue							
<i>Taxes:</i>							
311	General Property Taxes (Note 3)	\$ 2,848,336	\$ -	\$ -	\$ 47,664	\$ -	\$ 2,896,000
313	General Sales and Use Taxes	1,987,248	1,496,889	-	-	344,353	3,828,490
315	Amusement Taxes	1,092	-	-	-	-	1,092
319	Penalties and Interest on Delinquent Taxes	12,007	-	-	-	204	12,211
320	Licenses and Permits	643,482	-	-	-	-	643,482
<i>Intergovernmental Revenue:</i>							
331	Federal Grants	53,542	1,005,705	-	-	-	1,059,247
334	State Grants	6,107	665,695	-	-	-	671,802
335.01	Bank Franchise Tax	12,082	-	-	-	-	12,082
335.03	Liquor Tax Reversion	43,057	-	-	-	-	43,057
335.04	Motor Vehicle Licenses	91,834	-	-	-	-	91,834
335.08	Local Government Highway and Bridge Fund	145,663	-	-	-	-	145,663
338.02	County Highway and Bridge Reserve Tax	5,855	-	-	-	-	5,855
338.04	Port of Entry	29,046	-	-	-	-	29,046
338.99	Other	5,033	-	-	-	-	5,033
<i>Charges for Goods and Services:</i>							
341	General Government	1,630,736	153,500	-	-	17,000	1,801,236
342	Public Safety	44,880	-	-	-	-	44,880
345	Health	7,981	-	-	-	-	7,981
346	Culture and Recreation	263,261	-	-	-	-	263,261
349	Other	7,787	-	-	-	-	7,787
<i>Fines and Forfeits:</i>							
351	Court Fines and Costs	8,130	-	-	-	-	8,130
<i>Miscellaneous Revenue:</i>							
361	Investment Earnings	125,934	-	9,606	-	4,992	140,532
362	Rentals/Airport Hangar Lease	17,716	-	-	-	-	17,716
363	Special Assessments	-	-	-	-	25,051	25,051
367	Contributions and Donations from Private Sources	131,463	27,000	-	-	-	158,463
369	Other	10,196	25,000	-	-	80,588	115,784
Total Revenue		8,132,468	3,373,789	9,606	47,664	472,188	12,035,715

CITY OF STURGIS

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES (CONTINUED)
 GOVERNMENTAL FUNDS
 FOR THE YEAR ENDED DECEMBER 31, 2017

	<u>General Fund</u>	<u>Capital Improvement Fund</u>	<u>Revolving Loan Fund</u>	<u>TIF Funds</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Expenditures						
<i>General Government:</i>						
411 Legislative	215,933	-	-	-	-	215,933
414 Financial Administration	1,242,328	4,436	-	-	-	1,246,764
419 Other (Note 11)	1,688,466	177,066	-	-	54,842	1,920,374
<i>Public Safety:</i>						
421 Police	1,994,028	-	-	-	-	1,994,028
422 Fire	131,406	21,297	-	-	-	152,703
<i>Public Works:</i>						
431 Highway and Streets	808,168	33,659	-	8,289	-	850,116
435 Airport	60,879	-	-	-	-	60,879
437 Cemeteries	105,840	-	-	-	-	105,840
<i>Culture and Recreation:</i>						
451 Recreation	727,442	10,443	-	-	-	737,885
452 Parks	474,481	-	-	-	-	474,481
455 Library	330,688	-	-	-	-	330,688
456 Auditorium	21,922	-	-	-	-	21,922
460 Conservation and Development	-	-	14,399	-	376,373	390,772
470 Debt Service	-	3,259,905	-	103,011	-	3,362,916
485 Capital Outlay	264,732	4,604,146	-	201,199	-	5,070,077
Total Expenditures	8,066,313	8,110,952	14,399	312,499	431,215	16,935,378
Excess of Revenue Over (Under)						
Expenditures	66,155	(4,737,163)	(4,793)	(264,835)	40,973	(4,899,663)
Other Financing Sources (Uses)						
391 Transfers In (Note 7)	110,000	75,975	-	-	-	185,975
391 Compensation for Loss or Damage to Capital Assets	2,681	-	-	-	-	2,681
391.29 Other Long-Term Debt Issued	-	4,333,313	-	201,199	-	4,534,512
511 Transfers Out (Note 7)	(87,975)	-	-	-	-	(87,975)
Total Other Financing Sources (Uses)	24,706	4,409,288	-	201,199	-	4,635,193
Net Change in Fund Balances (Deficit)	90,861	(327,875)	(4,793)	(63,636)	40,973	(264,470)
Fund Balance (Deficit), December 31, 2016	2,750,286	(304,669)	1,312,610	(1,690,191)	1,491,639	3,559,675
Fund Balance (Deficit), December 31, 2017	\$ 2,841,147	\$ (632,544)	\$ 1,307,817	\$ (1,753,827)	\$ 1,532,612	\$ 3,295,205

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

RECONCILIATION OF GOVERNMENTAL FUNDS STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES TO GOVERNMENT-WIDE STATEMENT OF ACTIVITIES FOR THE YEAR ENDED DECEMBER 31, 2017

Net Change in Fund Balances - Total Government Funds \$ (264,470)

Amounts reported for governmental activities in the Statement of Activities are different because:

Governmental funds report capital outlays as expenditures. However, in the Statement of Activities the cost of those assets is allocated over their estimated lives and reported as depreciation expense.	3,861,187
Capital assets contributed to the City are included in the Statement of Activities as capital outlay expenditures and capitalized in the Statement of Net Position.	893,931
Capital assets transferred to water and sewer proprietary funds.	(558,205)
Governmental funds report property taxes and special assessments as revenue when funds become available, but the Statement of Activities includes the property tax and special assessments as revenue when earned.	(6,460)
Repayment of bond principal, tax increment financing, and long-term debt are expenditures in the governmental funds, but the repayment reduces long-term liabilities in the Statement of Net Position.	3,061,492
Borrowings on long-term debt is an other financing source in the governmental funds, but increases long-term debt in the Statement of Net Position.	(4,534,512)
Governmental funds do not reflect the change in accrued leave, but the Statement of Activities reflects the change in accrued leave through expenditures.	2,318
Accrued interest on long-term debt is not due and payable in the current period and therefore is not reported in the funds. The amount represents the change in accrued interest during the current period.	(26,674)
Changes in the pension related deferred outflows, pension asset and related pension expenses are not reported in the governmental fund statements.	319,608
Pension expense reported in the Statement of Activities does not require the use of current financial resources and is not reported as expenditures in the governmental funds.	216,395

Change in Net Position of Governmental Activities \$ 2,964,610

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

STATEMENT OF NET POSITION
PROPRIETARY FUNDS
DECEMBER 31, 2017

Assets and Deferred Outflows of Resources	Liquor Fund	Water Fund	Wastewater Fund	Sanitation Fund	Ambulance Fund	Total Proprietary Funds
Current Assets						
101 Cash (Note 2)	\$ 4,820	\$ 799,768	\$ 700,055	\$ 767,841	\$ -	\$ 2,272,484
107 Restricted Cash (Note 5)	28,686	14,034	-	-	-	42,720
115 Accounts Receivable, Net	160	138,671	186,497	69,760	298,422	693,510
131 Due from Other Governments	-	-	-	-	5,100	5,100
142 Inventory of Supplies Purchased for Resale	447,223	-	-	-	-	447,223
155 Prepaid Expenses	3,046	3,204	1,601	3,203	3,724	14,778
Total Current Assets	483,935	955,677	888,153	840,804	307,246	3,475,815
Noncurrent Assets						
133 Advance to Other Funds (Note 6)	-	1,391,751	-	-	-	1,391,751
189 Net Pension Asset (Note 8)	698	1,101	967	1,380	2,223	6,369
Capital Assets (Note 4)						
160 Land	6,500	1,800	646,214	84,167	-	738,681
162 Buildings	826,042	181,183	445,257	310,994	359,809	2,123,285
163 Accumulated Depreciation - Buildings	(175,221)	(77,361)	(215,113)	(108,652)	(96,549)	(672,896)
164 Improvements Other Than Buildings	-	18,136,683	12,649,735	22,789	-	30,809,207
165 Accumulated Depreciation - Improvements Other Than Buildings	-	(5,546,071)	(4,068,654)	(17,917)	-	(9,632,642)
166 Machinery and Equipment	55,030	837,256	694,834	2,416,772	1,083,410	5,087,302
167 Accumulated Depreciation - Machinery and Equipment	(21,311)	(660,002)	(611,116)	(2,092,734)	(663,124)	(4,048,287)
168 Construction in Progress	-	164,992	2,104,016	-	-	2,269,008
Total Noncurrent Assets	691,738	14,431,332	11,646,140	616,799	685,769	28,071,778
Total Assets	1,175,673	15,387,009	12,534,293	1,457,603	993,015	31,547,593
Deferred Outflows of Resources						
196 Pension Related Deferred Outflows (Note 8)	41,669	85,880	111,708	146,758	268,724	654,739
Total Assets and Deferred Outflows of Resources	\$ 1,217,342	\$ 15,472,889	\$ 12,646,001	\$ 1,604,361	\$ 1,261,739	\$ 32,202,332

Liabilities and Net Position	Liquor Fund	Water Fund	Wastewater Fund	Sanitation Fund	Ambulance Fund	Total Proprietary Funds
Current Liabilities						
202 Accounts Payable	\$ 136,888	\$ 16,851	\$ 239,121	\$ 20,538	\$ 10,585	\$ 423,983
208 Due to Other Funds (Note 6)	48,934	-	-	-	676,449	725,383
215 Accrued Interest Payable	14,551	17,794	1,268	-	-	33,613
216 Accrued Wages Payable	4,740	8,339	4,750	8,236	12,534	38,599
217 Accrued Taxes Payable	15,870	-	-	-	-	15,870
220 Customer Deposits	-	156,605	-	-	-	156,605
226 Bonds Payable - Current (Note 5)	11,281	186,067	137,815	-	-	335,163
233 Accrued Leave Payable (Note 5)	892	25,967	24,607	21,596	4,474	77,536
Total Current Liabilities	233,156	411,623	407,561	50,370	704,042	1,806,752
Long-Term Liabilities						
231 Bonds Payable (Note 5)	716,250	4,815,005	2,884,926	-	-	8,416,181
Total Long-Term Liabilities	716,250	4,815,005	2,884,926	-	-	8,416,181
Total Liabilities	949,406	5,226,628	3,292,487	50,370	704,042	10,222,933
Net Position						
253.10 Net Investment in Capital Assets	-	8,037,408	8,622,432	615,419	683,546	17,958,805
253.21 Restricted for Revenue Bond Debt Service (Note 5)	28,686	14,034	-	-	-	42,720
253.29 Restricted for SDRS Pension Purposes (Note 8)	42,367	86,981	112,675	148,138	270,947	661,108
253.9 Unrestricted (Deficit)	196,883	2,107,838	618,407	790,434	(396,796)	3,316,766
Total Net Position	267,936	10,246,261	9,353,514	1,553,991	557,697	21,979,399
Total Liabilities and Net Position	\$ 1,217,342	\$ 15,472,889	\$ 12,646,001	\$ 1,604,361	\$ 1,261,739	\$ 32,202,332

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION
 PROPRIETARY FUNDS
 FOR THE YEAR ENDED DECEMBER 31, 2017

	<u>Liquor Fund</u>	<u>Water Fund</u>	<u>Wastewater Fund</u>	<u>Sanitation Fund</u>	<u>Ambulance Fund</u>	<u>Total Proprietary Funds</u>
Total Operating Revenue						
380 Charges for Goods and Services (Note 5)	\$ 2,358,673	\$ 1,850,678	\$ 1,741,488	\$ 1,364,324	\$ 959,136	\$ 8,274,299
Operating Expenses						
410 Personal Services	202,950	405,974	261,505	438,784	736,023	2,045,236
420 Other Current Expense	221,273	548,944	229,811	783,863	241,947	2,025,838
426.2 Materials (Cost of Goods Sold)	1,753,608	-	-	-	-	1,753,608
457 Depreciation (Note 4)	30,381	384,028	272,562	83,763	95,716	866,450
Total Operating Expenses	2,208,212	1,338,946	763,878	1,306,410	1,073,686	6,691,132
Operating Income (Loss)	150,461	511,732	977,610	57,914	(114,550)	1,583,167
Nonoperating Revenue (Expense)						
361 Investment Earnings (Note 2)	9,821	-	-	-	-	9,821
369 Other	3,863	-	-	15,962	145,817	165,642
442 Interest Expense	(30,747)	(160,288)	(80,337)	-	-	(271,372)
Total Nonoperating Revenue (Expense)	(17,063)	(160,288)	(80,337)	15,962	145,817	(95,909)
Income before Transfers and Contributions	133,398	351,444	897,273	73,876	31,267	1,487,258
391.07 Capital Contributions	-	191,036	367,169	-	-	558,205
391.10 Transfers In (Note 7)	-	-	-	12,000	-	12,000
511 Transfers Out (Note 7)	-	-	(100,000)	(10,000)	-	(110,000)
Total Transfers and Contributions	-	191,036	267,169	2,000	-	460,205
Change in Net Position	133,398	542,480	1,164,442	75,876	31,267	1,947,463
Net Position, December 31, 2016	134,538	9,703,781	8,189,072	1,478,115	526,430	20,031,936
Net Position, December 31, 2017	\$ 267,936	\$ 10,246,261	\$ 9,353,514	\$ 1,553,991	\$ 557,697	\$ 21,979,399

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2017

	Liquor Fund	Water Fund	Wastewater Fund
Cash Flows from Operating Activities			
Receipts from Customers	\$ 2,386,160	\$ 1,848,513	\$ 1,666,916
Payments to Suppliers	(1,937,400)	(632,891)	(315,251)
Payments to Employees	(223,956)	(459,815)	(303,395)
Net Cash Flows Provided by (Used in) Operating Activities	224,804	755,807	1,048,270
Cash Flows from Noncapital Financing Activities			
Internal Activity, Net	(192,588)	323,069	(108,475)
Net Cash Flows Provided by (Used in) Noncapital Financing Activities	(192,588)	323,069	(108,475)
Cash Flows from Capital and Related Financing Activities			
Purchases of Capital Assets	-	(495,941)	(181,257)
Principal Borrowings on Debt	-	-	313,649
Principal Paid on Debt	(11,423)	(246,938)	(547,570)
Interest Paid	(29,559)	(161,280)	(81,311)
Other Receipts	3,863	-	-
Net Cash Flows Provided by (Used in) Capital and Related Financing Activities	(37,119)	(904,159)	(496,489)
Cash Flows Provided by Investing Activities			
Cash Received from Investment Earnings	9,821	-	-
Increase (Decrease) in Cash and Cash Equivalents	4,918	174,717	443,306
Cash and Cash Equivalents, 2016	28,588	639,085	256,749
Cash and Cash Equivalents, 2017	\$ 33,506	\$ 813,802	\$ 700,055
Reconciliation of Operating Income (Loss) to Net Cash Provided by (Used in) Operating Activities			
Operating Income (Loss)	\$ 150,461	\$ 511,732	\$ 977,610
<i>Adjustments to Reconcile Operating Income (Loss) to Net Cash Flows Provided by (Used in) Operating Activities:</i>			
Depreciation Expense	30,381	384,028	272,562
Change in Assets and Liabilities:			
Accounts Receivable	28,687	(4,292)	(74,572)
Inventory of Supplies Purchased for Resale	25,200	-	-
Prepaid Expenses	362	(196)	401
Pension Asset	(698)	(1,101)	(967)
Pension Related Deferred Outflows	1,857	2,930	2,575
Accounts Payable	11,209	(83,732)	(85,841)
Accrued Wages Payable	6	1,720	331
Accrued Taxes Payable	710	(19)	-
Customer Deposits	(1,200)	2,127	-
Accrued Leave Payable	(366)	(282)	(771)
Pension Liability	(21,805)	(57,108)	(43,058)
Net Cash Flows Provided by (Used in) Operating Activities	\$ 224,804	\$ 755,807	\$ 1,048,270
Noncash Capital and Related Financing Activities			
Capital Assets Contributed	\$ -	\$ 191,036	\$ 367,169
Purchase of Capital Assets with Long-Term Debt	-	-	1,793,779

The accompanying notes are an integral part of the financial statements.

<u>Sanitation Fund</u>	<u>Ambulance Fund</u>	<u>Total Proprietary Funds</u>
\$ 1,367,054	\$ 880,783	\$ 8,149,426
(781,280)	(247,010)	(3,913,832)
(508,850)	(834,350)	(2,330,366)
<u>76,924</u>	<u>(200,577)</u>	<u>1,905,228</u>
251,414	155,377	428,797
<u>251,414</u>	<u>155,377</u>	<u>428,797</u>
-	(100,617)	(777,815)
-	-	313,649
-	-	(805,931)
-	-	(272,150)
15,962	145,817	165,642
<u>15,962</u>	<u>45,200</u>	<u>(1,376,605)</u>
-	-	9,821
344,300	-	967,241
423,541	-	1,347,963
\$ 767,841	\$ -	\$ 2,315,204
\$ 57,914	\$ (114,550)	\$ 1,583,167
83,763	95,716	866,450
2,730	(78,353)	(125,800)
-	-	25,200
(187)	267	647
(1,380)	(2,223)	(6,369)
3,674	5,919	16,955
2,770	(5,330)	(160,924)
1,281	121	3,459
-	-	691
-	-	927
(6,543)	(1,178)	(9,140)
(67,098)	(100,966)	(290,035)
\$ 76,924	\$ (200,577)	\$ 1,905,228
\$ -	\$ -	\$ 558,205
-	-	1,793,779

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2017

(1) Summary of Significant Accounting Policies

Reporting Entity

The reporting entity of the City of Sturgis (the City), consists of the primary government (which includes all of the funds, organizations, institutions, agencies, departments, and offices that make up the legal entity, plus those funds for which the primary government has a fiduciary responsibility; those organizations for which the primary government is financially accountable; and other organizations for which the nature and significance of their relationship with the primary government are such that their exclusion would cause the financial reporting entity's financial statements to be misleading or incomplete).

Basis of Presentation

Government-wide Financial Statements:

The Statement of Net Position and Statement of Activities display information about the reporting entity as a whole. They include all funds of the reporting entity except for fiduciary funds. The statements distinguish between governmental and business-type activities. Governmental activities generally are financed through taxes, intergovernmental revenues, and other non-exchange revenues. Business-type activities are financed in whole or in part by fees charged to external parties for goods or services.

The Statement of Activities presents a comparison between direct expenses and program revenues for each segment of the business-type activities of the City and for each function of the City's governmental activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function. Program revenues include (a) charges paid by recipients of goods and services offered by the programs and (b) grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues.

Fund Financial Statements:

Fund financial statements of the reporting entity are organized into funds, each of which is considered to be a separate accounting entity. Each fund is accounted for by providing a separate set of self-balancing accounts that constitute its assets, liabilities, fund equity, revenues, and expenditures/expenses. Funds are organized into three major categories: governmental, proprietary, and fiduciary. An emphasis is placed on major funds within the governmental and proprietary categories. A fund is considered major if it is the primary operating fund of the City or it meets the following criteria:

1. Total assets, liabilities and deferred inflows and outflows of resources, revenues, or expenditures/expenses of the individual governmental or enterprise fund are at least 10 percent of the corresponding total for all funds of that category or type, and
2. Total assets, liabilities and deferred inflows and outflows of resources, revenues, or expenditures/expenses of the individual governmental or enterprise fund are at least 5 percent of the corresponding total for all governmental and enterprise funds combined, or
3. Management has elected to classify one or more governmental or enterprise funds as major for consistency in reporting from year to year, or because of public interest in the fund's operations.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017**

(1) Summary of Significant Accounting Policies (Continued)

Basis of Presentation (Continued)

The major funds of the City financial reporting entity are described below:

Governmental Funds:

General Fund - the general fund is the general operating fund of the City. It is used to account for all financial resources except those required to be accounted for in another fund. The general fund is always considered to be a major fund.

Special Revenue Funds - special revenue funds are used to account for the proceeds of specific revenue sources (other than trusts for individuals, private organizations, or other governments or for major capital projects) that are legally restricted to expenditures for specified purposes.

Capital Improvement Fund – Under Ordinance 2012-01, at least 40 percent of the tax levied under Title 20 Tax, Chapter 20.01 Municipal Sales and Service Tax, and Use Tax shall be used only for capital improvements, land acquisition, debt reduction, and the purchase of machinery and equipment. This is a major fund.

Revolving Loan Fund - to account for federal grants and other municipal monies used for financing improvements. The fund may be used both to pay the portion of the cost of an improvement and to advance the portion of such costs to businesses which are to be repaid over a period of years. This is a major fund.

Debt Service Funds - debt service funds are used to account for the accumulation of resources for, and the payment of, general long-term debt principal, interest, and related costs. The City has the following debt service fund:

TIF Debt Service Fund – TIF funds are Tax Increment Financing Districts allowed by SDCL 11-9-24 to account for the proceeds of incremental property taxes, restricted for the payment of principal and interest on debt issued to finance a public improvement. Separate accounts are maintained for TIF Districts #9, #10, #11, #12, and #13 revenues and expenditures. This is a major fund.

Capital Projects Funds - capital projects funds are used to account for financial resources to be used for the acquisition or construction of major capital facilities (other than those financed by proprietary funds or trust funds for individuals, private organizations, or other governments). There are no major capital projects funds.

Permanent Funds - permanent funds are used to report resources that are legally restricted to the extent that only earnings, and not principal, may be used for purposes that support the City's programs - that is for the benefit of the City and its citizenry. There are no major permanent funds.

Proprietary Funds:

Enterprise Funds - enterprise funds are used to account for operations (a) that are financed and operated in a manner similar to private business enterprises, where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017**

(1) Summary of Significant Accounting Policies (Continued)

Basis of Presentation (Concluded)

Proprietary Funds (Continued):

Proprietary Funds include:

Liquor Fund - financed primarily by the sale of liquor; this fund accounts for construction and operation of the City liquor store. This is a major fund.

Water Fund - financed primarily by user charges; this fund accounts for the construction and operation of the City waterworks system and related facilities (SDCL 9-47-1). This is a major fund.

Wastewater Fund - financed primarily by user charges; this fund accounts for the construction and operation of the City sanitary sewer system and related facilities (SDCL 9-48-2). This is a major fund.

Sanitation Fund - financed primarily by user charges; this fund accounts for the construction and operation of the City rubble site and collection and disposal of solid waste and includes activity from the Special Sanitation Fund. This is a major fund.

Ambulance Fund - financed primarily by user charges; this fund accounts for construction and operation of the City ambulance service. This is a major fund.

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 revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements, regardless of the measurement focus.

Measurement Focus:

Government-wide Financial Statements:

In the government-wide Statement of Net Position and Statement of Activities, both governmental and business-type activities are presented using the economic resources measurement focus, applied on the accrual basis of accounting.

Non-exchange transactions, in which the City gives (or receives) value without directly receiving (or giving) equal value in exchange, include property taxes, grants, entitlements and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenues from grants, entitlements and donations are recognized in the year in which all eligibility requirements have been satisfied.

Fund Financial Statements:

In the fund financial statements, the current financial resources measurement focus and the modified accrual basis of accounting are applied to governmental funds, while the economic resources measurement focus and the accrual basis of accounting are applied to the proprietary and fiduciary funds.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017**

(1) Summary of Significant Accounting Policies (Continued)

Measurement Focus and Basis of Accounting (Continued)

Basis of Accounting:

Government-wide Financial Statements:

In the Government-wide Statement of Net Position and Statement of Activities, governmental and business-type activities are presented using the accrual basis of accounting. Under the accrual basis of accounting, revenues and related assets are recorded when earned (usually when the right to receive cash vests); and expenses and related liabilities are recorded when an obligation is incurred (usually when the obligation to pay cash in the future vests).

Fund Financial Statements:

All governmental fund types are accounted for using the modified accrual basis of accounting. Their revenues, including property taxes, are recognized when they become measurable and available. Available means resources are collected or to be collected soon enough after the end of the fiscal year that they can be used to pay the bills of the current period. The accrual period for the City does not exceed one bill-paying cycle, and for the City, the length of that cycle is 60 days. The revenues which are accrued at December 31, 2017 are property tax revenues and special assessments.

Under the modified accrual basis of accounting, receivables may be measurable, but not available. Available means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Reported deferred inflows of resources are those where asset recognition criteria have been met, but for which revenue recognition criteria have not been met.

Expenditures are generally recognized when the related fund liability is incurred. Exceptions to this general rule include principal and interest on general long-term debt, which are recognized when due.

All proprietary funds are accounted for using the accrual basis of accounting. Their revenues are recognized when they are earned, and their expenses are recognized when they are incurred.

Interfund Eliminations and Reclassifications

Government-wide Financial Statements:

In the process of aggregating data for the government-wide financial statements, some amounts reported as interfund activity and balances in the fund financial statements have been eliminated or reclassified, as follows:

In order to minimize the grossing-up effect on assets and liabilities within the governmental and business-type activities columns of the primary government, amounts reported as interfund receivables and payables have been eliminated in the governmental and business-type activities columns, except for the net, residual amounts due between governmental and business-type activities, which are presented as internal balances.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017**

(1) Summary of Significant Accounting Policies (Continued)

Interfund Eliminations and Reclassifications (Continued)

Fund Financial Statements:

Noncurrent portions of long-term interfund receivables (reported in Advance to asset accounts) are equally offset by a nonspendable fund balance account which indicates that they do not constitute available spendable resources since they are not a component of net current assets. Current portions of interfund receivables (reported in Due from asset accounts) are considered available spendable resources.

Capital Assets

Capital assets include land, buildings, machinery and equipment, and all other tangible or intangible assets that are used in operations and that have initial useful lives extending beyond a single reporting period. Infrastructure assets are long-lived capital assets that normally are stationary in nature and can be preserved for a significantly greater number of years than most capital assets.

The accounting treatment over capital assets depends on whether the assets are used in governmental fund operations or proprietary fund operations and whether they are reported in the government-wide or fund financial statements.

Government-wide Financial Statements:

Capital assets are recorded at historical cost, or estimated cost, where actual cost could not be determined. Donated capital assets are valued at their estimated fair value on the date donated. Reported cost values include ancillary charges necessary to place the asset into its intended location and condition for use. Subsequent to initial capitalization, improvements or betterments that are significant and which extend the useful life of a capital asset are also capitalized.

For governmental activities capital assets, construction-period interest is not capitalized, in accordance with USGAAP; while for capital assets used in business-type activities; construction-period interest is capitalized in accordance with USGAAP.

Infrastructure assets used in general government operations, consisting of certain improvements other than buildings, including roads, bridges, sidewalks, drainage systems, and lighting systems, acquired prior to January 1, 2004, were not required to be capitalized by the City. Infrastructure assets acquired since January 1, 2004, are recorded at cost, and classified as "Improvements Other than Buildings."

Depreciation of all exhaustible capital assets is recorded as an allocated expense in the Government-wide Statement of Activities. Accumulated depreciation is reported on the Government-wide Statement of Net Position and on each proprietary fund's Statement of Net Position/Balance Sheet.

Capitalization thresholds (the dollar values above which asset acquisitions are added to the capital asset accounts), depreciation methods, and estimated useful lives of capital assets reported in the government-wide statements and proprietary funds are as follows:

	<u>Capitalization Threshold</u>	<u>Depreciation Method</u>	<u>Estimated Useful Life</u>
Land	\$ -0-	----N/A-----	---N/A-----
Buildings	\$ 15,000	Straight-line	10-50 years
Improvements Other Than Buildings	\$ 15,000	Straight-line	10-50 years
Machinery and Equipment	\$ 10,000	Straight-line	5-40 years

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2017

(1) Summary of Significant Accounting Policies (Continued)

Capital Assets (Continued)

Land is an inexhaustible capital asset and is not depreciated.

Fund Financial Statements:

In the fund financial statements, capital assets used in governmental fund operations are accounted for as capital outlay expenditures of the appropriate governmental fund upon acquisition. Capital assets used in proprietary fund operations are accounted for on the accrual basis, the same as in the government-wide statements.

Long-Term Liabilities

The accounting treatment of long-term liabilities depends on whether the assets are used in governmental fund operations or proprietary fund operations and whether they are reported in the government-wide or fund financial statements.

All long-term liabilities to be repaid from governmental and business-type resources are reported as liabilities in the government-wide statements. The long-term liabilities primarily consist of general obligation bonds, revenue bonds, tax increment financing, contract payable, and compensated absences.

In the fund financial statements, debt proceeds are reported as revenues (other financing sources), while payments of principal and interest are reported as expenditures when they become due. The accounting for proprietary fund long-term debt is on the accrual basis, the same in the fund statements as in the government-wide statements.

Program Revenues

Program revenues derive directly from the program itself or from parties other than the City's taxpayers or citizenry, as a whole. Program revenues are classified into three categories, as follows:

1. Charges for services – These arise from charges to customers, applicants, or others who purchase, use, or directly benefit from the goods, services, or privileges provided, or are otherwise directly affected by the services.
2. Program-specific operating grants and contributions – These arise from mandatory and voluntary non-exchange transactions with other governments, organizations, or individuals that are restricted for use in a particular program.
3. Program-specific capital grants and contributions – These arise from mandatory and voluntary non-exchange transactions with other governments, organizations, or individuals that are restricted for the acquisition of capital assets for use in a particular program.

Proprietary Funds Revenue and Expense Classifications

In the proprietary funds' Statement of Revenues, Expenses, and Changes in Fund Net Position, revenues and expenses are classified in a manner consistent with how they are classified in the Statement of Cash Flows. That is, transactions for which related cash flows are reported as capital and related financing activities, noncapital financing activities, or investing activities are not reported as components of operating revenues or expenses.

Cash and Cash Equivalents

The City pools the cash resources of its funds for cash management purposes. The proprietary funds essentially have access to the entire amount of their cash resources on demand. Accordingly, each proprietary fund's equity in the cash management pool is considered to be cash and cash equivalents for the purpose of the Statement of Cash Flows.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017**

(1) Summary of Significant Accounting Policies (Continued)

Equity Classifications

Government-wide Financial Statements:

Equity is classified as net position and is displayed in three components:

1. Net investment in capital assets – Consists of capital assets, including restricted capital assets, net of accumulated depreciation (if applicable) and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.
2. Restricted net position – Consists of net position with constraints placed on their use either by (a) external groups such as creditors, grantors, contributors, or laws and regulations of other governments; or (b) law through constitutional provisions or enabling legislation.
3. Unrestricted net position – All other net position that do not meet the definition of restricted or net investment in capital assets.

Fund Financial Statements:

The City classifies governmental fund balance as follows:

Nonspendable – includes fund balance amounts that cannot be spent either because it is not in spendable form or because of legal or contractual constraints.

Restricted – includes fund balance amounts that are constrained for specific purposes which are externally imposed by providers, such as creditors or amounts constrained due to constitutional provisions or enabling legislation.

Committed – includes fund balance amounts that are constrained for specific purposes that are internally imposed by the government through formal action of the highest level of decision making authority and does not lapse at year-end. The Brick Fund and Capital Improvement Fund were created through ordinances passed by the City Council, the highest decision making authority. The City Council would have to pass ordinances to remove the commitments. However, due to a deficit fund balance at year-end, the Capital Improvement Fund is presenting a negative unassigned fund balance, rather than a committed balance.

Assigned – includes fund balance amounts that are intended to be used for specific purposes that are neither considered restricted or committed. Fund balance may be assigned by the City Council, Mayor, or Finance Officer.

Unassigned – includes positive fund balance within the General Fund which has not been classified within the above-mentioned categories and negative fund balances in other governmental funds.

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017

(1) Summary of Significant Accounting Policies (Continued)

Equity Classifications (Continued)

With regard to the City's governmental funds, the City uses restricted amounts first when both restricted and unrestricted fund balances are available unless there are legal documents/contracts that prohibit doing this, such as a grant agreement requiring dollar-for-dollar spending. Additionally, the City would first use committed, then assigned, and lastly unassigned amounts of unrestricted fund balance when expenditures are made. The City set a minimum fund balance policy within the general fund to keep on hand at least two months of regular fund operating revenues or regular general fund operating expenditures.

Proprietary fund equity is classified the same as in the government-wide financial statements. The City does not have a formal minimum fund balance policy. With regard to the City's proprietary funds, it is the City's policy to first use restricted net position, prior to the use of unrestricted net position, when an expense is incurred for purposes for which both restricted and unrestricted net position are available.

As of December 31, 2017, the City had the following governmental fund classifications:

	General Fund	Capital Improvement Fund	Revolving Loan Fund	TIF Funds	Other Governmental Funds	Total Governmental Funds
263 Nonspendable:						
263.02 Nonspendable - Prepaid Expenses	\$ 38,591	\$ -	\$ -	\$ -	\$ -	\$ 38,591
263.04 Nonspendable - Advances	1,092,484	-	400,000	-	-	1,492,484
263.05 Nonspendable - Notes Receivable	-	1,804	411,586	-	-	413,390
263.49 Nonspendable - SDPAA Reserve (Note 9)	135,844	-	-	-	-	135,844
263.51 Nonspendable - Perpetual Care Cemetery	-	-	-	-	50,000	50,000
263.99 Nonspendable - Library Trust	-	-	-	-	327,535	327,535
	<u>1,266,919</u>	<u>1,804</u>	<u>811,586</u>	<u>-</u>	<u>377,535</u>	<u>2,457,844</u>
264 Restricted:						
264.03 Restricted - Perpetual Care Cemetery	-	-	-	-	131,020	131,020
264.04 Restricted - BBB Tax	-	-	-	-	753,869	753,869
264.05 Restricted - Library Purposes	-	-	-	-	269,987	269,987
264.09 Restricted - BID Tax	-	-	-	-	201	201
264.97 Restricted - Revolving Loan	-	-	496,231	-	-	496,231
	<u>-</u>	<u>-</u>	<u>496,231</u>	<u>-</u>	<u>1,155,077</u>	<u>1,651,308</u>
265 Committed						
265.97 Committed - Brick Fund	134,742	-	-	-	-	134,742
266 Assigned						
266.01 Assigned - Subsequent Year's Budget	89,201	-	-	-	-	89,201
267 Unassigned	<u>1,350,285</u>	<u>(634,348)</u>	<u>-</u>	<u>(1,753,827)</u>	<u>-</u>	<u>(1,037,890)</u>
Total Fund Balances	\$ 2,841,147	\$ (632,544)	\$ 1,307,817	\$ (1,753,827)	\$ 1,532,612	\$ 3,295,205

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017**

(1) Summary of Significant Accounting Policies (Concluded)

Inventory of Supplies Purchased for Resale

Inventory consists of inventory held for resale, which is recorded at the lower of cost or market, using the first-in, first-out method. Inventory is recorded as an asset at the time of purchase, and charged to expense as it is consumed.

Deferred Inflows and Deferred Outflows of Resources

In addition to assets, the statement of net position reports a separate section for deferred outflows of resources. Deferred outflows of resources represent consumption of net position that applies to a future period or periods. These items will not be recognized as an outflow of resources until the applicable future period. Deferred outflows of resources consist of pension activity.

In addition to liabilities, the statement of net position and governmental funds balance sheet report a separate section for deferred inflows of resources. Deferred inflows of resources represent acquisitions of net position that applies to a future period or periods. These items will not be recognized as an inflow of resources until the applicable future period. Deferred inflows of resources consist primarily of property taxes and special assessments in the governmental fund balance sheet.

Receivables and Payables

Receivables and payables are not aggregated in these financial statements. The City expects all receivables to be collected within one year. Included in accounts receivable at December 31, 2017 is an allowance for doubtful accounts totaling \$10,000 for the general fund. Included in utility accounts receivable at December 31, 2017 are allowances for doubtful accounts totaling approximately \$2,500, \$4,000, \$3,500 and \$800,000 for the water, wastewater, sanitation and ambulance funds, respectively.

(2) Deposits and Investments

The City follows the practice of aggregating the cash assets of various funds to maximize cash management efficiency and returns. Various restrictions on deposits and investments are imposed by statutes. These restrictions are summarized below:

Deposits - The City's cash deposits are made in qualified public depositories as defined by SDCL 4-6A-1, 9-22-6, 9-22-6.1 and 9-22-6.2, and may be in the form of demand or time deposits. Qualified depositories are required by SDCL 4-6A-3 to maintain at all times, segregated from their other assets, eligible collateral having a value equal to at least 100 percent of the public deposit accounts which exceed deposit insurance such as the FDIC and NCUA. In lieu of pledging eligible securities, a qualified public depository may furnish irrevocable standby letters of credit issued by Federal Home Loan Banks accompanied by written evidence of that bank's public debt rating, which may not be less than "AA" or a qualified public depository may furnish a corporate surety bond of a corporation duly authorized to do business in South Dakota.

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017

(2) Deposits and Investments (Continued)

Investments - In general, SDCL 4-5-6 permits City funds to be invested only in (a) securities of the United States and securities guaranteed by the United States Government either directly or indirectly; or (b) repurchase agreements fully collateralized by securities described in (a) above; or in shares of an open-end, no-load fund administered by an investment company whose investments are in securities described in (a) above and repurchase agreements described in (b) above. Also, SDCL 4-5-9 requires investments to be in the physical custody of the political subdivision or may be deposited in a safekeeping account with any bank or trust company designated by the political subdivision as its fiscal agent.

The City categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs.

As of December 31, 2017, the City had the following investments:

Investments	Credit Rating	Maturity	Fair Value
Treasury Money Market	N/A	N/A	\$ 75,546
Negotiable Certificates of Deposits	N/A	1-5 Years	979,078
			\$ 1,054,624

Money markets and negotiable certificates of deposit are measured as level 2 recurring fair value measurements according to the fair value hierarchy.

State law allows income from deposits and investments to be credited to either the general fund or the fund making the investment. The City's policy is to credit all income from deposits and investments to the General Fund, including investment income generated by the Perpetual Maintenance Fund, which must be credited to the General Fund, and used only for maintenance for the municipal cemetery, as required by SDCL 9-32-18. USGAAP, on the other hand, requires income from deposits and investments to be reported in the fund whose assets generated that income except where legal or contractual requirements require investment income to be credited to a fund other than the one associated with the assets. Where the governing board has discretion to credit investment income to a fund other than the fund that provided the resources for investment, a transfer to the designated fund is reported. Accordingly, in the fund financial statements, interfund transfers of investment earnings are reported, while in the government-wide financial statements, they have been eliminated, except for the net amounts transferred between governmental activities and business-type activities. Liquor Fund interest income consists of monies received from Build America Bonds, not income generated from bank account balances.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017**

(2) Deposits and Investments (Concluded)

Interest Rate Risk:

The City limits interest rate risk by structuring the portfolio to meet the cash requirements of ongoing operations, thereby mitigating the need to liquidate securities at a loss prior to maturity.

Credit Risk:

State law limits eligible investments for the City as discussed above. The City will further reduce credit risk by limiting the portfolio to interest bearing checking accounts, savings accounts, US Treasury bills, bonds, notes, US Government Agencies, certificates of deposit, certificates of deposit purchased through CDARS, money market mutual funds, and repurchase agreements fully collateralized by allowable securities.

Custodial Credit Risk:

Custodial credit risk is the risk that, in the event of a depository failure, the City's deposits may not be returned to it. The City will minimize custodial credit risk for deposits by requiring the financial institution to submit a copy of their collateralization report to the finance officer to determine whether the financial institution is in compliance with SDCL 4-6A and 51A-10-9. As of December 31, 2017, the City's deposits in financial institutions collateralized by securities held by the pledging financial institution were as follows:

	<u>Bank Balance</u>
Insured - FDIC	\$ 532,152
Uninsured, collateralized in accordance with SDCL 4-6A-3	4,219,528
Total Deposits	\$ 4,751,680

Concentration Risk:

The City will minimize concentration of credit risk by diversifying the investment portfolio so that the impact of potential losses from any one type of security or issuer will be minimized. Investments issued or explicitly guaranteed by the U.S. government and investments in mutual funds, external investment pools, and other pooled investments are excluded from this requirement. More than five percent of the City's certificates of deposit are in: American Express (9.5 percent), Capital One Bank (11.9 percent), GE Capital (24.2 percent), Goldman Sachs (23.7 percent), and Discover Bank (23.7 percent).

(3) Property Taxes

Property taxes are levied on or before October 1 and payable in two installments before April 30 and October 31 of the following year. They attach as an enforceable lien on property as of January 1 of each year. The county bills and collects the taxes and remits them to the City.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017**

(3) Property Taxes (Continued)

The City is permitted by several state statutes to levy the following amounts of taxes per \$1,000 of taxable valuation on taxable real property in the City:

General Fund	\$27
Bond Redemption Funds	Amounts Required by Bond Agreements
Judgment Fund (Upon Judgment Being Made)	\$10

State statute allows the tax rates to be raised by special election of the voters.

(4) Changes in Capital Assets

A summary of changes in capital assets for year ending December 31 is as follows:

	Balance 12/31/2016	Additions	Transfers/ Deletions	Balance 12/31/2017
<i>Governmental Activities:</i>				
Capital Assets, not being Depreciated:				
Land	\$ 2,923,815	\$ -	\$ -	\$ 2,923,815
Construction Work in Progress	382,541	5,219,796	(1,707,290)	3,895,047
Total Capital Assets, not being Depreciated	3,306,356	5,219,796	(1,707,290)	6,818,862
Capital Assets, being Depreciated:				
Buildings	13,389,430	-	141,774	13,531,204
Improvements Other Than Buildings	32,729,355	463,130	1,007,311	34,199,796
Machinery and Equipment	4,716,612	281,082	(19,498)	4,978,196
Total Capital Assets, being Depreciated	50,835,397	744,212	1,129,587	52,709,196
Less Accumulated Depreciation for:				
Buildings	4,682,314	302,770	-	4,985,084
Improvements Other Than Buildings	8,805,299	710,633	-	9,515,932
Machinery and Equipment	2,845,007	195,487	(19,498)	3,020,996
Total Accumulated Depreciation	16,332,620	1,208,890	(19,498)	17,522,012
Total Governmental Activities Capital Assets, being Depreciated, Net	34,502,777	(464,678)	1,149,085	35,187,184
Total Governmental Capital Assets, Net	\$ 37,809,133	\$ 4,755,118	\$ (558,205)	\$ 42,006,046

Depreciation expense was charged to functions as follows:

Public Works	\$ 544,336
Culture and Recreation	300,940
General Government	99,632
Public Safety	263,982
Total Depreciation Expense - Governmental	\$ 1,208,890

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017

(4) Changes in Capital Assets (Continued)

	Balance 12/31/2016	Additions	Transfers/ Deletions	Balance 12/31/2017
<i>Business-Type Activities:</i>				
Capital Assets, not being Depreciated:				
Land	\$ 738,681	\$ -	\$ -	\$ 738,681
Construction Work in Progress	1,578,765	2,470,977	(1,780,734)	2,269,008
Total Capital Assets, not being Depreciated	2,317,446	2,470,977	(1,780,734)	3,007,689
Capital Assets, being Depreciated:				
Buildings	2,123,285	-	-	2,123,285
Improvements Other Than Buildings	28,470,268	-	2,338,939	30,809,207
Machinery and Equipment	4,986,685	100,617	-	5,087,302
Total Capital Assets, being Depreciated	35,580,238	100,617	2,338,939	38,019,794
Less Accumulated Depreciation for:				
Buildings	612,261	60,635	-	672,896
Improvements Other Than Buildings	9,035,202	597,440	-	9,632,642
Machinery and Equipment	3,839,912	208,375	-	4,048,287
Total Accumulated Depreciation	13,487,375	866,450	-	14,353,825
Total Business-Type Activities Capital Assets, being Depreciated, Net	22,092,863	765,833	2,338,939	23,665,969
Total Business-Type Capital Assets, Net	\$ 24,410,309	\$ 1,705,144	\$ 558,205	\$ 26,673,658
Depreciation expense was charged to functions as follows:				
Ambulance	\$ 95,716			
Wastewater	272,562			
Water	384,028			
Sanitation	83,763			
Liquor	30,381			
Total Depreciation Expense - Business-Type	\$ 866,450			

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017**

(5) Long-Term Debt

The following is a summary of the long-term debt transactions for the year ending December 31:

	Balance 12/31/2016	Additions	Deletions	Balance 12/31/2017	Due Within One Year
Primary Government:					
Governmental Activities:					
2008 Revenue Bonds	\$ 2,820,000	\$ -	\$ 2,820,000	\$ -	\$ -
Tax Increment Financing Obligations	1,548,801	201,199	-	1,750,000	-
Notes Payable	997,421	4,333,313	241,492	5,089,242	243,595
Compensated Absences	216,865	297,456	299,774	214,547	214,547
Total Governmental Activities	5,583,087	4,831,968	3,361,266	7,053,789	458,142
Business-Type Activities:					
2010 GO Crossover Refunding Bonds	600,000	-	600,000	-	-
2010 Sales Tax Revenue Bond	738,954	-	11,423	727,531	11,281
2009 Drinking Water Revenue Bond	247,801	-	56,199	191,602	57,474
2009 Clean Water Revenue Bond	216,382	-	13,570	202,812	13,981
2011 Drinking Water Revenue Bond	3,111,512	-	42,765	3,068,747	44,132
2012 Drinking Water Revenue Bond	1,822,697	-	81,974	1,740,723	84,461
Wastewater Note Payable	712,501	2,107,428	-	2,819,929	123,834
Compensated Absences	86,676	132,017	141,157	77,536	77,536
Total Business-Type Activities	7,536,523	2,239,445	947,088	8,828,880	412,699
Total Primary Government	\$ 13,119,610	\$ 7,071,413	\$ 4,308,354	\$ 15,882,669	\$ 870,841

The City has restricted reserves of \$28,686, and \$14,034 at December 31, 2017, in accordance with debt covenants.

The City has pledged revenues of the Water and Wastewater Funds for the retirement of debt issues associated with those funds through the maturity dates listed below. All debt secured by pledged revenues funded capital projects and improvements. The current principal balance plus interest at the stated applicable rate over the life of the debt represents the amount of future revenue pledged. Below is a comparison of principal and interest payments and total pledged revenue for the current year.

	Water <u>Fund</u>	Wastewater <u>Fund</u>
Current Year Principal and Interest	\$ 407,226	\$ 627,907
Pledged Revenue	1,850,678	1,741,488

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017**

(5) Long-Term Debt (Continued)

Long-term debt at December 31, 2017, is comprised of the following:

Revenue Bonds

Sales Tax Revenue Bonds, Series 2010 (Build America Bonds - Direct Pay), for \$811,000, mature in July 2050, interest at a fixed 4.00 percent, due in annual installments of \$40,980. Sales tax revenues pledged and financed through the Liquor Fund. The City will receive a credit from the Federal government for 35 percent of the interest paid on the bonds. 727,531

Drinking Water Revenue Borrower Bond, 2009 Series for \$547,576, mature in January 2021, interest at a fixed 2.25 percent, due in quarterly installments of \$15,325. Water revenues pledged and financed through the Water Fund. 191,602

Clean Water Revenue Borrower Bond, 2009 Series for \$298,617, mature in October 2030, interest at a fixed 3.00 percent, due in quarterly installments of \$4,977. Wastewater revenues pledged and financed through the Wastewater Fund. 202,812

Drinking Water Revenue Borrower Bond, 2011 Series for \$3,200,000, matures in September 2054, interest at a fixed 3.25 percent due in monthly installments of \$11,936. Water revenues pledged and financed through the Water Fund. 3,068,747

Drinking Water Revenue Borrower Bond, Series 2012 for \$2,035,893, mature in July 2034, interest at a fixed 3.00 percent, due in quarterly installments of \$33,935. Water revenues pledged and financed through the Water Fund. 1,740,723

Notes Payable

Note Payable to First Interstate Bank, matures with a balloon payment in 2019, interest at a fixed 3.75 percent, due in monthly installments of \$7,116. Financed through Capital Improvement Fund. 948,832

Note Payable to Pioneer Bank for \$3,052,000, matures with a balloon payment in 2036, interest at a fixed 3.85 percent, due in monthly installments of \$19,186. Financed through Wastewater Fund. 2,819,929

Note payable to Pioneer Bank for \$5,757,000, interest only payments at a 4 percent fixed rate through December 2018. Principal and interest payments at a fixed 4.00 percent rate beginning January 2019 and through May 2028. Financed through the Capital Improvements Fund. 3,513,813

Note Payable to SD Department of Transportation. Non-interest bearing and due in varying annual installments through 2021. Financed through the Capital Improvements Fund. 626,597

Tax Increment Financing Obligations

TIF #12 maximum borrowings of \$1,900,000, including interest not to exceed 10.00 percent per annum, due in varying installments within 30 days of property tax collections from the County. Financed through TIF Debt Service Funds. 1,750,000

Total Bonds, Notes Payable, and TIF Obligations 15,590,586

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017

(5) Long-Term Debt (Continued)

Compensated Absences:

General Fund	214,547
Liquor Fund	892
Water Fund	25,967
Wastewater Fund	24,607
Sanitation Fund	21,596
Ambulance Fund	4,474
Total Compensated Absences	292,083

Total Long-Term Debt **\$ 15,882,669**

The annual requirements to amortize long-term debt outstanding as of December 31, 2017, except for compensated absences are as follows:

	Revenue Bonds		TIF Obligations		Notes Payable		Total	
	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>
2018	\$ 189,832	\$ 211,329	\$ 118,905	\$ -	\$ 285,114	\$ 367,429	\$ 593,851	\$ 578,758
2019	183,626	217,483	126,137	-	251,950	1,532,750	561,713	1,750,233
2020	177,233	223,865	133,810	-	219,220	651,774	530,263	875,639
2021	171,342	183,754	141,042	-	200,101	525,879	512,485	709,633
2022	165,890	173,970	148,274	-	180,843	497,248	495,007	671,218
2023-2027	742,740	956,583	851,614	-	587,523	2,802,935	2,181,877	3,759,518
2028-2032	581,350	1,066,327	1,035,500	-	169,960	1,174,939	1,786,810	2,241,266
2033-2037	431,654	659,080	465,529	1,750,000	11,633	356,217	908,816	2,765,297
2038-2042	336,577	584,483	-	-	-	-	336,577	584,483
2043-2047	228,191	692,859	-	-	-	-	228,191	692,859
2048-2052	101,242	721,323	-	-	-	-	101,242	721,323
2053-2057	7,177	240,359	-	-	-	-	7,177	240,359
Total	\$3,316,854	\$5,931,415	\$3,020,811	\$1,750,000	\$1,906,344	\$7,909,171	\$ 8,244,009	\$15,590,586

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017**

(5) Long-Term Debt (Concluded)

Tax Increment Financing Obligations

Tax increment financing is a method of financing improvements and development in an area which has been determined to be blighted according to the criteria set forth in SDCL 11-9. In some instances, the City pledges future tax revenues generated by the tax increment district to acquire public improvements within the established Tax Increment District which were constructed by a private developer.

It is a specific condition of the developer's agreement and a condition of the City's obligation that all sums payable shall be limited to the proceeds of the positive tax increment. It is also specifically agreed that the City has made no representation that the proceeds from such funds shall be sufficient to retire the indebtedness incurred by the developer to construct the public improvements.

During the year ended December 31, 2017, TIF related property tax revenues were \$47,664. Interest expenditures, excluding corresponding accruals, related to TIF obligations totaled \$103,011 for the year ended December 31, 2017.

(6) Individual Fund Interfund Receivable and Payable Balances

Interfund receivable and payable balances at December 31, 2017, are as follows:

Fund	Interfund Receivables	Interfund Payables
<i>Major Funds:</i>		
Ambulance Fund	\$ -	\$ 676,449
Liquor Fund	-	48,934
Capital Improvement Funds	259,625	-
General Fund	633,599	-
TIF Fund	-	167,841
Total Interfund Receivable and Payable Balances	\$ 893,224	\$ 893,224

The General Fund lent money to the TIF funds to fund projects. The General Fund and Capital Improvement Fund loaned monies to the Liquor Fund and Ambulance Fund to help maintain a positive cash balance at year end. The balances will be repaid within the next year.

Interfund advances balances at December 31, 2017, are as follows:

Fund	Interfund Advance To	Interfund Advance From
<i>Major Funds:</i>		
General Fund	\$ 1,092,484	\$ -
Revolving Loan Fund	400,000	-
Water Fund	1,391,751	-
TIF Funds	-	2,074,235
Capital Improvement Fund	-	810,000
Total Interfund Receivable and Payable Balances	\$ 2,884,235	\$ 2,884,235

The General Fund and Revolving Loan Fund advanced monies to the Capital Improvement Fund to assist with costs for HD Rally Point. The balance will be repaid through 2025. The General Fund and Water Fund advanced monies to the TIF Funds to assist in funding for TIF #11. The balance will be repaid through 2033 and bears interest at 4.00 percent. The General Fund advanced monies to the TIF Funds to assist in funding for TIF #13. The balance will be repaid through 2025 and bears interest at 5.00 percent.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017**

(7) Interfund Transfers

	Transfers In	Transfers Out
<i>Major Funds:</i>		
General Fund	\$ 110,000	\$ 87,975
Capital Improvement Fund	75,975	-
Wastewater Fund	-	100,000
Sanitation Fund	12,000	10,000
Total Transfers	\$ 197,975	\$ 197,975

Transfers between the funds were made to cover general operational costs of the City, to repair the Community Center roof, transfer proceeds from sale of land, and to transfer interest income to the General Fund in accordance with the City's policy.

(8) Pension Plan

All employees, working more than 20 hours per week during the year, participate in the SDRS, a cost sharing, multiple employer defined benefit pension plan administered by SDRS to provide retirement benefits for employees of the State of South Dakota and its political subdivisions. The SDRS provides retirement, disability, and survivors' benefits. The right to receive retirement benefits vests after three years of credited service. Authority for establishing, administering and amending plan provisions are found in SDCL 3-12. The SDRS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained at <http://www.sdrs.sd.gov/publications/> or by writing to the SDRS, P.O. Box 1098, Pierre, SD 57501-1098 or by calling (605) 773-3731.

Benefits Provided:

SDRS has three different classes of employees, Class A, Class B public safety and Class B judicial. Class A retirement benefits are determined as 1.7 percent prior to 2008 and 1.55 percent thereafter of the employee's final 3-year average compensation times the employee's years of service. Employees with 3 years of service are eligible to retire at age 55. Class B public safety benefits are determined as 2.4 percent for service prior to 2008 and 2.0 percent thereafter of employee final average compensation. Class B judicial benefits are determined as 3.733 percent for service prior to 2008 and 3.333 percent thereafter of employee final average compensation. All Class B employees with 3 years of service are eligible to retire at age 45. Employees are eligible for service-related disability benefits regardless of length of service. Three years of service is required for nonservice-related disability eligibility. Disability benefits are determined in the same manner as retirement benefits but are payable immediately without an actuarial reduction. Death benefits are a percent of the employee's final average salary.

The annual increase in the amount of the SDRS benefits payable on each July 1st is indexed to the consumer price index (CPI) based on SDRS funded status:

- If the SDRS market value funded ratio is 100% or more - 3.1% COLA
- If the SDRS market value funded ratio is 80.0% to 99.9%, index with the CPI
 - 90.0% to 99.9% funded - 2.1% minimum and 2.8% maximum COLA
 - 80.0% to 89.9% funded - 2.1% minimum and 2.4% maximum COLA
- If the SDRS market value funded ratio is less than 80% - 2.1% COLA

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017**

(8) Pension Plan (Continued)

The 2017 legislation modified the COLA, effective for the July 1, 2018 increase:

- Baseline actuarial accrued liabilities will be calculated assuming the COLA is equal to long-term inflation assumption of 2.25%.
- If the fair value of assets is greater or equal to the baseline actuarial accrued liabilities, the COLA will be:
 - The increase in the 3rd quarter CPI-W, no less than 0.5% and no greater than 3.5%.
- If the fair value of assets is less than the baseline actuarial accrued liabilities, the COLA will be:
 - The increase in the 3rd quarter CPI-W, no less than 0.5% and no greater than a restricted maximum such that, if the restricted maximum is assumed for future COLAs, the fair value of assets will be greater or equal to the accrued liabilities.

All benefits except those depending on the Member’s Accumulated Contributions are annually increased by the Cost-of-Living Adjustment.

Contributions:

Per SDCL 3-12, contribution requirements of the active employees and the participating employers are established and may be amended by the SDRS Board. Covered employees are required by state statute to contribute the following percentages of their salary to the plan; Class A Members, 6.0 percent of salary; Class B Judicial Members, 9.0 percent of salary; and Class B Public Safety Members, 8.0 percent of salary. State statute also requires the employer to contribute an amount equal to the employee’s contribution. State statute also requires the employer to make an additional contribution in the amount of 6.2 percent for any compensation exceeding the maximum taxable amount for social security for general employees only. The City’s share of contributions to the SDRS for the fiscal years ended December 31, 2017, 2016, and 2015 were \$299,638, \$293,505 and \$291,141 respectively, equal to the required contributions each year.

Pension Assets, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources to Pensions:

At June 30, 2017, SDRS is 100.10 percent funded and accordingly has a net pension asset. The proportionate shares of the components of the net pension asset of South Dakota Retirement System, for the City as of June 30, 2017 are as follows:

	Governmental Activities	Business-Type Activities	Total
Proportionate Share of Net Position Restricted for Pension Benefits	\$ 21,209,483	\$ 8,171,768	\$ 29,381,251
Less: Proportionate Share of Total Pension Asset	(21,192,953)	(8,165,399)	(29,358,352)
Proportionate Share of Net Pension Asset	\$ 16,530	\$ 6,369	\$ 22,899

At December 31, 2017, the City reported an asset of \$22,899 for its proportionate share of the net pension asset. The net pension asset was measured as of June 30, 2017, and the total pension asset used to calculate the net pension asset was based on a projection of the City’s share of contributions to the pension plan relative to the contributions of all participating entities. At June 30, 2017, the City’s proportion was 0.2523287 percent, which is a decrease of .0003 percent from its proportion measured as of June 30, 2016.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017**

(8) Pension Plan (Continued)

For the year ended December 31, 2017, the City recognized pension revenue of \$515,683. At December 31, 2017, the City reported deferred outflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between Expected and Actual Experience	\$ 366,908	\$ -
Changes in Assumption	1,777,972	-
Net Difference between Projected and Actual Earnings on Pension Plan Investments	(440,258)	-
Changes in Proportion and Difference between City Contributions and Proportionate Share of Contributions	-	-
City Contributions Subsequent to the Measurement Date	153,301	-
Total	\$ 1,857,923	\$ -

Deferred outflow of resources includes \$153,301 resulting from City contributions subsequent to the measurement date will be recognized as an increase of the net pension asset in the year ending December 31, 2018. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense (revenue) as follows:

2018	\$ 462,340
2019	776,165
2020	570,675
2021	(104,558)
	<u>\$ 1,704,622</u>

Actuarial Assumptions:

The total pension asset in the June 30, 2017 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	2.25 percent
Salary Increases	Graded by years of service, from 6.50 percent at entry to 3.00 percent
Investment Rate of Return	6.50 percent, net of pension plan investment expense

Mortality rates were based on 97 percent of the RP-2014 Mortality Table, projected generationally with Scale MP-2016, white collar rates for females and total dataset for males. Mortality rates for disabled members were based on the RP-2014 Disabled Retiree Mortality Table, projected generationally with Scale MP-2016.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2017**

(8) Pension Plan (Concluded)

Actuarial Assumptions (Continued):

Investment portfolio management is the statutory responsibility of the South Dakota Investment Council (SDIC), which may utilize the services of external money managers for management of a portion of the portfolio. SDIC is governed by the Prudent Man Rule (i.e., the council should use the same degree of care as a prudent man). Current SDIC investment policies dictate limits on the percentage of assets invested in various types of vehicles (equities, fixed income securities, real estate, cash, private equity, etc.). The long-term expected rate of return on pension plan investments was determined using a method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighing the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of real rates of return for each major asset class included in the pension plan’s target asset allocation as of June 30, 2017 (see the discussion of the pension plan’s investment policy) are summarized in the following table using geometric means:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
Global Equity	58.0%	4.8%
Fixed Income	30.0%	1.8%
Real Estate	10.0%	4.6%
Cash	2.0%	0.7%
	<u>100.0%</u>	

Discount Rate:

The discount rate used to measure the total pension asset was 6.50 percent. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the current contribution rate and that matching employer contributions will be made at rates equal to the member rate. Based on these assumptions, the pension plan’s fiduciary net position was projected to be available to make all future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension asset.

Sensitivity of Asset to Changes in the Discount Rate:

The following presents the City’s proportionate share of net pension liability/(asset) calculated using the discount rate of 6.50 percent, as well as what the District’s proportionate share of the net pension liability/(asset) would be if it were calculated using a discount rate that is 1-percentage point lower (5.50 percent) or 1-percentage point higher (7.50 percent) than the current rate:

	<u>1% Decrease</u>	<u>Current Discount Rate</u>	<u>1% Increase</u>
City’s Proportionate Share of the Net Pension (Asset)/Liability	\$ 4,193,964	\$ (22,899)	\$ (3,456,797)

Pension Plan Fiduciary Net Position:

Detailed information about the plan’s fiduciary net position is available in the separately issued SDRS financial report.

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2017

(9) Risk Management

The City 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. During the year ended December 31, 2017, the City managed its risks as follows:

Employee Health Insurance:

The City purchases health insurance for its employees from a commercial insurance carrier. Settled claims resulting from these risks have not exceeded the liability coverage during the past four years.

Liability Insurance:

The City joined the South Dakota Public Assurance Alliance (SDPAA), a public entity risk pool currently operating as a common risk management and insurance program for South Dakota local government entities. The objective of the SDPAA is to administer and provide risk management services and risk sharing facilities to the members and to defend and protect the members against liability, to advise members on loss control guidelines and procedures, and provide them with risk management services, loss control and risk reduction information and to obtain lower costs for that coverage. The City's responsibility is to promptly report to and cooperate with the SDPAA to resolve any incident which could result in a claim being made by or against the City. The City pays an annual premium to the pool to provide coverage for general liability, vehicle coverage, wrongful acts, and errors and omissions of public officials.

The agreement with the SDPAA provides that the above coverage will be provided to a \$2,000,000 limit. Member premiums are used by the pool for payment of claims and to pay for reinsurance for claims in excess of \$250,000 for property coverage and \$500,000 for liability coverage to the upper limit. The City carries a \$1,000 deductible for the wrongful acts coverage and auto coverage.

As of December 31, 2017, the City has a fully vested balance in the cumulative reserve fund of \$135,844. Access to this balance is restricted by SDPAA.

The City does not carry additional insurance to cover claims in excess of the upper limit. Settled claims resulting from the risks have not exceeded the liability coverage during the past four years.

Property and Building Insurance:

The City purchases property and building insurance from a commercial insurance carrier. Settled claims resulting from these risks have not exceeded the liability coverage during the past four years.

Worker's Compensation:

The City joined the South Dakota Municipal League Worker's Compensation Fund (the Fund), a public entity risk pool currently operating as a common risk management and insurance program for South Dakota local government entities. The objective of the Fund is to formulate, develop, and administer, on behalf of the member organizations, a program of worker's compensation coverage, to obtain lower costs for that coverage, and to develop a comprehensive loss control program. The City's responsibility is to initiate and maintain a safety program to give its employees safe and sanitary working conditions and to promptly report to and cooperate with the Fund to resolve any worker's compensation claims. The City pays an annual premium to provide worker's compensation coverage for its employees under a retrospectively rated policy, and the premiums are accrued based on the ultimate cost of the experience to date of the Fund members. Coverage limits are set by state statute. The pool pays the first \$650,000 of any claim per individual. The pool has reinsurance which covers up to \$2,000,000 per individual per incident. The City does not carry additional insurance to cover claims in excess of the upper limit. Settled claims resulting from these risks have never exceeded the liability coverage over the past four years.

Unemployment Benefits:

The City provides coverage for unemployment benefits by paying into the Unemployment Compensation Fund established by state law and managed by the State of South Dakota.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONCLUDED)
DECEMBER 31, 2017**

(10) Notes Receivable

Notes receivable are revolving loans the City makes to promote urban development. The following is a summary of the notes receivable at December 31, 2017:

Governmental:

<u>Loan</u>	<u>Collateral</u>	<u>Rate</u>	<u>Maturity</u>	<u>Balance</u>
Fickbohm	None	0%	October 1, 2019	\$ 1,804
Knuckle Brewery	Real Estate	3%	August 5, 2024	17,482
Sturgis ATV	Real Estate	3%	August 5, 2024	17,478
Jake's Garage	Real Estate	3%	December 5, 2024	18,263
Dakota Hardware	Real Estate, Inventory, Equipment	2%	November 1, 2024	70,570
Baldwin	Real Estate	3%	February 5, 2025	18,912
Dominos	Real Estate	3%	June 1, 2025	19,238
X-Treme Bikes	Inventory, Equipment, Cash	3%	April 1, 2026	84,666
Discovery Kids	Equipment, Cash	3%	August 1, 2026	164,977
				\$ 413,390

(11) Operating Leases

The City leases buildings under non-cancelable operating leases. Rent expense under these leases was \$200,000 for the year ended December 31, 2017.

Future minimum lease payments under the terms of these non-cancelable operating leases are as follows for the years ending December 31:

2018	\$ 200,000
2019	220,000
2020	220,000
\$ 640,000	

REQUIRED SUPPLEMENTARY INFORMATION

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CITY OF STURGIS

**BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2017**

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual - Budgetary Basis</u>	<u>Variance</u>
Revenue				
<i>Taxes:</i>				
311 General Property Taxes	\$ 2,847,350	\$ 2,847,350	\$ 2,848,336	\$ 986
313 General Sales and Use Taxes	2,125,585	2,125,585	1,987,248	(138,337)
315 Amusement Taxes	240	240	1,092	852
319 Penalties and Interest on Delinquent Taxes	8,800	8,800	12,007	3,207
320 Licenses and Permits	576,100	576,100	643,482	67,382
<i>Intergovernmental Revenue:</i>				
331 Federal Grants	-	-	53,542	53,542
334 State Grants	-	-	6,107	6,107
335.01 Bank Franchise Tax	10,000	10,000	12,082	2,082
335.03 Liquor Tax Reversion	41,000	41,000	43,057	2,057
335.04 Motor Vehicle Licenses	80,800	80,800	91,834	11,034
335.08 Local Government Highway and Bridge Fund	145,500	145,500	145,663	163
338.02 County Highway and Bridge Reserve Tax (25%)	5,855	5,855	5,855	-
338.04 Port of Entry	12,400	12,400	29,046	16,646
339 Other	4,400	4,400	5,033	633
<i>Charges for Goods and Services:</i>				
341 General Government	1,418,040	1,418,040	1,630,736	212,696
342 Public Safety	54,750	54,750	44,880	(9,870)
345 Health	1,800	1,800	7,981	6,181
346 Culture and Recreation	249,606	249,606	263,261	13,655
349 Other	-	-	7,787	7,787
<i>Fines and Forfeits:</i>				
351 Court Fines and Costs	6,000	6,000	8,130	2,130
<i>Miscellaneous Revenue:</i>				
361 Earnings on Deposits and Investments	175,000	175,000	125,934	(49,066)
362 Rentals/Airport Hangar Lease	29,700	29,700	17,716	(11,984)
367 Contributions and Donations - Private Sources	9,550	9,550	131,463	121,913
369 Other	1,200	1,200	10,196	8,996
Total Revenue	7,803,676	7,803,676	8,132,468	328,792

CITY OF STURGIS

BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS (CONTINUED)
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2017

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual - Budgetary Basis</u>	<u>Variance</u>
Expenditures				
<i>General Government:</i>				
411 Legislative	265,547	268,047	215,933	52,114
414 Financial Administration	1,222,421	1,241,375	1,242,328	(953)
419 Other	1,578,449	1,771,711	1,688,466	83,245
<i>Public Safety:</i>				
421 Police	1,896,880	2,057,517	2,052,665	4,852
422 Fire	152,908	152,908	131,406	21,502
<i>Public Works:</i>				
431 Highway and Streets	918,959	866,733	808,168	58,565
435 Airport	58,425	60,925	74,679	(13,754)
437 Cemeteries	122,078	122,078	105,840	16,238
<i>Culture and Recreation:</i>				
451 Recreation	719,694	744,194	755,681	(11,487)
452 Parks	681,993	655,403	491,581	163,822
455 Library	341,639	341,639	330,688	10,951
456 Auditorium	27,850	27,850	21,922	5,928
Total Expenditures	7,986,843	8,310,380	8,066,313	244,067
Excess of Revenue Over (Under) Expenditures	(183,167)	(506,704)	66,155	572,859
Other Financing Sources (Uses)				
391.01 Transfers In	110,000	11,000	110,000	99,000
391.04 Compensation for Loss or Damage to Capital Assets	-	-	2,681	2,681
511 Transfers Out	(12,000)	(12,000)	(87,975)	(75,975)
Total Other Financing Sources	98,000	(1,000)	24,706	25,706
Net Change in Fund Balance	(85,167)	(507,704)	90,861	598,565
Fund Balance, December 31, 2016	2,750,286	2,750,286	2,750,286	-
Fund Balance, December 31, 2017	\$ 2,665,119	\$ 2,242,582	\$ 2,841,147	\$ 598,565

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

CITY OF STURGIS

BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS
CAPITAL IMPROVEMENT FUND
FOR THE YEAR ENDED DECEMBER 31, 2017

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual - Budgetary Basis</u>	<u>Variance</u>
Revenue				
<i>Taxes:</i>				
313 General Sales and Use Taxes	\$ 1,571,085	\$ 1,571,085	\$ 1,496,889	\$ (74,196)
<i>Intergovernmental Revenue:</i>				
331 Federal Grants	-	-	1,005,705	1,005,705
334 State Grants	-	-	665,695	665,695
<i>Miscellaneous Revenue:</i>				
341 Rally Property Leases	255,000	255,000	153,500	(101,500)
367 Contributions and Donations	-	-	27,000	27,000
369 Other	-	-	25,000	25,000
Total Revenue	1,826,085	1,826,085	3,373,789	1,547,704
Expenditures				
<i>General Government:</i>				
414 Financial Administration	-	-	4,436	(4,436)
419 Other	230,000	247,890	177,066	70,824
<i>Public Safety:</i>				
422 Fire	21,000	22,000	21,297	703
<i>Public Works:</i>				
431 Highway and Streets	-	32,200	33,659	(1,459)
435 Airport	-	1,742	-	-
<i>Culture and Recreation:</i>				
451 Recreation	-	15,500	10,443	5,057
470 Debt Service	690,141	3,093,976	3,259,905	(165,929)
900 Capital Outlay	884,944	2,816,612	4,604,146	(1,787,534)
Total Expenditures	1,826,085	6,229,920	8,110,952	(1,882,774)
Excess of Revenue Over (Under) Expenditures	-	(4,403,835)	(4,737,163)	(335,070)
Other Financing Sources (Uses)				
391.01 Transfers In	-	-	75,975	75,975
391.29 Long-Term Debt Issued	-	3,513,813	4,333,313	819,500
Total Other Financing Sources (Uses)	-	3,513,813	4,409,288	895,475
Net Change in Fund Balance	-	(890,022)	(327,875)	560,405
Fund Balance, December 31, 2016	(304,669)	(304,669)	(304,669)	-
Fund Balance, December 31, 2017	\$ (304,669)	\$ (1,194,691)	\$ (632,544)	\$ 560,405

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

CITY OF STURGIS

BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS
REVOLVING LOAN FUND
FOR THE YEAR ENDED DECEMBER 31, 2017

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual - Budgetary Basis</u>	<u>Variance</u>
Revenue				
<i>Miscellaneous Revenue:</i>				
361 Investment Earnings	\$ 10,400	\$ 10,400	\$ 9,606	\$ (794)
Total Revenue	10,400	10,400	9,606	(794)
Expenditures				
419 Other	10,400	10,400	14,399	(3,999)
Net Change in Fund Balance	-	-	(4,793)	(4,793)
Fund Balance, December 31, 2016	1,312,610	1,312,610	1,312,610	-
Fund Balance, December 31, 2017	\$ 1,312,610	\$ 1,312,610	\$ 1,307,817	\$ (4,793)

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

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CITY OF STURGIS

**SCHEDULE OF THE CITY'S PROPORTIONATE SHARE OF THE NET PENSION ASSET (LIABILITY)
DECEMBER 31, 2017**

	<u>2017</u>	<u>2016</u>	<u>2015</u>
City's Proportion of the Net Pension Asset (Liability)	0.25232870%	0.25267720%	0.24867220%
City's Proportionate Share of Net Pension Asset (Liability)	\$ (22,899)	\$ (853,519)	\$ 1,054,689
City's Covered Payroll (Plan's Fiscal Year)	\$ 4,699,493	\$ 4,639,694	\$ 4,346,273
City's Proportionate Share of the Net Pension Asset (Liability) as a Percentage of its Covered Payroll	-0.49%	-18.40%	24.27%
Plan Fiduciary Net Position as a Percentage of the Total Pension Asset (Liability)	100.10%	96.89%	104.10%

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CITY OF STURGIS

**SCHEDULE OF THE CITY'S CONTRIBUTIONS
DECEMBER 31, 2017**

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Contractually Required Contribution	\$ 299,638	\$ 293,505	291,141
Contributions in Relation to the Contractually Required Contribution	299,638	293,505	291,141
Contribution Deficiency (Excess)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
City's Covered Payroll	\$ 4,789,633	\$ 4,705,530	4,686,344
Contributions as a Percentage of Covered Payroll	6.3%	6.2%	6.2%

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CITY OF STURGIS

**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
DECEMBER 31, 2017**

(1) Budgets and Budgetary Accounting

The City follows these procedures in establishing the budgetary data reflected in the financial statements:

1. At the first regular board meeting in September of each year or within ten days thereafter, the governing board introduces the annual appropriation ordinance for the ensuing fiscal year.
2. After adoption by the governing board, the operating budget is legally binding and actual disbursements for each purpose cannot exceed the amounts budgeted, except as indicated in item number 4.
3. A line item for contingencies may be included in the annual budget. Such line item may not exceed 5 percent of the total municipal budget and may be transferred by resolution of the governing board to any other budget category that is deemed insufficient during the year.
4. If it is determined during the year that sufficient amounts have not been budgeted, State statute allows the adoption of supplemental budgets.
5. Unexpended appropriations lapse at year end unless encumbered by resolution of the governing board.
6. The City did not encumber any amounts at December 31, 2017.
7. Formal budgetary integration is employed as a management control device during the year for the general fund and major special revenue funds.
8. Budgets for the general fund and major special revenue funds are adopted on a basis consistent with accounting principles generally accepted in the United States (USGAAP).

OTHER SUPPLEMENTARY INFORMATION

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CITY OF STURGIS

COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS
DECEMBER 31, 2017

	Special Sales Tax Fund	Library Fund	BID Fund	Alice W. Dunn Fund	Perpetual Maintenance Fund	Total Nonmajor Governmental Funds
Assets						
101 Cash	\$ 121,737	\$ 83,858	\$ 1,737	\$ 84,052	\$ 181,027	\$ 472,411
105 Savings Certificates	-	-	-	427,535	-	427,535
108 Sales Tax Receivable	22,929	-	-	-	-	22,929
115 Accounts Receivable	2,500	2,077	54	-	-	4,631
121 Special Assessments Receivable	-	-	24,412	-	-	24,412
151 Investment Held for Sale	608,100	-	-	-	-	608,100
Total Assets	\$ 755,266	\$ 85,935	\$ 26,203	\$ 511,587	\$ 181,027	\$ 1,560,018
Liabilities, Deferred Inflows of Resources, and Fund Balances						
<i>Liabilities</i>						
202 Accounts Payable	\$ 288	\$ -	\$ 1,590	\$ -	\$ -	\$ 1,878
216 Accrued Wages Payable	962	-	-	-	-	962
217 Accrued Taxes Payable	147	-	-	-	7	154
Total Liabilities	1,397	-	1,590	-	7	2,994
<i>Deferred Inflows of Resources</i>						
246 Unavailable Revenue - Special Assessments	-	-	24,412	-	-	24,412
<i>Fund Balances</i>						
263.51 Nonspendable - Perpetual Care Cemetery	-	-	-	-	50,000	50,000
263.99 Nonspendable - Library Trust	-	-	-	327,535	-	327,535
264.03 Restricted - Perpetual Care Cemetery	-	-	-	-	131,020	131,020
264.04 Restricted - BBB Tax	753,869	-	-	-	-	753,869
264.05 Restricted - Library Purposes	-	85,935	-	184,052	-	269,987
264.09 Restricted - BID Tax	-	-	201	-	-	201
Total Fund Balances	753,869	85,935	201	511,587	181,020	1,532,612
Total Liabilities, Deferred Inflows of Resources, and Fund Balances	\$ 755,266	\$ 85,935	\$ 26,203	\$ 511,587	\$ 181,027	\$ 1,560,018

CITY OF STURGIS

COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
 NONMAJOR GOVERNMENTAL FUNDS
 FOR THE YEAR ENDED DECEMBER 31, 2017

	Special Sales Tax Fund	Library Fund	BID Fund	Alice W. Dunn Fund	Perpetual Maintenance Fund	Total Nonmajor Governmental Funds
Revenue:						
313 General Sales and Use Taxes	\$ 344,353	\$ -	\$ -	\$ -	\$ -	\$ 344,353
319 Penalties and Interest on Delinquent Taxes	-	-	204	-	-	204
341 Charges for Goods and Services - General Government	-	-	17,000	-	-	17,000
361 Investment Earnings	-	37	-	4,955	-	4,992
363 Special Assessments	-	-	25,051	-	-	25,051
369 Other	59,502	11,165	4,297	-	5,624	80,588
Total Revenue	403,855	11,202	46,552	4,955	5,624	472,188
Expenditures:						
419 General Government - Other	-	-	54,842	-	-	54,842
460 Conservation and Development	376,373	-	-	-	-	376,373
Total Expenditures	376,373	-	54,842	-	-	431,215
Net Change in Fund Balances	27,482	11,202	(8,290)	4,955	5,624	40,973
Fund Balance, December 31, 2016	726,387	74,733	8,491	506,632	175,396	1,491,639
Fund Balance, December 31, 2017	\$ 753,869	\$ 85,935	\$ 201	\$ 511,587	\$ 181,020	\$ 1,532,612

CITY OF STURGIS

**SCHEDULE OF RALLY ACTIVITIES (UNAUDITED)
FOR THE YEAR ENDED DECEMBER 31, 2017**

Revenue

Taxes:

313 Sales Tax	\$ 590,408
320 Licenses and Permits	381,289

Charges for Goods and Services:

341 General Government	1,284,124
346 Culture & Recreation	9,298
344 Special Sanitation Fee	190,439

Total Revenue	2,455,558
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Expenditures

General Government:

419 Other	(1,322,723)
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Total Expenditures	(1,322,723)
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Excess of Revenue over Expenditures	\$ 1,132,835
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OTHER REPORTS

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Ketel Thorstenson, LLP

Certified Public Accountants/Business & Personal Consultants

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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*

City Council
City of Sturgis
Sturgis, South 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, the business-type activities, each major fund, and the aggregate remaining fund information of **CITY OF STURGIS** (the City) as of and for the year ended December 31, 2017, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated _____, 2018

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City'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'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 weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying Schedule of Findings, 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 City'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 as #2017-001 and #2017-002 to be material weaknesses.

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 deficiencies described in the accompanying Schedule of Findings as #2017-003, #2017-004 and #2017-005 to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free from 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 two instances of noncompliance or other matters that is described in the Schedule of Findings as #2017-004 and #2017-005 that are required to be reported under *Government Auditing Standards*.

City Council

City's Response to Findings

The City's response to the findings identified in our audit is described in the Schedule of Findings. The City's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the response.

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 results of that testing, and not to provide an opinion on the effectiveness of the City'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 City's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. As required by South Dakota Codified Law 4-11-11, this report is a matter of public record and its distribution is not limited.

KETEL THORSTENSON, LLP
Certified Public Accountants

_____, 2018

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CITY OF STURGIS

SCHEDULE OF FINDINGS FOR THE YEAR ENDED DECEMBER 31, 2017

MATERIAL WEAKNESSES

2017-001 FINDING: Financial Statement Preparation

Condition and Cause: As in prior years, we were requested to draft the audited financial statements and related footnote disclosures as part of our regular audit services. Ultimately, it is management's responsibility to provide for the preparation of the City's statements and footnotes, and the responsibility of the auditor to determine the fairness of presentation of those statements. From a practical standpoint, we do both for the City at the same time in connection with our audit. This is not unusual for us to do with municipalities of your size.

Criteria and Effect: This deficiency could result in a material misstatement to the financial statements that could have been prevented or detected by the City's management.

Repeat Finding from Prior Year: Yes, prior year finding 2016-001.

Recommendation: As in prior years, we have instructed management to review a draft of the auditor prepared financials in detail for their accuracy; we have answered any questions they might have, and have encouraged research of any accounting guidance in connection with the adequacy and appropriateness of classification and disclosure in the City's statements. We are satisfied that the appropriate steps have been taken to provide the City with the completed financial statements. It is the responsibility of management and those charged with governance to make the decision whether to accept the degree of risk associated with this condition because of cost or other considerations.

Response/Corrective Action Plan: See Corrective Action Plan.

2017-002 FINDING: Audit Adjustments

Condition and Cause: During the course of our engagement, we proposed material audit adjustments that were approved and recorded. Adjustments included adjustments to rollforward equity, to record accrued interest on TIF #12 debt, to adjust governmental capital assets, to reclassify sales proceeds, to adjust notes receivable, to adjust the allowance for doubtful accounts in the ambulance fund, to record loan and grants for the Main Street reconstruction project, and to record adjustments for pension activity. Additionally, we proposed reclassification entries with no effect on net income. Furthermore, other entries were proposed as a part of the audit, but were not recorded due to the overall insignificance on the financial statements.

Criteria and Effect: These adjustments would not have been identified as a result of the City's existing internal controls, and therefore, could have resulted in a material misstatement of the City's financial statements.

Repeat Finding from Prior Year: Yes, prior year finding 2016-002.

Recommendation: We recommend that management consider the following:

- a. The City should consider obtaining assistance, prior to the audit, to ensure accuracy of general ledger information. Specifically, the City should consider assistance with the recording of capital assets and long-term debt.
- b. Capital assets should be reviewed to make sure all additions and disposals are properly reflected, including the activity within TIF Funds. During the course of the year, the City should reconcile capital assets, at a minimum, on a quarterly basis.
- c. The Ambulance Fund receivables should continue to be analyzed for collectability and adjusted on a regular basis.

Response/Corrective Action Plan: The City agrees with the above finding. See Corrective Action Plan.

CITY OF STURGIS

**SCHEDULE OF FINDINGS (CONTINUED)
FOR THE YEAR ENDED DECEMBER 31, 2017**

SIGNIFICANT DEFICIENCIES

2017-003 FINDING: Internal Controls

Condition and Cause: The Finance Officer and Senior Accountant have access to the general ledger and prepare and post journal entries. Journal entries are not reviewed before they are posted.

Criteria and Effect: Journal entries posted by the Finance Officer or Senior Accountant may not be supported by appropriate documentation, or have a greater risk of being posted incorrectly without adequate review procedures.

Repeat Finding from Prior Year: Yes, prior year finding 2016-004.

Recommendation: The Finance Officer should review journal entries proposed by the Senior Accountant prior to posting. Additionally, the Senior Accountant or a City Manager should review the journal entries proposed by the Finance Officer prior to posting.

Response/Corrective Action Plan: The City agrees with the above finding. See Corrective Action Plan.

2017-004 FINDING: Certificates of Deposit

Condition and Cause: The City is invested in participating and negotiable certificates of deposit.

Criteria and Effect: South Dakota Codified Law 4-5-6 indicates the types of investments that the City may invest public funds. Based on 4-5-6, the City is in violation of State law.

Repeat Finding from Prior Year: Yes, prior year finding 2016-006.

Recommendation: We recommend that the City re-evaluate their investment policy and invest these funds in investments allowed by SDCL 4-5-6.

Response/Corrective Action Plan: The City agrees with the above finding. See City's Corrective Action Plan.

2017-005 FINDING: Budget Overdraft

Condition and Cause: The City has a budgetary overdraft in violation of South Dakota Codified Law 9-21-9, in the following departments:

Fund	Department	Overdraft
General	Airport	\$ (13,754)
General	Recreation	(11,487)
Capital Improvement	Financial Administration	(4,436)
Capital Improvement	Highways and Streets	(1,459)
Capital Improvement	Debt Service	(165,929)
Capital Improvement	Capital Outlay	(1,787,534)
Revolving Loan Fund	Other	(3,999)

Criteria and Effect: The City did not follow state law, which could result in additional inquiries from state officials regarding such violation.

Repeat Finding from Prior Year: No.

Recommendation: The City should complete supplemental appropriations for unbudgeted expenditures.

Response/Corrective Action Plan: The City agrees with the above finding. See City's Corrective Action Plan.

MANAGEMENT RESPONSE

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**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
DECEMBER 31, 2017**

The City of Sturgis respectfully submits the following summary schedule of prior audit findings from December 31, 2016 Schedule of Findings. The findings are numbered consistently with the numbers assigned in the 2016 Schedule of Findings.

2016-001 FINDING: Financial Statement Preparation

Status: It is more cost effective for the City to hire Ketel Thorstenson, LLP, a public accounting firm, to prepare the full disclosure financial statements as a part of the annual audit process. The City has designated a member of management to review the draft financial statements and accompanying notes to the financial statements.

Initial Year Report: Originally issued years ago.

Reasons for Recurrence and Corrective Action Plan: As the City has accepted the risk associated with the auditor's preparing of the financial statements, it will be repeated in 2017, see Corrective Action Plan.

2016-002 FINDING: Audit Adjustments

Status: The City made efforts to record all year-end entries, but several audit adjustments were made.

Initial Year Report: Originally issued years ago. The

Reasons for Recurrence and Corrective Action Plan: The finding is altered based on specific audit adjustments each year, but is repeated in the Schedule of Findings. See Corrective Action Plan.

2016-003 FINDING: Liquor Store Internal Controls

Status: In 2016, the City implemented new liquor store software which caused pricing and quantity issues at year end. The City also had a deficiency in segregation of duties due to limited personnel.

Initial Year Report: Originally issued in 2015. During 2017, the liquor store internal controls were revised to address the 2016 audit finding. The finding is not repeated in 2017.

2016-004 FINDING: Internal Controls

Status: During the course of the year, the Finance Officer had access to the general ledger, prepared and posted journal entries, had access to check stock, was a check signer and also reconciled the bank statement.

Initial Year Report: Originally issued years ago.

Reasons for Recurrence and Corrective Action Plan: During 2017, several internal controls were revised, however, not all recommendations were implemented. This finding is altered and repeated in 2017.



**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS (CONTINUED)
DECEMBER 31, 2017**

2016-005 FINDING: Bank Reconciliations

Status: The bank reconciliations for the First Interstate checking account did not agree to the general ledger by \$1,403. The Library bank account did not agree to the general ledger by \$615.

Initial Year Report: Originally issued in 2016.

2016-006: FINDING: Certificates of Deposit

Status: The City is invested in participating and negotiable certificates of deposit which are in violation of South Dakota Codified Law 4-5-6.

Initial Year Report: Originally issued in 2016.

Reasons for Recurrence and Corrective Action Plan: The existing certificates of deposit have not matured. As the certificates of deposit mature, the City will re-evaluate the investment policy and determine if there is a more appropriate investment strategy.

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**CORRECTIVE ACTION PLAN
DECEMBER 31, 2017**

The City respectfully submits the following corrective action plan regarding findings from December 31, 2017 Schedule of Findings. The findings are numbered consistently with the numbers assigned in the Schedule of Findings.

2017-001 FINDING: Financial Statement Preparation

Responsible Officials: Fay Bueno, Finance Officer

Corrective Action Plan: The City has accepted the risk associated with Finding #2017-001 regarding the preparation of the financial statements, and will continue to have the independent auditor prepare the annual financial statements. For future audits, Finance Officer, Fay Bueno, and the Senior Accountant, Dotti Oldenkamp, will continue to monitor the financial statement preparation process.

Anticipated Completion Date: Ongoing

2017-002 FINDING: Audit Adjustments

Responsible Officials: Fay Bueno, Finance Officer

Corrective Action Plan: The City will make every effort to make accurate accounting adjustments throughout the year. When recording a journal entry that is unfamiliar to the Finance Officer or Senior Accountant, they will request assistance of the auditor. Capital assets will be reviewed monthly by the Finance Officer and capitalized in a timely manner. The ambulance receivables are being analyzed and adjusted by the Senior Accountant on a monthly basis.

Anticipated Completion Date: Ongoing

2017-003 FINDING: Internal Controls

Responsible Officials: Fay Bueno, Finance Officer

Corrective Action Plan: The Finance Officer and Senior Accountant will review each other's journal entries before posting. All appropriate documentation will be accompanied by a sign-off sheet.

Anticipated Completion Date: August 2018.

2017-004 FINDING: Certificates of Deposit

Responsible Officials: Fay Bueno, Finance Officer

Corrective Action Plan: As the certificates of deposit mature, the City will re-evaluate the investment policy and determine if there is a more appropriate investment strategy.

Anticipated Completion Date: As certificates of deposit mature.



**CORRECTIVE ACTION PLAN (CONTINUED)
DECEMBER 31, 2017**

2017-004 FINDING: Budgetary Overdraft

Responsible Officials: Fay Bueno, Finance Officer

Corrective Action Plan: In the future the City will perform supplemental appropriations for overspent budget line items.

Anticipated Completion Date: December 2018.

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