

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

YEAR ENDED DECEMBER 31, 2016

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

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INTRODUCTORY SECTION

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

ORGANIZATION SCHEDULE
DECEMBER 31, 2016

<u>City Council</u>	<u>Position</u>	<u>Term Expires</u>
Elected		
Judy Humeniuk ¹	Mayor	December 31, 2016
Brock Stebakken	Councilmember	December 31, 2018
Greg Johnson	Councilmember	December 31, 2018
Kent Hanson ²	Councilmember	December 31, 2016
Steve Johnson	Councilmember	December 31, 2020
Appointed		
Tina Rennemo	Clerk-Treasurer	Indefinite

¹ Replaced by Rick Rone. Term expires 12/31/2018.

² Replaced by Marla Carlson. Term expires 12/31/2020.

FINANCIAL SECTION

Colleen Hoffman, Director
Crystelle Philipp, CPA
Marit Knutson, CPA



Hoffman, Philipp, & Knutson, PLLC

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INDEPENDENT AUDITOR'S REPORT

City Council
City of Baudette

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 Baudette, Minnesota, as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit 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 City'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 City'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.

Basis for Qualified Opinion on Governmental Activities

Management has not adopted the provisions of Governmental Accounting Standards Board Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27* for the Fire Relief Association. Accounting principles generally accepted in the United States of America require that GASB Statement No. 68 be adopted for governmental activities, including Fire Relief Associations. The amount by which this departure would affect the assets, net position, and revenues of the governmental activities has not been determined.

Unmodified Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities, each major fund, and the aggregate remaining fund information of the City of Baudette, Minnesota, as of December 31, 2016, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

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

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Baudette's basic financial statements. The introductory section, the supplementary information, and the other schedules section, as listed in the table of contents, are presented for purposes of additional analysis and are not a required part of the basic financial statements. The supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements as a whole. The introductory and other schedules sections have 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 them.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 13, 2017, on our consideration of the City of Baudette's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's internal control over financial reporting and compliance.

A handwritten signature in blue ink that reads "Hoffman, Philipp, & Knutson". The signature is written in a cursive style.

Hoffman, Philipp, & Knutson, PLLC

June 13, 2017

City of Baudette
Office of the Clerk-Treasurer

106 Main Street West – P.O. Box 548 – Baudette, Minnesota 56623

Phone (218) 634-1850 Fax (218) 634-2942

MANAGEMENT'S DISCUSSION AND ANALYSIS
(Unaudited)

The management of the City of Baudette offers readers of the City's Financial Statements this narrative overview and analysis of the financial activities of the City of Baudette for the fiscal year ended December 31, 2016. The Management's Discussion and Analysis provides comparisons with the previous year and is designed to focus on the current year's activities, resulting changes, and currently known facts, and should be read in conjunction with the City's basic financial statements that follow this section.

FINANCIAL HIGHLIGHTS

During the current year, the City of Baudette adopted the accounting principles discussed in further detail in the Notes to the Financial Statements. Such accounting principles have been adopted prospectively, and therefore, comparative information in this section has not been restated to reflect the effect of the adoption of these accounting principles.

The total net position of governmental activities is \$2,916,913, of which \$2,050,240 is the net investment in capital assets, \$156,958 is restricted for economic development, and \$709,715 is unrestricted. The total net position of governmental activities decreased by \$90,703 for the year ended December 31, 2016. This decrease was primarily attributed to the increase in net pension liability.

The total net position of business-type activities is \$8,322,486, of which \$4,886,211 is the net investment in capital assets and \$3,436,275 is unrestricted. The total net position of business-type activities increased by \$167,186 in 2016, as a result of the refunding of long term debt. For the year ended December 31, 2016, the City has elected to report Utility Funds separately as the Electric Enterprise Fund, the Sewer Enterprise Fund, and the Water Enterprise Fund. This will enable the City Council to more accurately monitor the performance in each area of City utilities.

At the close of 2016, the City's General Fund reported an ending fund balance of \$1,284,782, a decrease of \$75,341, from the prior year. Of the total fund balance amount, \$30,586 is non-spendable, \$156,958 is restricted for specific purposes, \$727,745 is assigned for specific purposes, and \$369,493 is noted as unassigned fund balance. Maintaining an adequate fund balance is necessary to provide City services throughout the year.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the City's basic financial statements, which are comprised of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements.



The City of Baudette is an Equal Opportunity Employer

Government-Wide Financial Statements

The government-wide financial statements are designed to provide readers with a broad overview of the City's finances. These statements include all assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private-sector businesses. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

The *Statement of Net Position* presents information on all of the City's assets and liabilities, with the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the City is improving or deteriorating.

The *Statement of Activities* presents information showing how the government's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes).

In the *Statement of Net Position* and the *Statement of Activities*, we divide the City into two kinds of activities:

- Governmental activities—Most of the City's basic services are reported here, including general government, public safety, highways and streets, culture and recreation, and economic development. Property taxes and intergovernmental revenues finance most of these activities.
- Business-type activities—The City charges fees to cover the costs of certain services it provides. Included here are the operations of the municipal liquor store and the utilities – electric, sewer and water.

The government-wide financial statements can be found as Exhibits 1 and 2 of this report.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City of Baudette, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City can be divided into two categories: governmental funds and proprietary funds.

Governmental Funds Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, fund-level financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's short-term financing decisions.

Both the Balance Sheet – Governmental Funds and the Statement of Revenues, Expenditures, and Changes in Fund Balances – Governmental Funds provide a reconciliation to facilitate the comparison between governmental funds and governmental activities.

The City reports one governmental fund, the General Fund, in the Governmental Funds Balance Sheet and in the Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances. The General Fund is considered to be a major fund.

The City of Baudette adopts an annual budget for its General Fund. A budgetary comparison schedule has been provided for this fund to demonstrate compliance with its budget.

Proprietary Funds The City of Baudette maintains four proprietary funds. (1) The Electric Enterprise Fund is used to account for the operations of the City’s Electric department. Financing is provided by charges to residents for services (2) The Liquor Enterprise Fund is used to account for the City’s liquor store. Financing is provided through the liquor store’s sale of on and off-sale liquor. (3) The Sewer Enterprise Fund is used to account for the operations of the City’s sewer department. Financing is provided by charges to residents for services. (4) The Water Enterprise Fund is used to account for the operations of the City’s water department. Financing is provided by charges to residents for services. Proprietary funds provide the same type of information as the government-wide financial statements, and are included in the Statement of Net Position and the Statement of Activities as business-type activities. All of the enterprise funds are considered to be major funds.

Notes to the Financial Statements

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found beginning on page 24 of this report.

Other information—In addition to the basic financial statements and accompanying notes, this report also presents certain *required supplementary information*. The City also provides other information including a schedule of intergovernmental revenue.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Over time, net position serves as a useful indicator of the City’s financial position. The City’s assets exceeded liabilities by \$11,239,399 at the close of 2016. The largest portion of the City’s net position (approximately 62 percent) reflects its net investment in capital assets (i.e., land, construction in progress, infrastructure, buildings, and machinery and equipment). It should be noted that this amount is not available for future spending. One percent of the City’s net position is restricted for economic development and approximately 37 percent of the City’s net position is unrestricted. The unrestricted net position amount of \$4,145,990 as of December 31, 2016, may be used to meet the City’s ongoing obligations to citizens.

The City’s overall financial position increased from last year. Total assets increased by \$2,286,094 from the prior year, primarily as a result of the operating income in the Electric Enterprise Fund and project construction. Total liabilities increased by \$2,835,899 from the prior year, primarily due to the issuance of bonds for a street, sewer, and water project. This resulted in a decreased net position of \$76,483 from the prior year.

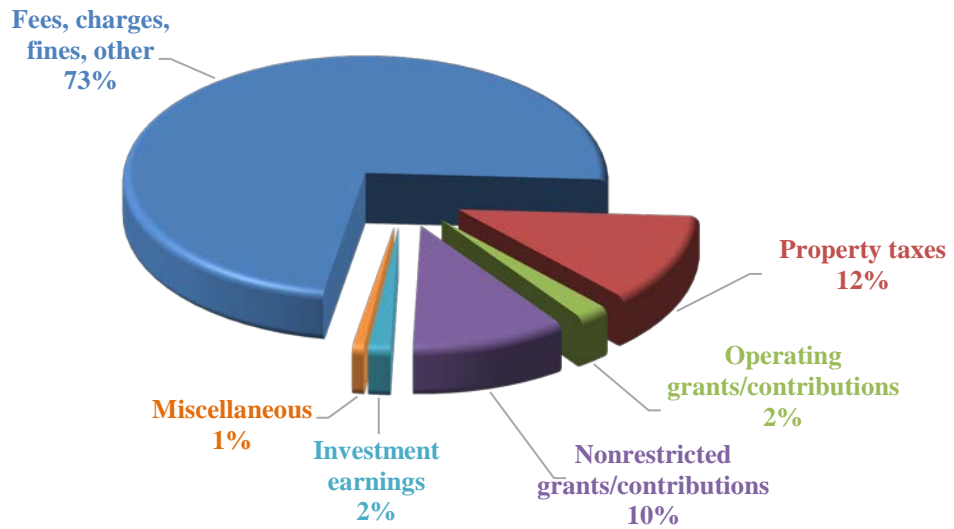
NET POSITION

	Governmental Activities		Business-Type Activities		Total	
	2016	2015	2016	2015	2016	2015
Current and other assets	\$ 1,368,125	\$ 1,242,909	\$ 3,995,849	\$ 2,965,245	\$ 5,363,974	\$ 4,208,154
Capital assets	2,443,477	2,097,949	8,315,211	7,530,465	10,758,688	9,628,414
Total assets	\$ 3,811,602	\$ 3,340,858	\$ 12,311,060	\$ 10,495,710	\$ 16,122,662	\$ 13,836,568
Deferred outflows - pensions	\$ 583,603	\$ 84,243	\$ 239,304	\$ 49,553	\$ 822,907	\$ 133,796
Other liabilities	\$ 83,102	\$ 23,393	\$ 130,448	\$ 159,098	\$ 213,550	\$ 182,491
Long-term liabilities outstanding	1,304,914	356,591	4,069,534	2,213,017	5,374,448	2,569,608
Total liabilities	\$ 1,388,016	\$ 379,984	\$ 4,199,982	\$ 2,372,115	\$ 5,587,998	\$ 2,752,099
Deferred inflows - pensions	\$ 90,276	\$ 37,501	\$ 45,726	\$ 17,848	\$ 136,002	\$ 55,349
Net position						
Net investment in capital assets	\$ 2,050,240	\$ 2,082,207	\$ 4,886,211	\$ 5,671,465	\$ 6,936,451	\$ 7,753,672
Restricted	156,958	75,659	-	-	156,958	75,659
Unrestricted	709,715	849,750	3,436,275	2,483,835	4,145,990	3,333,585
Total net position	\$ 2,916,913	\$ 3,007,616	\$ 8,322,486	\$ 8,155,300	\$ 11,239,399	\$ 11,162,916

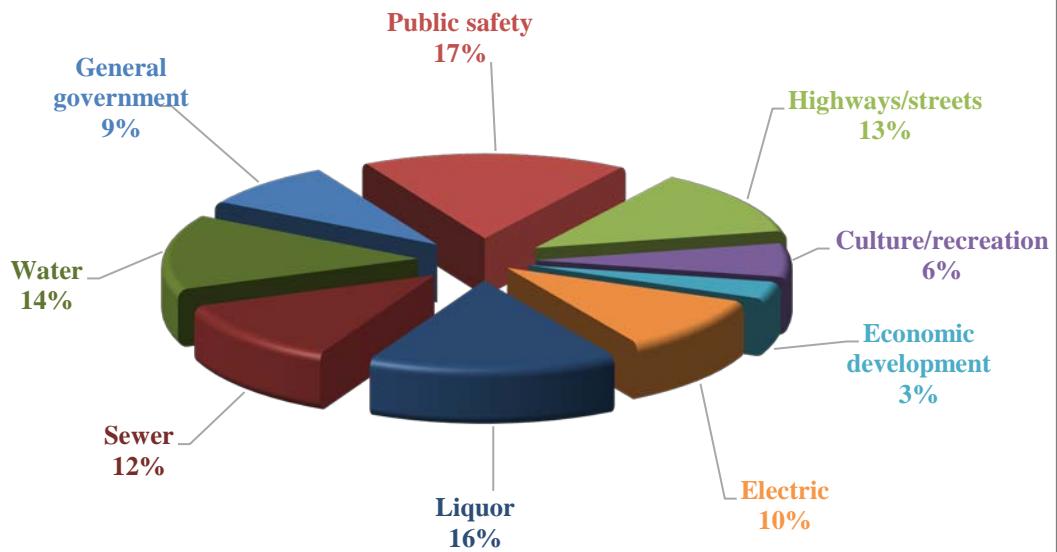
CHANGES IN NET POSITION

	Governmental Activities		Business-Type Activities		Total	
	2016	2015	2016	2015	2016	2015
Revenues						
Program Revenues						
Fees, charges, fines and other	\$ 133,284	\$ 141,726	\$ 4,667,503	\$ 4,408,268	\$ 4,800,787	\$ 4,549,994
Operating grants and contributions	62,356	353,732	-	-	62,356	353,732
Capital grants and contributions	2,352	-	-	-	2,352	-
General Revenues and Transfers						
Property taxes	359,273	321,373	-	-	359,273	321,373
Grants and contributions not restricted to specific programs	304,970	304,535	-	-	304,970	304,535
Investment earnings	-	4,247	43,710	27,998	43,710	32,245
Miscellaneous	-	-	20,452	-	20,452	-
Transfers	370,000	345,000	(370,000)	(345,000)	-	-
Total revenues	\$ 1,232,235	\$ 1,470,613	\$ 4,361,665	\$ 4,091,266	\$ 5,593,900	\$ 5,561,879
Expenses						
General government	\$ 239,301	\$ 237,346	\$ -	\$ -	\$ 239,301	\$ 237,346
Public safety	469,300	379,320	-	-	469,300	379,320
Highways and streets	342,598	305,327	-	-	342,598	305,327
Culture and recreation	172,893	182,528	-	-	172,893	182,528
Economic development	88,354	65,700	-	-	88,354	65,700
Interest	10,492	748	-	-	10,492	748
Electric	-	-	1,929,440	-	1,929,440	-
Liquor	-	-	1,427,109	1,383,017	1,427,109	1,383,017
Sewer	-	-	390,949	-	390,949	-
Utility	-	-	-	2,547,008	-	2,547,008
Water	-	-	446,981	-	446,981	-
Total expenses	\$ 1,322,938	\$ 1,170,969	\$ 4,194,479	\$ 3,930,025	\$ 5,517,417	\$ 5,100,994
Increase (decrease) in net position	\$ (90,703)	\$ 299,644	\$ 167,186	\$ 161,241	\$ 76,483	\$ 460,885
Net position, January 1, as previously reported	\$ 3,007,616	\$ 2,986,450	\$ 8,155,300	\$ 8,301,043	\$ 11,162,916	\$ 11,287,493
Prior period adjustment	-	(278,478)	-	(306,984)	-	(585,462)
Net position, January 1	\$ 3,007,616	\$ 2,707,972	\$ 8,155,300	\$ 7,994,059	\$ 11,162,916	\$ 10,702,031

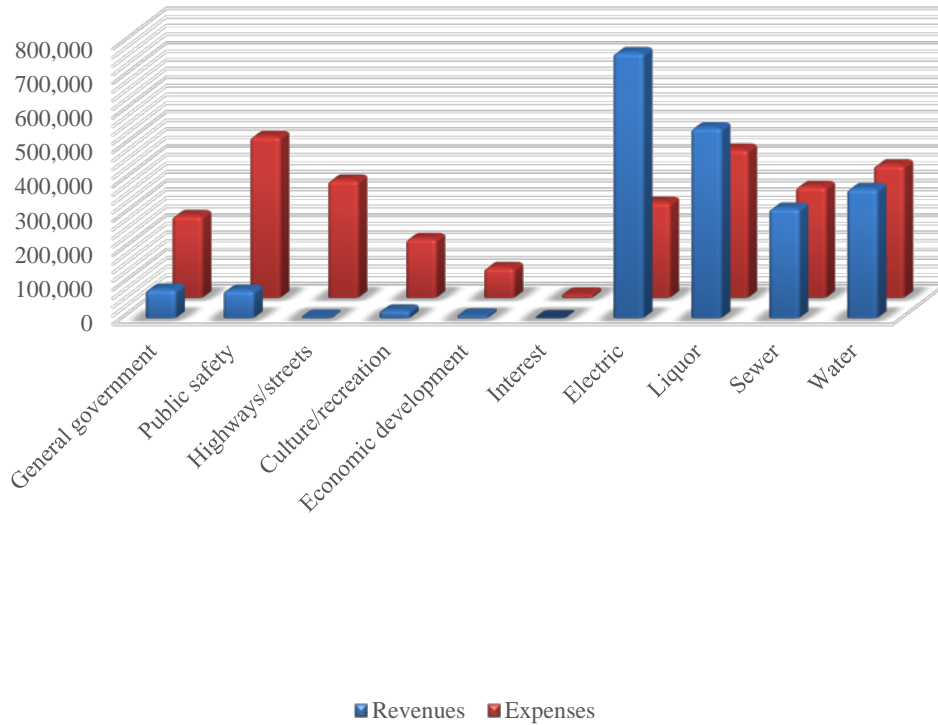
Revenues by Source



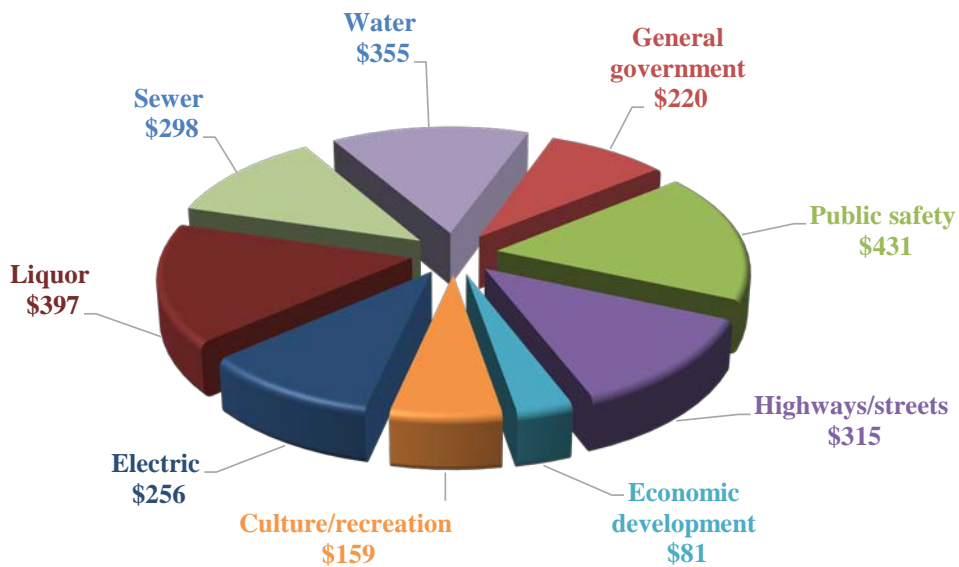
Expenses by Function



Program Revenues & Expenses



Expenditures Per Capita 1,088 Population as of April 1, 2016



FINANCIAL ANALYSIS OF THE GOVERNMENT'S FUNDS

As noted earlier, the City uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements, with a focus on short-term inflows, outflows, and balances of spendable resources. In particular, unrestricted fund balance may serve as a useful measure of the City's net resources available for spending at the end of the fiscal year.

Governmental Fund

At the end of 2016, the City's General Fund reported ending fund balances of \$1,284,782. Of this amount, approximately 2 percent constitutes non-spendable fund balance, 12 percent constitutes legally or contractually restricted fund balance, 57 percent constitutes specifically assigned fund balance, and 29 percent constitutes unassigned fund balance.

The General Fund is the operating fund of the City. As a measure of the General Fund's liquidity, it is useful to compare both unrestricted fund balance and total fund balance to total fund expenditures for 2016. Unrestricted fund balance represents 81 percent of total General Fund expenditures, while total fund balance represents 83 percent of that same amount.

In 2016, the fund balance amount in the General Fund increased by \$75,341. This increase is primarily attributed to a transfer of \$220,000 from the Electric Enterprise Fund and \$150,000 from the Liquor Enterprise Fund.

Proprietary Funds

The Electric Enterprise Fund reported an operating income in 2016 of \$492,842 as a result of budgeted projects that were not completed, and a reduction of utility expense for City services. Minnkota Power did not raise utility rates as high as anticipated in 2016.

The Liquor Enterprise Fund reported an operating income in 2016 of \$121,449, indicating that it is charging for products and services at a strong margin for this type of business.

The Sewer Enterprise Fund reported an operating loss in 2016 of \$4,252, indicating that it is not collecting fees for services at a rate higher than current expenses.

The Water Enterprise Fund reported an operating loss in 2016 of \$9,617, indicating that it is not collecting fees for services at a rate higher than expenses.

GENERAL FUND BUDGETARY HIGHLIGHTS

Budget amendments were approved for 2016. They include a \$45,400 increase in the revenue budget and \$276,850 increase in the expenditures budget.

Actual revenues were less than overall final budgeted revenues by \$41,434, with the largest negative variance in miscellaneous revenue. Actual expenditures were less than overall final budgeted expenditures by \$32,701.

CAPITAL ASSETS AND LONG-TERM DEBT

Capital Assets

The City's investment in capital assets for its governmental and business-type activities as of December 31, 2016, amounted to \$10,758,688 (net of accumulated depreciation). The total increase in the City's investment in capital assets for the current fiscal year was approximately four percent. This increase was primarily due to the completion of the water system project and reduction of asset related debt.

	Governmental Activities		Business-Type Activities		Total	
	2016	2015	2016	2015	2016	2015
Land	\$ 222,328	\$ 222,328	\$ 81,418	\$ 81,418	\$ 303,746	\$ 303,746
Construction in progress	402,093	-	1,084,906	42,330	1,486,999	42,330
Infrastructure	1,035,754	1,107,810	6,895,663	7,214,000	7,931,417	8,321,810
Buildings	511,130	539,439	95,051	101,603	606,181	641,042
Machinery and equipment	272,172	228,372	158,173	91,114	430,345	319,486
Total capital assets	<u>\$ 2,443,477</u>	<u>\$ 2,097,949</u>	<u>\$ 8,315,211</u>	<u>\$ 7,530,465</u>	<u>\$ 10,758,688</u>	<u>\$ 9,628,414</u>

Additional information on the City's capital assets can be found in the notes to the financial statements.

Long-Term Debt

At the end of the current fiscal year, the City had total debt outstanding of \$3,822,237 which is backed by the full faith and credit of the government.

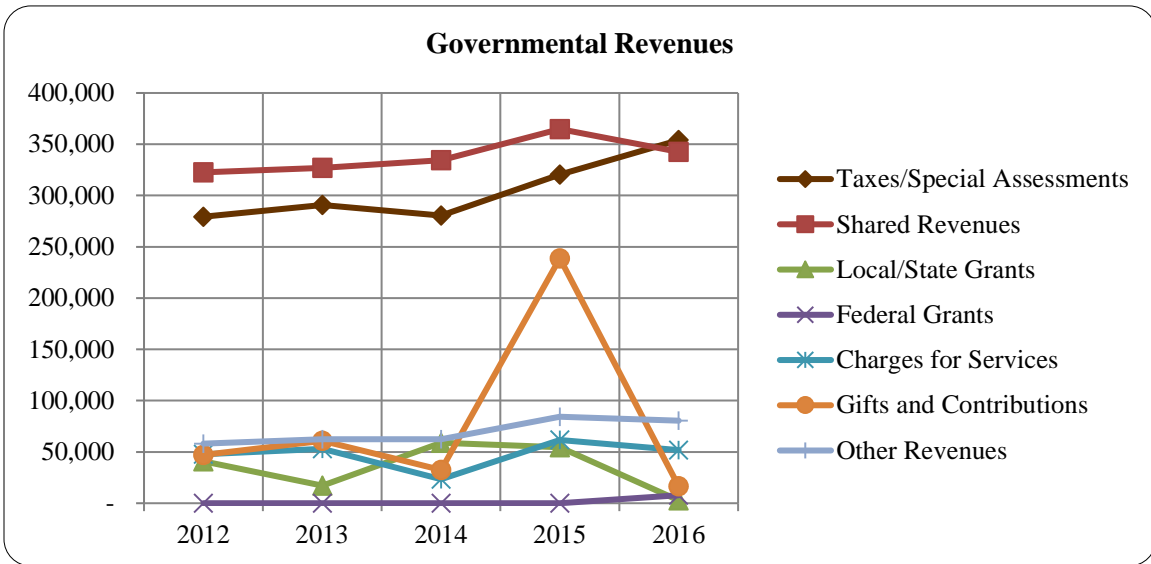
	Governmental Activities		Business-Type Activities		Total	
	2016	2015	2016	2015	2016	2015
G.O. Bonds of 2002	\$ -	\$ -	\$ -	\$ 791,000	\$ -	\$ 791,000
G.O. Revenue Notes of 2008	-	-	365,000	400,000	365,000	400,000
G.O. Refunding Bonds of 2016	355,000	-	2,445,000	-	2,800,000	-
MPFA Loans	-	-	619,000	668,000	619,000	668,000
Capital Equipment Note	38,237	15,742	-	-	38,237	15,742
	<u>\$ 393,237</u>	<u>\$ 15,742</u>	<u>\$ 3,429,000</u>	<u>\$ 1,859,000</u>	<u>\$ 3,822,237</u>	<u>\$ 1,874,742</u>

Minnesota Statutes limit the amount of debt that the City may have to three percent of its total market value, excluding revenue bonds. At the end of 2016, overall debt of the City is below the three percent debt limit.

Additional information on the City's long-term debt can be found in the notes to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

- The City depends on financial resources flowing from, or associated with, both the Federal Government and the State of Minnesota. Because of this dependency, the City is subject to changes in specific flows of intergovernmental revenues based on modifications to Federal and State laws and Federal and State appropriations. It is also subject to changes in investment earnings and asset values associated with U.S. Treasury Securities because of actions by foreign governments and other holders of publicly held U.S. Treasury Securities. The analysis below focuses on the revenues of the City's governmental funds taken from Exhibit 5 and the Schedule of Intergovernmental Revenue.



- Specific unemployment statistics for the City of Baudette are not available. However, the unemployment rate for Lake of the Woods County was 6 percent as of December 31, 2016. This is higher than the statewide rate of 4.1 percent and higher than the national average rate of 4.5 percent.
- Baudette's population as of April 1, 2016, was 1,088, a decrease of 18 since the 2010 census of 1,106.

On December 12, 2016, the City of Baudette set its 2017 revenue and expenditure budgets.

REQUESTS FOR INFORMATION

This annual financial report is designed to provide a general overview of the City of Baudette for all those with an interest in the City's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the City of Baudette Clerk-Treasurer, City Hall, P.O. Box 548, Baudette, Minnesota 56623.

BASIC FINANCIAL STATEMENTS

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

EXHIBIT 1

**STATEMENT OF NET POSITION
DECEMBER 31, 2016**

	Governmental Activities	Business-type Activities	Total
<u>Assets</u>			
Cash and pooled investments	\$ 756,207	\$ 1,682,250	\$ 2,438,457
Investments	553,693	1,489,237	2,042,930
Taxes receivable			
Current	8,693	-	8,693
Prior	15,325	-	15,325
Delinquent special assessments receivable	240	-	240
Accounts receivable	3,381	342,627	346,008
Loans receivable	30,586	-	30,586
Inventory	-	475,488	475,488
Prepaid items	-	6,247	6,247
Capital assets			
Non-depreciable	624,421	1,166,324	1,790,745
Depreciable - net of accumulated depreciation	1,819,056	7,148,887	8,967,943
Total Assets	\$ 3,811,602	\$ 12,311,060	\$ 16,122,662
<u>Deferred Outflows of Resources</u>			
Related to pensions	\$ 583,603	\$ 239,304	\$ 822,907
<u>Liabilities</u>			
Accounts payable	\$ 49,300	\$ 46,711	\$ 96,011
Salaries payable	18,315	17,604	35,919
Compensated absences payable	12,808	17,830	30,638
Due to other governments	163	23,908	24,071
Accrued interest payable	2,516	12,970	15,486
Customer deposits payable	-	11,425	11,425
Long-term liabilities			
Due within one year	15,181	107,830	123,011
Due in more than one year	1,289,733	3,961,704	5,251,437
Total Liabilities	\$ 1,388,016	\$ 4,199,982	\$ 5,587,998
<u>Deferred Inflows of Resources</u>			
Related to pensions	\$ 90,276	\$ 45,726	\$ 136,002
<u>Net Position</u>			
Net investment in capital assets	\$ 2,050,240	\$ 4,886,211	\$ 6,936,451
Amounts restricted for economic development	156,958	-	156,958
Unrestricted amounts	709,715	3,436,275	4,145,990
Total Net Position	\$ 2,916,913	\$ 8,322,486	\$ 11,239,399

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

**STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2016**

	Expenses	Program Revenues	
		Fees, Charges, Fines and Other	Operating Grants and Contributions
Functions/Programs			
Governmental activities			
General government	\$ 239,301	\$ 84,215	\$ -
Public safety	469,300	26,182	53,086
Highways and streets	342,598	382	1,500
Culture and recreation	172,893	22,382	-
Economic development	88,354	123	7,770
Interest	10,492	-	-
Total governmental activities	\$ 1,322,938	\$ 133,284	\$ 62,356
Business-type activities			
Electric	\$ 1,929,440	\$ 2,422,282	\$ -
Liquor	1,427,109	1,548,558	-
Sewer	390,949	319,791	-
Water	446,981	376,872	-
Total business-type activities	\$ 4,194,479	\$ 4,667,503	\$ -
Total	\$ 5,517,417	\$ 4,800,787	\$ 62,356

General revenues and transfers

Property taxes
Grants and contributions not restricted to specific programs
Investment earnings
Miscellaneous
Transfers

Total general revenues and transfers

Change in net position

Net Position - January 1

Net Position - December 31

EXHIBIT 2

<u>Capital Grants and Contributions</u>	<u>Net (Expense) Revenue and Changes in Net Position</u>		
	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Total</u>
\$ -	\$ (155,086)	\$ -	\$ (155,086)
2,112	(387,920)	-	(387,920)
240	(340,476)	-	(340,476)
-	(150,511)	-	(150,511)
-	(80,461)	-	(80,461)
-	(10,492)	-	(10,492)
<u>\$ 2,352</u>	<u>\$ (1,124,946)</u>	<u>\$ -</u>	<u>\$ (1,124,946)</u>
\$ -	\$ -	\$ 492,842	\$ 492,842
-	-	121,449	121,449
-	-	(71,158)	(71,158)
-	-	(70,109)	(70,109)
<u>\$ -</u>	<u>\$ -</u>	<u>\$ 473,024</u>	<u>\$ 473,024</u>
<u>\$ 2,352</u>	<u>\$ (1,124,946)</u>	<u>\$ 473,024</u>	<u>\$ (651,922)</u>
	\$ 359,273	\$ -	\$ 359,273
	304,970	-	304,970
	-	43,710	43,710
	-	20,452	20,452
	<u>370,000</u>	<u>(370,000)</u>	<u>-</u>
	<u>\$ 1,034,243</u>	<u>\$ (305,838)</u>	<u>\$ 728,405</u>
	\$ (90,703)	\$ 167,186	\$ 76,483
	<u>3,007,616</u>	<u>8,155,300</u>	<u>11,162,916</u>
	<u>\$ 2,916,913</u>	<u>\$ 8,322,486</u>	<u>\$ 11,239,399</u>

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

EXHIBIT 3

**BALANCE SHEET
GOVERNMENTAL FUNDS
DECEMBER 31, 2016**

		<u>General Fund</u>
<u>Assets</u>		
Cash and pooled investments	\$	756,207
Investments		553,693
Taxes receivable		
Current		8,693
Prior		15,325
Special assessments receivable - prior		240
Accounts receivable		3,381
Loans receivable		30,586
		<hr/>
Total Assets	\$	<u>1,368,125</u>
<u>Liabilities, Deferred Inflows of Resources, and Fund Balances</u>		
Liabilities		
Accounts payable	\$	49,300
Salaries payable		18,315
Due to other governments		163
		<hr/>
Total Liabilities	\$	<u>67,778</u>
Deferred Inflows of Resources		
Taxes	\$	15,325
Special assessments		240
		<hr/>
Total Deferred Inflows of Resources	\$	<u>15,565</u>
Fund Balances		
Nonspendable for loans receivable	\$	30,586
Restricted for		
Small Cities Development Program		62,558
USDA loan pool		94,400
Assigned to		
Capital projects		125,273
Cemetery		25,439
Community development		26,464
Culture and recreation		213,174
Economic development		157,141
Public safety		180,254
Unassigned		369,493
		<hr/>
Total Fund Balances	\$	<u>1,284,782</u>
		<hr/>
Total Liabilities, Deferred Inflows of Resources, and Fund Balances	\$	<u>1,368,125</u>

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

EXHIBIT 4

**RECONCILIATION OF GOVERNMENTAL FUNDS BALANCE SHEET TO
THE STATEMENT OF NET POSITION--GOVERNMENTAL ACTIVITIES
DECEMBER 31, 2016**

Fund balances - total governmental funds (Exhibit 3)	\$	1,284,782
<p>Amounts reported for governmental activities in the Statement of Net Position are different because:</p>		
Capital assets, net of accumulated depreciation, used in governmental activities are not financial resources and, therefore, are not reported in the governmental funds.		2,443,477
Other long-term assets are not available to pay for current period expenditures and, therefore, are deferred in the governmental funds.		15,565
<p>Long-term liabilities are not due and payable in the current period and, therefore, are not reported in the governmental funds.</p>		
Accrued interest payable	\$ (2,516)	
Compensated absences payable	(20,682)	
Capital lease payable	(38,237)	
General obligation bonds payable	(355,000)	
Unamortized premium on bonds	(7,473)	(423,908)
<p>Net pension liability and related outflows/inflows of resources represent the allocation of the pension obligations of the statewide plans to the City. Such balances are not reported in the governmental funds:</p>		
Deferred outflows of resources related to pensions	\$ 583,603	
Deferred inflows of resources related to pensions	(90,276)	
Net pension liability	(896,330)	(403,003)
Net position of governmental activities (Exhibit 1)	\$	2,916,913

**CITY OF BAUDETTE
BAUDETTE MINNESOTA**

EXHIBIT 5

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2016**

	General Fund
Revenues	
Property taxes	\$ 354,023
Licenses and permits	4,663
Intergovernmental	352,988
Charges for services	51,920
Fines and forfeitures	5,182
Gifts and contributions	16,450
Miscellaneous	70,532
Total Revenues	\$ 855,758
Expenditures	
Current	
General government	\$ 191,813
Public safety	354,477
Highways and streets	249,734
Culture and recreation	160,598
Economic development	88,354
Debt service	
Principal retirement	15,961
Interest	7,976
Capital outlay	
Public safety	38,456
Highways and streets	354,983
Culture and recreation	88,994
Total Expenditures	\$ 1,551,346
Excess of Revenues Over (Under) Expenditures	\$ (695,588)
Other Financing Sources	
Transfers in	\$ 370,000
Proceeds from issuance of debt	400,929
Total Other Financing Sources	\$ 770,929
Net Change in Fund Balance	\$ 75,341
Fund Balance - January 1	1,209,441
Fund Balance - December 31	\$ 1,284,782

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

EXHIBIT 6

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND
CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE
STATEMENT OF ACTIVITIES--GOVERNMENTAL ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2016**

Net change in fund balances - total governmental funds (Exhibit 5) **\$ 75,341**

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

Governmental funds report capital outlay as expenditures. However, in
the Statement of Activities, the cost of those assets is allocated over
their estimated useful lives and reported as depreciation expense.

Expenditures for general capital assets	\$ 482,433	
Current year depreciation	(136,905)	345,528

Revenues in the Statement of Activities that do not provide current
financial resources are not reported as revenues in the governmental funds.

Change in:		
Taxes receivable	\$ (5,250)	
Special assessments receivable	(240)	(5,490)

The issuance of long-term debt provides current financial resources to
governmental funds, while the repayment of the principal consumes the
current financial resources of governmental funds. Neither transaction has
any effect on net position.

Proceeds from issuance of debt	\$ (400,929)	
Principal repayment of capital leases	15,961	(384,968)

Some expenses reported in the Statement of Activities do not require
the use of current financial resources and, therefore, are not reported as
expenditures in the governmental funds

Change in:		
Accrued interest payable	\$ 2,516	
Unamortized premium on bonds	(7,473)	
Compensated absences payable	20,682	15,725

Net pension liability does not represent the impending use of current resources.
Therefore, the change in the liability and the related deferrals are not
reported in the governmental funds.

		(136,839)
Change in net position of governmental activities (Exhibit 2)		\$ (90,703)

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

EXHIBIT 7

**STATEMENT OF NET POSITION
PROPRIETARY FUNDS
DECEMBER 31, 2016**

	Electric Enterprise	Liquor Enterprise	Sewer Enterprise	Water Enterprise	Total
<u>Assets</u>					
Current Assets					
Cash and pooled investments	\$ 1,049,936	\$ 58,680	\$ 22,499	\$ 551,135	\$ 1,682,250
Investments	1,489,237	-	-	-	1,489,237
Accounts receivable	256,924	7,950	27,045	50,708	342,627
Inventory	91,206	338,719	6,606	38,957	475,488
Prepaid items	-	6,247	-	-	6,247
Total Current Assets	\$ 2,887,303	\$ 411,596	\$ 56,150	\$ 640,800	\$ 3,995,849
Noncurrent Assets					
Capital assets					
Non-depreciable	\$ -	\$ -	\$ 219,295	\$ 947,029	\$ 1,166,324
Depreciable - net of accumulated depreciation	285,186	95,051	2,428,069	4,340,581	7,148,887
Total Noncurrent Assets	\$ 285,186	\$ 95,051	\$ 2,647,364	\$ 5,287,610	\$ 8,315,211
Total Assets	\$ 3,172,489	\$ 506,647	\$ 2,703,514	\$ 5,928,410	\$ 12,311,060
<u>Deferred Outflows of Resources</u>					
Related to pensions	\$ 79,767	\$ 107,514	\$ 24,277	\$ 27,746	\$ 239,304
<u>Liabilities</u>					
Current Liabilities					
Accounts payable	\$ 2,978	\$ 27,367	\$ 294	\$ 16,072	\$ 46,711
Salaries payable	4,578	9,180	1,567	2,279	17,604
Compensated absences payable	5,321	7,067	1,739	3,703	17,830
Due to other governments	-	13,082	-	10,826	23,908
Accrued interest payable	-	-	10,454	2,516	12,970
Customer deposits	11,425	-	-	-	11,425
Revenue notes payable	-	-	20,000	20,000	40,000
MPFA loans payable	-	-	-	50,000	50,000
Total Current Liabilities	\$ 24,302	\$ 56,696	\$ 34,054	\$ 105,396	\$ 220,448
Noncurrent Liabilities					
Compensated absences payable	\$ 3,904	\$ 2,940	\$ -	\$ -	\$ 6,844
Net pension liability	188,616	254,221	57,406	65,605	565,848
Bonds payable	-	-	1,005,000	1,440,000	2,445,000
Unamortized premium on bonds	-	-	20,695	29,317	50,012
Revenue notes payable	-	-	162,500	162,500	325,000
MPFA loans payable	-	-	-	569,000	569,000
Total Noncurrent Liabilities	\$ 192,520	\$ 257,161	\$ 1,245,601	\$ 2,266,422	\$ 3,961,704
Total Liabilities	\$ 216,822	\$ 313,857	\$ 1,279,655	\$ 2,371,818	\$ 4,182,152
<u>Deferred Inflows of Resources</u>					
Related to pensions	\$ 15,242	\$ 20,544	\$ 4,639	\$ 5,301	\$ 45,726
<u>Net Position</u>					
Net investment in capital assets	\$ 285,186	\$ 95,051	\$ 1,459,864	\$ 3,046,110	\$ 4,886,211
Unrestricted amounts	2,735,006	184,709	(16,367)	532,927	3,436,275
Total Net Position	\$ 3,020,192	\$ 279,760	\$ 1,443,497	\$ 3,579,037	\$ 8,322,486

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

EXHIBIT 8

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2016**

	<u>Electric Enterprise</u>	<u>Liquor Enterprise</u>	<u>Sewer Enterprise</u>	<u>Water Enterprise</u>	<u>Total</u>
Sales and Cost of Goods Sold					
Sales	\$ 2,422,282	\$ 1,548,558	\$ -	\$ -	\$ 3,970,840
Cost of goods sold	(1,651,112)	(995,027)	-	-	(2,646,139)
Gross Profit	\$ 771,170	\$ 553,531	\$ -	\$ -	\$ 1,324,701
Operating Revenues					
Charges for services	-	-	319,791	376,872	696,663
Total Gross Profit and Operating Revenues	\$ 771,170	\$ 553,531	\$ 319,791	\$ 376,872	\$ 2,021,364
Operating Expenses					
Personnel services	\$ 146,431	\$ 304,334	\$ 93,284	\$ 106,631	\$ 650,680
Advertising	-	3,189	-	-	3,189
Insurance	7,368	5,513	5,126	4,586	22,593
License and dues	9,095	-	-	8,058	17,153
Other services and charges	28,028	3,516	7,762	13,447	52,753
Supplies	23,379	19,358	10,481	31,824	85,042
Utilities	3,949	14,131	6,028	22,575	46,683
Repairs and maintenance	24,168	13,201	78,530	24,130	140,029
Miscellaneous	585	54,670	8,008	186	63,449
Depreciation	35,325	14,170	114,824	175,052	339,371
Total Operating Expenses	\$ 278,328	\$ 432,082	\$ 324,043	\$ 386,489	\$ 1,420,942
Operating Income (Loss)	\$ 492,842	\$ 121,449	\$ (4,252)	\$ (9,617)	\$ 600,422
Nonoperating Revenues (Expenses)					
Investment earnings	\$ 43,710	\$ -	\$ -	\$ -	\$ 43,710
Miscellaneous	3,913	13,718	-	2,821	20,452
Interest expense	-	-	(66,906)	(60,492)	(127,398)
Total Nonoperating Revenues (Expenses)	\$ 47,623	\$ 13,718	\$ (66,906)	\$ (57,671)	\$ (63,236)
Income (Loss) Before Transfers	\$ 540,465	\$ 135,167	\$ (71,158)	\$ (67,288)	\$ 537,186
Transfers out	(220,000)	(150,000)	-	-	(370,000)
Change in Net Position	\$ 320,465	\$ (14,833)	\$ (71,158)	\$ (67,288)	\$ 167,186
Net Position - January 1	2,699,727	294,593	1,514,655	3,646,325	8,155,300
Net Position - December 31	\$ 3,020,192	\$ 279,760	\$ 1,443,497	\$ 3,579,037	\$ 8,322,486

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

EXHIBIT 9

**STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2016
Increase (Decrease) in Cash and Cash Equivalents**

	Electric Enterprise	Liquor Enterprise	Sewer Enterprise	Water Enterprise	Total
Cash Flows from Operating Activities					
Receipts from customers	\$ 2,438,488	\$ 1,542,531	\$ 320,426	\$ 504,914	\$ 4,806,359
Payments to employees	(123,627)	(255,559)	(84,686)	(94,602)	(558,474)
Payments to suppliers	(1,713,320)	(1,134,972)	(122,428)	(291,825)	(3,262,545)
Net cash provided by (used in) operating activities	\$ 601,541	\$ 152,000	\$ 113,312	\$ 118,487	\$ 985,340
Cash Flows from Noncapital and Related Financing Activities					
Transfers to other funds	\$ (220,000)	\$ (150,000)	\$ -	\$ -	\$ (370,000)
Miscellaneous	3,913	13,668	-	2,821	20,402
Net cash provided by (used in) noncapital and related financing activities	\$ (216,087)	\$ (136,332)	\$ -	\$ 2,821	\$ (349,598)
Cash Flows from Capital and Related Financing Activities					
Proceeds from issuance of debt	\$ -	\$ -	\$ 1,005,000	\$ 1,440,000	\$ 2,445,000
Purchase of capital assets	(7,500)	-	(210,275)	(906,342)	(1,124,117)
Principal paid on bonded debt	-	-	(808,500)	(66,500)	(875,000)
Interest paid on bonded debt	-	-	(77,038)	(37,331)	(114,369)
Net cash provided by (used in) capital and related financing activities	\$ (7,500)	\$ -	\$ (90,813)	\$ 429,827	\$ 331,514
Cash Flows from Investing Activities					
Investment earnings received	\$ 43,710	\$ -	\$ -	\$ -	\$ 43,710
Net Increase (Decrease) in Cash and Cash Equivalents	\$ 421,664	\$ 15,668	\$ 22,499	\$ 551,135	\$ 1,010,966
Cash and Cash Equivalents at January 1	2,117,509	43,012	-	-	2,160,521
Cash and Cash Equivalents at December 31	\$ 2,539,173	\$ 58,680	\$ 22,499	\$ 551,135	\$ 3,171,487
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities					
Operating income (loss)	\$ 492,842	\$ 121,499	\$ (4,252)	\$ (9,617)	\$ 600,472
Adjustments to reconcile net operating income (loss) to net cash provided by (used in) operating activities					
Depreciation expense	\$ 35,325	\$ 14,170	\$ 114,824	\$ 175,052	\$ 339,371
Decrease (increase) in assets					
Accounts receivable	24,932	(5,040)	858	(12,341)	8,409
Inventory	45,392	(27,322)	(6,606)	(38,957)	(27,493)
Prepaid items	-	(554)	-	-	(554)
Increase (decrease) in liabilities					
Accounts payable	(11,250)	12,919	113	(17,795)	(16,013)
Salaries payable	(3,806)	2,665	1,567	2,279	2,705
Due to other governments	(10,123)	1,212	-	10,371	1,460
Compensated absences payable	9,225	10,007	1,739	3,703	24,674
Customer deposits	2,351	-	-	-	2,351
Net pension liability	16,653	22,444	5,069	5,792	49,958
Total adjustments	\$ 108,699	\$ 30,501	\$ 117,564	\$ 128,104	\$ 384,868
Net cash provided by (used in) operating activities	\$ 601,541	\$ 152,000	\$ 113,312	\$ 118,487	\$ 985,340

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

NOTES TO THE FINANCIAL STATEMENTS
AS OF AND FOR THE YEAR ENDED DECEMBER 31, 2016

I. Summary of Significant Accounting Policies

The City's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (statements and interpretations). The more significant accounting policies established in GAAP and used by the City are discussed below

A. Financial Reporting Entity

The City of Baudette has the powers, duties, and privileges granted by state law, codified in Minnesota Statutes, Chapter 412. The City operates under a Mayor-Council form of government and provides services such as general government, public safety, highways and streets, culture and recreation, conservation of natural resources, economic development, a municipal liquor store, and the electric, sewer and water utilities, as authorized by its charter.

The City participates in a joint venture as described in Note IV-D.

B. Basic Financial Statements

1. Government-Wide Statements

The government-wide financial statements (i.e., the statement of net position and the statement of activities) include the financial activities of the overall City government. Eliminations have been made to minimize the double-counting of internal activities. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges to external parties for support.

In the government-wide statement of net position, both the governmental and business-type activities columns: (a) are presented on a consolidated basis by column; and (b) are reported on a full accrual, economic resource basis, which recognizes all long-term assets and receivables as well as long-term debt and obligations. The City's net position is reported in three parts: (1) net investment in capital assets; (2) restricted net position; and (3) unrestricted net position. The City first utilizes restricted resources to finance qualifying activities.

The statement of activities demonstrates the degree to which the direct expenses of each function of the City's governmental activities and different business-type activities are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or activity. Program revenues include: (1) fees, charges, and fines paid by the recipients of goods, services, or privileges provided by a given function or activity; and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or activity. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues and transfers.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

I. Summary of Significant Accounting Policies

B. Basic Financial Statements (Continued)

2. Fund Financial Statements

The fund financial statements provide information about the City's funds. Separate statements for each fund category—governmental and proprietary—are presented. The emphasis of governmental and proprietary fund financial statements is on major individual governmental and enterprise funds, with each displayed as separate columns in the fund financial statements.

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

The City reports the following major governmental fund:

The General Fund is the City's primary operating fund. It accounts for and reports all financial resources of the general government not accounted for in another fund.

The City reports the following major enterprise funds:

The Electric Enterprise Fund is used to account for the operations of the City's electric department. Financing is provided charges to residents for services.

The Liquor Enterprise Fund is used to account for operations of the municipal liquor dispensary. Financing is provided through the liquor store's sale of on and off-sale liquor.

The Sewer Enterprise Fund is used to account for operations of the sewer utility. Financing is provided by charges to residents for services.

The Water Enterprise Fund is used to account for operations of the water utility. Financing is provided by charges to residents for services.

C. Measurement Focus and Basis of Accounting

The government-wide and proprietary fund financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

I. Summary of Significant Accounting Policies

C. Measurement Focus and Basis of Accounting (Continued)

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. The City considers all revenues to be available if they are collected within 60 days after the end of the current period. Property and other taxes, licenses, and interest are all considered to be susceptible to accrual. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, compensated absences, and claims and judgments, which are recognized as expenditures to the extent that they have matured. Proceeds of general long-term debt are reported as other financing sources.

During the year ended December 31, 2016, the Association adopted GASB Statement No. 72, *Fair Value Measurement and Application*. This statement addresses accounting and financial reporting issues related to fair value measurements. It provides guidance for determining a fair value measurement for financial reporting purposes and for applying fair value to certain investments and disclosures related to all fair value measurement. No restatement is required as a result of implementing this statement.

As a general rule, the effect of internal activity has been eliminated from the government-wide financial statements.

D. Assets, Liabilities, and Net Position or Equity

1. Cash and Cash Equivalents

The City has defined cash and cash equivalents to include cash on hand, demand deposits, and time deposits. Additionally, each fund's equity in the City's deposits is treated as a cash equivalent because the funds can deposit or effectively withdraw cash at any time without prior notice or penalty. Cash and cash equivalents are valued at fair value.

2. Deposits and Investments

The cash balances of the funds are invested by the City Clerk for the purpose of increasing earnings through investment activities. Pooled and fund investments are reported at their fair value at December 31, 2016, based on market prices. Total investment earnings for 2016 were \$43,710.

3. Receivables and Payables

Property taxes are levied as of January 1 on property values assessed as of the same date. The tax levy notice is mailed by Lake of the Woods County in March with the first half payment due on May 15 and the second half due on October 15.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

I. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Position or Equity

3. Receivables and Payables (Continued)

Taxes receivable consist of uncollected taxes payable in the years 2008 through 2016. Taxes receivable are offset by deferred inflows of resources for the amount not collected within 60 days of December 31 to indicate they are not available to finance current expenditures. No provision has been made for an estimated uncollectible amount.

Accounts receivable consist primarily of charges for services for electric, sewer and water utilities.

Loans receivable consist of rehabilitation and business loans. Loans receivable are classified as non-spendable fund balance in the General Fund for the balance outstanding as of year-end.

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either “due to/from other funds” (i.e., the current portion of interfund loans) or “advances from/to other funds” (i.e., the non-current portion of interfund loans).

All other outstanding balances between funds are reported as “due to/from other funds.” Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as “internal balances.”

All receivables are shown net of an allowance for uncollectible amounts, if applicable.

4. Inventories and Prepaid Items

All inventories are valued at cost using the weighted average method. Inventories in governmental funds are recorded as expenditures when purchased rather than when consumed. Inventories in the proprietary funds and at the government-wide level are recorded as expenses when consumed.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

5. Capital Assets

Capital assets, which include land, construction in progress, infrastructure, buildings, and machinery and equipment, are reported in the applicable governmental or business-type activities column in the government-wide financial statements. Capital assets are defined by the government as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of two years, except land and construction in progress which is capitalized regardless of cost.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

I. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Position or Equity

5. Capital Assets (Continued)

Capital assets are recorded at historical cost or estimated historical cost when purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extended the life of the asset are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets of business-type activities is included as part of the capitalized value of the assets constructed. During the current period, the City did not have any capitalized interest.

The City of Baudette has elected to report infrastructure acquired prior to periods ending after June 30, 1980.

Infrastructure, buildings, and machinery and equipment are depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Infrastructure	3-40
Buildings	10-40
Machinery and equipment	3-20

6. Deferred Outflows and Inflows of Resources

In addition to assets, the Statement of Net Position reports a separate section for deferred outflows of resources. This element represents a consumption of net position that applies to future periods, and therefore, will not be recognized as an outflow of resources (expense) until that time. The City reports deferred outflows of resources in the government-wide and proprietary funds Statement of Net Position in relation to the activity of the pension funds in which City employees participate.

In addition to liabilities, the Statement of Net Position and Balance Sheet report a separate section for deferred inflows of resources. This element represents an acquisition of net position or fund balance that applies to future periods, and therefore, will not be recognized as an inflow of resources (revenue) until that time. The City reports delinquent property tax receivables as deferred inflows of resources in the governmental funds, in accordance with the modified accrual basis of accounting.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

I. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Position or Equity

6. Deferred Outflows and Inflows of Resources (Continued)

In addition, the City reports deferred inflows of resources in the government-wide and proprietary funds Statement of Net Position in relation to the activity of the pension funds in which City employees participate. Accordingly, such amounts are deferred and recognized as inflows of resources in the period that they become available.

7. Employee Benefits

The liability for compensated absences reported in financial statements consist of unpaid, accumulated annual vacation. The liability has been calculated using the vesting method, in which leave amounts for both employees who currently are eligible to receive termination payments and other employees who are expected to become eligible in the future to receive such payments upon termination are included. There is no liability for unpaid accumulated sick leave since the City does not have a policy to pay any amounts when employees separate from service with the City. Compensated absences are accrued when incurred in the government-wide proprietary fund financial statements. A liability for these amounts is reported in the governmental funds only if they have matured, for example, as a result of employee resignations and retirements.

8. Long-Term Obligations

In the government-wide and proprietary fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental or business-type activities. In the fund financial statements, governmental fund types recognize the face amount of the debt issued is reported as other financing sources when issued.

9. Pensions

For purposes of measuring the net pension liability, deferred outflows/inflows of resources, and pension expense, information about the fiduciary net position of the Public Employees Retirement Association (PERA) and additions to/deductions from PERA's fiduciary net position have been determined on the same basis as they are reported by PERA except that PERA's fiscal year end is June 30. For this purpose, plan contributions are recognized as of employer payroll paid dates and benefit payments and refunds are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

10. Net Position and Fund Balance

Certain funds of the City are classified as restricted net position on the statement of net position because the restriction is either imposed by law through constitutional provisions or enabling legislation or imposed externally by creditors, grantors, contributors, or laws or regulations of other governments. Therefore, their use is limited by applicable laws and regulations.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

I. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Position or Equity

10. Net Position and Fund Balance (Continued)

In the fund financial statements, the City classifies governmental fund balances as follows:

Non-spendable – includes fund balance amounts that cannot be spent because it is either not in spendable form or legally or contractually required to be maintained intact.

Restricted – includes fund balance amounts that are constrained for specific purposes which are either externally imposed by creditors (such as debt covenants), grantors, contributors, or laws or regulations of other governments or imposed by law through constitutional provisions or enabling legislation.

Committed – includes fund balance amounts that are constrained for specific purposes imposed by resolution of the City Council and do not lapse at year-end. To remove the constraint on specified use of committed resources the City Council shall pass a resolution. The City does not have any committed fund balances at December 31, 2016.

Assigned – includes fund balance amounts that are intended to be used for specific purposes that are neither restricted nor committed. The City Council has delegated the authority to assign and remove assignments of fund balance amounts for specified purposes to the City Clerk/Treasurer.

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.

Stabilization arrangements are defined as formally setting aside amounts for use in emergency situations or when revenue shortages or budgetary imbalances arise. The City Council will set aside amounts by resolution as deemed necessary that can only be expended when the need for stabilization arises, such as resources as a reserve for delinquent taxes; a reserve against economic uncertainties leading to overestimates in revenue forecasts; resources to provide for unpredictable changes in state law; and monies for unforeseen expenditures such as natural disasters, for which no other government resources are made available or there is a delay in receiving those funds from other government entities. The need for stabilization will only be utilized for situations that are not expected to occur routinely. As of December 31, 2016 the City had no amount set aside for stabilization.

When both restricted and unrestricted resources are available for use, it is the City's policy to use restricted resources first, then unrestricted resources as they are needed. When committed, assigned or unassigned resources are available for use, it is the City's policy to use resources in the following order: 1) committed, 2) assigned, and 3) unassigned.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

I. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Position or Equity (Continued)

11. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, and deferred inflows and disclosure of contingent amounts at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

II. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

Reconciliations of the City's total deposits and investments to the basic financial statements, as of December 31, 2016, are as follows:

Government-wide Statement of Net Position	
Governmental Activities	
Cash and pooled investments	\$ 756,207
Investments	553,693
Business-type Activities	
Cash and pooled investments	1,682,250
Investments	<u>1,489,237</u>
Total Cash and Investments	<u><u>\$ 4,481,387</u></u>
Cash on hand	\$ 5,833
Certificates of Deposit	125,273
Checking	2,432,625
Investment account	1,861,169
Savings	<u>56,487</u>
Total deposits and cash on hand	<u><u>\$ 4,481,387</u></u>

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

II. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments (Continued)

Deposits

Minnesota Statutes, §§ 118A.02 and 118A.04 authorize the City to deposit its cash and to invest in certificates of deposit in financial institutions designated by the Board. Minnesota Statute, § 118A.03 requires that all City deposits be covered by insurance, surety bond, or collateral. The market value of collateral pledged shall be at least ten percent more than the amount on deposit plus accrued interest at the close of the financial institution's banking day, not covered by insurance or bonds.

Authorized collateral includes treasury bills, notes, and bonds; issues of U.S. government agencies; general obligations rated "A" or better, revenue obligations rated "AA" or better; irrevocable standard letters of credit issued by the Federal Home Loan Bank; and certificates of deposit. Minnesota statutes require that securities pledged as collateral be held in safekeeping in a restricted account at the Federal Reserve Bank or in an account at a trust department of a commercial bank or other financial institution not owned or controlled by the financial institution furnishing the collateral.

Custodial Credit Risk

Custodial credit risk for deposits is the risk that in the event of a financial institution failure, the City's deposits may not be returned to it. The City does not have a deposit policy for custodial credit risk. However, the City complies with Minnesota statutes in establishing authorized collateral for deposits. As of December 31, 2016, the City's deposits were not exposed to custodial credit risk.

Investments

Minnesota Statutes, §§ 118A.04 and 118A.05 generally authorize the following types of investments available to the City:

- (1) securities which are direct obligations or are guaranteed or insured issues of the United States, its agencies, its instrumentalities, or organizations created by an act of Congress, except mortgage-backed securities defined as high risk by Minnesota Statute, § 118A.04, subdivision 6;
- (2) mutual funds through shares of registered investment companies provided the mutual fund receives certain ratings depending on its investments;
- (3) general obligations of the State of Minnesota and its municipalities, and certain state agency and local obligations of Minnesota and other states provided such obligations have certain specified bond ratings by a national bond rating service;
- (4) bankers' acceptances of United States banks;

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

II. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

Investments (Continued)

- (5) commercial paper issued by United States corporations or their Canadian subsidiaries that is rated in the highest quality category by two nationally recognized rating agencies and matures in 270 days or less; and
- (6) with certain restrictions, in repurchase agreements, securities lending agreements, joint powers investment trusts, and guaranteed investment contracts.

Interest Rate Risk

Interest rate risk is the risk that changes in the market interest rates will adversely affect the fair value of an investment. The City does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

At December 31, 2016, the City had the following investments and maturities:

	<u>Fair Value</u>	<u>Less Than 1 Year</u>	<u>1-5 Years</u>	<u>5+ Years</u>
Federal Home Loan Mortgage Corporation	\$ 15,802	\$ -	\$ 15,802	\$ -
Federal National Mortgage Association	25,447	-	25,447	-
US Treasury	663,448	150,123	438,061	75,264
Municipal Bonds	1,082,312	75,310	415,516	591,486
Money Market	<u>74,161</u>	<u>74,161</u>	<u>-</u>	<u>-</u>
Total Investments	<u>\$ 1,861,170</u>	<u>\$ 299,594</u>	<u>\$ 894,826</u>	<u>\$ 666,750</u>
	100%	16%	48%	36%

Credit Risk

Generally, a credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. It is the City's policy to invest only in securities that meet the ratings requirements set by state statute.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

II. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

Investments

Credit Risk (Continued)

The City's exposure to credit risk as of December 31, 2016, is as follows:

	S & P Rating	Fair Value
Federal Home Loan Mortgage Corporation	AA+	\$ 15,802
Federal Home Loan Bank	AA+	25,447
US Treasury	N/R	663,448
Municipal Bonds	AAA	96,744
Municipal Bonds	AA+	203,177
Municipal Bonds	AA	279,137
Municipal Bonds	AA-	195,128
Municipal Bonds	N/R	308,126
Money Market	N/A	74,161
		\$ 1,861,170

N/A – not applicable

N/R – not rated

Custodial Credit Risk

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The City does not have a policy on custodial credit risk. Some brokers have excess SIPC coverage which may mitigate all or part of custodial credit risk. At December 31, 2016, the following investments may be subject to custodial credit risk:

Municipal GO Bonds	\$ 697,722
US Treasury Notes	663,448
Total Custodial Credit Risk	1,361,170

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

II. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

Investments (Continued)

Concentration of Credit Risk

The concentration of credit risk is the risk of loss that may be caused by the City's investment in a single issuer, excluding U.S. guaranteed investments, external investment pools, and mutual funds.

Investments in any one issuer that represent five percent or more of the City's investments are:

Issuer	Reported Amount	
US Treasury	\$ 663,448	38%
Municipal Bonds	1,082,312	62%

2. Receivables

Receivables as of December 31, 2016, for the City's governmental and business-type activities, including any applicable allowances for uncollectible accounts, are as follows:

	Total Receivables	Amounts Not Scheduled for Collection During the Subsequent Year
Governmental Activities		
Taxes	\$ 24,018	\$ -
Accounts	3,381	-
Loans	30,586	23,531
Total Governmental Activities	\$ 57,985	\$ 23,531
Business-Type Activities		
Accounts	\$ 342,627	\$ -

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

III. Detailed Notes on All Funds

A. Assets (Continued)

3. Capital Assets

Capital asset activity for the governmental and business-type activities for the year ended December 31, 2016, was as follows:

Construction in progress	-	402,093	-	402,093
	<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>
Total capital assets not depreciated	222,328	402,093	-	624,421
Capital assets being depreciated				
Infrastructure	\$ 1,964,716	\$ -	\$ -	\$ 1,964,716
Buildings	1,224,364	-	-	1,224,364
Machinery and equipment	<u>1,504,640</u>	<u>80,340</u>	<u>-</u>	<u>1,584,980</u>
Total capital assets being depreciated	<u>\$ 4,693,720</u>	<u>\$ 80,340</u>	<u>\$ -</u>	<u>\$ 4,774,060</u>
Less: accumulated depreciation for				
Infrastructure	\$ 856,906	\$ 72,056	\$ -	\$ 928,962
Buildings	684,925	28,309	-	713,234
Machinery and equipment	<u>1,276,268</u>	<u>36,540</u>	<u>-</u>	<u>1,312,808</u>
Total accumulated depreciation	<u>\$ 2,818,099</u>	<u>\$ 136,905</u>	<u>\$ -</u>	<u>\$ 2,955,004</u>
Total capital assets, depreciated, net	<u>\$ 1,875,621</u>	<u>\$ (56,565)</u>	<u>\$ -</u>	<u>\$ 1,819,056</u>
Governmental Activities				
Capital Assets, Net	<u>\$ 2,097,949</u>	<u>\$ 345,528</u>	<u>\$ -</u>	<u>\$ 2,443,477</u>

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

II. Detailed Notes on All Funds

A. Assets

3. Capital Assets (Continued)

Business-Type Activities

	Beginning Balance	Increases	Decreases	Ending Balance
Capital assets, not being depreciated				
Land	\$ 81,418	\$ -	\$ -	\$ 81,418
Construction in progress	42,330	1,042,576	-	1,084,906
Total capital assets not depreciated	<u>\$ 123,748</u>	<u>\$ 1,042,576</u>	<u>\$ -</u>	<u>\$ 1,166,324</u>
Capital assets being depreciated				
Buildings	\$ 147,116	\$ -	\$ -	\$ 147,116
Infrastructure	11,940,176	-	-	11,940,176
Machinery and equipment	873,727	81,541	-	955,268
Total capital assets being depreciated	<u>\$ 12,961,019</u>	<u>\$ 81,541</u>	<u>\$ -</u>	<u>\$ 12,895,444</u>
Less: accumulated depreciation for				
Buildings	\$ 45,513	\$ 6,552	\$ -	\$ 52,065
Infrastructure	4,726,176	318,337	-	5,044,513
Machinery and equipment	782,613	14,482	-	797,095
Total accumulated depreciation	<u>\$ 5,554,302</u>	<u>\$ 339,371</u>	<u>\$ -</u>	<u>\$ 5,893,673</u>
Total capital assets, depreciated, net	<u>\$ 7,406,717</u>	<u>\$ (257,830)</u>	<u>\$ -</u>	<u>\$ 7,001,771</u>
Business-Type Activities				
Capital Assets, Net	<u>\$ 7,530,465</u>	<u>\$ 784,746</u>	<u>\$ -</u>	<u>\$ 8,315,211</u>

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

II. Detailed Notes on All Funds

A. Assets

3. Capital Assets (Continued)

Depreciation Expense

Depreciation expense was charged to functions of the City as follows:

Governmental Activities		
General government	\$	14,277
Public safety		21,666
Highways and streets		89,206
Culture and recreation		11,756
		11,756
Total Depreciation Expense - Governmental Activities	\$	136,905
Business-Type Activities		
Liquor	\$	14,170
Electric		35,325
Sewer		114,824
Water		175,052
		175,052
Total Depreciation Expense - Business-Type Activities	\$	339,371

B. Interfund Receivables, Payables, and Transfers

Interfund Transfers

Interfund transfers for the year ended December 31, 2016, consisted of the following operating transfers:

Transfer to General Fund from Electric Enterprise Fund	\$	220,000	For operations
Transfer to General Fund from Liquor Enterprise Fund		150,000	For operations
Total Interfund Transfers	\$	370,000	

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

II. Detailed Notes on All Funds (Continued)

C. Liabilities

Compensated Absences

Under the City's personnel policies, employees are granted vacation leave in varying amounts based on their length of service. Vacation leave accrual varies from 5 to 25 days per year and may be accumulated to a maximum of 280 hours. Sick leave accrual is 13 days per year and may be accumulated to a maximum of 880 hours under the City's employment policy.

Unvested sick leave, approximately \$121,967 at December 31, 2016, is available to employees in the event of illness-related absences and is not paid to them at termination. Compensated absences are generally liquidated by the General Fund and the Electric, Liquor, Sewer, and Water Enterprise Funds.

Long-Term Debt

Governmental Activities

City of Baudette Kansas State Bank Capital Equipment Notes represent debt incurred for a 2013 Ford interceptor squad car. These notes have an original issue amount of \$31,500. They carry a net interest rate of 4.50 percent and are due in annual payments from the General Fund of \$8,253 through June 1, 2017. The balance due on this note at December 31, 2016, is \$7,995. An additional note to represent debt incurred for an additional Ford interceptor squad car was issued November 14, 2016. This note has an original issue of \$38,456 with a net interest rate of 3.40 percent and is due in annual payments from the General Fund of \$8,214. The balance due on this note at December 31, 2016, \$30,242.

City of Baudette General Obligation Bonds of 2016 represent debt incurred for a street, sewer and water project. The street project portion of these bonds have an original issue amount of \$355,000 carry a net interest rate of 2.343 percent and are due in annual payments from the General Fund of \$10,000 to \$25,000 through February 1, 2037. The balance due on these bonds at December 31, 2016 is \$355,000.

Business-Type Activities

City of Baudette General Obligation Bonds of 2002 represent debt incurred for sewer system improvements. These bonds have an original issue amount of \$925,000. They carry a net interest rate of 4.75 percent and are due in annual principal payments from the Sewer Enterprise Fund of between \$15,000 and \$51,000 through January 1, 2042. These bonds were refunded in 2016, and the balance due at December 31, 2016 is \$0.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

II. Detailed Notes on All Funds

C. Liabilities

Business-Type Activities (Continued)

City of Baudette General Obligation Bonds of 2016 represent debt incurred for a street, sewer and water project. The sewer and water project portion of these bonds have an original issue amount of \$640,000, carry a net interest rate of 2.343 percent. Also included was \$800,000 to refund the General Obligation Sewer Bonds of 2002 on September 15, 2016. These bonds are due in annual payments from the Sewer and Water Enterprise Funds of \$5,000 to \$65,000 through February 1, 2037. As a result of the refunding, the City reduced its total debt service payments by \$225,860, and recognized an economic gain of \$222,388. The balance due on these bonds at December 31, 2016 is \$1,440,000.

City of Baudette General Obligation Revenue Note of 2008 represents debt incurred for water and sewer improvements. This note has an original issue amount of \$590,000, carries a net interest rate of 4.19 percent, and is due in annual principal payments from both the Sewer and Water Enterprise Funds of between \$40,000 and \$55,000 through February 1, 2024. The balance due on this note at December 31, 2016, is \$365,000.

City of Baudette Minnesota Public Facilities Authority (MPFA) Loan of 2004 represents debt incurred for the Baudette Bay water loop. This loan has a final issue amount of \$337,729, carries a net interest rate of 2.46 percent, and is due in annual principal payments from the Water Enterprise Fund of between \$18,000 and \$21,000 through August 20, 2024. The balance due on this loan at December 31, 2016, is \$156,000.

City of Baudette Minnesota Public Facilities Authority (MPFA) Loan of 2010 represents debt incurred for the water tower. This loan has a final issue amount of \$750,760, which carries a net interest rate of 1.925 percent and is due in annual principal payments from the Water Enterprise Fund of between \$31,000 and \$40,000 through August 20, 2029. The balance due on this loan at December 31, 2016, is \$463,000.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

II. Detailed Notes on All Funds

C. Liabilities

Long-Term Debt

Business-Type Activities (Continued)

Debt Service Requirements

Debt service requirements for business-type activities for the year ended December 31, 2016, are as follows:

Year Ending December 31	G.O. Refunding Bonds		G.O. Revenue Notes		MPFA Loans	
	Principal	Interest	Principal	Interest	Principal	Interest
2017	-	48,980	40,000	15,532	50,000	12,751
2018	105,000	54,750	40,000	13,792	50,000	11,692
2019	135,000	52,350	40,000	12,053	52,000	10,633
2020	135,000	49,650	45,000	10,170	53,000	9,531
2021	140,000	46,900	45,000	8,146	54,000	8,408
2022-2026	740,000	194,300	155,000	11,004	243,000	24,942
2027-2031	535,000	130,200	-	-	117,000	4,543
2032-2036	540,000	58,500	-	-	-	-
2037	115,000	1,725	-	-	-	-
Total	\$ 2,445,000	\$ 637,355	\$ 365,000	\$ 70,697	\$ 619,000	\$ 82,500
(Discount) Premium	50,012					
Total	\$ 2,495,012					

Governmental Activities

Debt service requirements for governmental-type activities for the year ended December 31, 2016, are as follows:

Year Ending December 31	G.O. Refunding Bonds	
	Principal	Interest
2017	\$ -	\$ 7,549
2018	10,000	8,500
2019	15,000	8,250
2020	15,000	7,950
2021	15,000	7,650
2022-2026	75,000	34,049
2027-2031	100,000	25,350
2032-2036	100,000	11,250
2037	25,000	375
Total	\$ 355,000	\$ 110,923
(Discount) Premium	7,473	
Total	\$ 362,473	

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

II. Detailed Notes on All Funds

C. Liabilities

Long-Term Debt

Debt Service Requirements

Governmental Activities (Continued)

Year Ending December 31	Kansas State Bank			
	2013 Ford Police Inceptor		2017 Ford Police Inceptor	
	Principal	Interest	Principal	Interest
2017	\$ 7,995	\$ 257	\$ 7,186	\$ 1,028
2018	-	-	7,430	784
2019	-	-	7,683	531
2020	-	-	7,944	270
Total	<u>\$ 7,995</u>	<u>\$ 257</u>	<u>\$ 30,243</u>	<u>\$ 2,613</u>

Changes in Long-Term Liabilities

Governmental Activities

Long-term liability activity for the governmental activities for the year ended December 31, 2016, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Kansas State Note 2013 Ford Inceptor	\$ 15,742	\$ -	\$ 7,747	\$ 7,995	\$ 7,995
Kansas State Note 2017 Ford Inceptor	-	38,456	8,214	30,242	7,186
G.O. Bonds of 2016	-	355,000	-	355,000	-
Bond Premium	-	7,473	-	7,473	-
Compensated Absences	-	20,682	-	20,682	12,808
Net Pension Liability	-	340,849	-	340,849	-
Governmental Activities Long-Term Liabilities	<u>\$ 15,742</u>	<u>\$ 762,460</u>	<u>\$ 15,961</u>	<u>\$ 762,241</u>	<u>\$ 27,989</u>

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

II. Detailed Notes on All Funds

C. Liabilities

Long-Term Debt

Changes in Long-Term Liabilities (Continued)

Business-Type Activities

Long-term liability activity for the business-type activities for the year ended December 31, 2016, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
G.O. Bonds of 2002	\$ 791,000	\$ -	\$ 14,000	\$ 777,000	\$ 15,000
G.O. Bonds of 2016	-	1,440,000	-	1,440,000	-
Bond Premium	-	50,012	-	50,012	-
G.O. Revenue Notes	400,000	-	95,661	304,339	35,000
MPFA Loans	668,000	-	47,000	621,000	49,000
Net Pension Liability	-	354,017	-	354,017	-
Business-Type Activities					
Long-Term Liabilities	<u>\$ 1,859,000</u>	<u>\$ 1,844,029</u>	<u>\$ 156,661</u>	<u>\$ 3,546,368</u>	<u>\$ 99,000</u>

III. Defined Benefit Pension Plans

A. Plan Description

The City of Baudette participated in the following cost-sharing multiple-employer defined benefit pension plans administered by the Public Employees Retirement Association of Minnesota (PERA). PERA's defined benefit pension plans are established and administered in accordance with *Minnesota Statutes*, Chapters 353 and 356. PERA's defined benefit pension plans are tax qualified plans under Section 401(a) of the Internal Revenue Code.

1. General Employees Retirement Plan (General Employees Plan (accounted for in the General Employees Fund))

All full-time and certain part-time employees of the City of Baudette are covered by the General Employees Plan. General Employees Plan members belong to either the Coordinated Plan or the Basic Plan. Coordinated Plan members are covered by Social Security and Basic Plan members are not. The Basic Plan was closed to new members in 1967. All new members must participate in the Coordinated Plan.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

III. Defined Benefit Pension Plans

A. Plan Description (Continued)

2. Public Employees Police and Fire Fund (Police and Fire Plan (accounted for in the Police and Fire Fund))

The Police and Fire Plan, originally established for police officers and firefighters not covered by a local relief association, now covers all police officers and firefighters hired since 1980. Effective July 1, 1999, the Police and Fire Plan also covers police officers and firefighters belonging to local relief associations that elected to merge with and transfer assets and administration to PERA.

Benefits Provided

PERA provides retirement, disability, and death benefits. Benefit provisions are established by state statute and can only be modified by the state legislature.

Benefit increases are provided to benefit recipients each January. Increases are related to the funding ratio of the plan. Members in plans that are at least 90 percent funded for two consecutive years are given 2.5 percent increases. Members in plans that have not exceeded 90 percent funded, or have fallen below 80 percent, are given one percent increases.

The benefit provisions stated in the following paragraphs of this section are current provisions and apply to active plan participants. Vested, terminated employees who are entitled to benefits but are not receiving them yet are bound by the provisions in effect at the time they last terminated their public service.

1. General Employees Plan Benefits

General Employees Plan benefits are based on a member's highest average salary for any five successive years of allowable service, age, and years of credit at termination of service. Two methods are used to compute benefits for PERA's Coordinated and Basic Plan members. The retiring member receives the higher of a step-rate benefit accrual formula (Method 1) or a level accrual formula (Method 2). Under Method 1, the annuity accrual rate for a Basic Plan member is 2.2 percent of average salary for each of the first ten years of service and 2.7 percent for each remaining year. The annuity accrual rate for a Coordinated Plan member is 1.2 percent of average salary for each of the first ten years and 1.7 percent for each remaining year. Under Method 2, the annuity accrual rate is 2.7 percent of average salary for Basic Plan members and 1.7 percent for Coordinated Plan members for each year of service. For members hired prior to July 1, 1989, a full annuity is available when age plus years of service equal 90 and normal retirement age is 65. For members hired on or after July 1, 1989, normal retirement age is the age for unreduced Social Security benefits capped at 66.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

III. Defined Benefit Pension Plans

A. Plan Description (Continued)

2. Police and Fire Plan Benefits

Benefits for Police and fire Plan members first hired after June 30,2010 but before July 1, 2014 vest a prorated basis from 50 percent after five years up to 100 percent after ten years of credited service. Benefits for Police and Fire Plan members first hired after June 30, 2014 vest on a prorated basis from 50 percent after ten years up to 100 percent after twenty years of credited service. The annuity accrual rate is 3 percent of average salary for each year of service. For Police and Fire Plan members who were first hired prior to July 1, 1989 a full annuity is available when age plus years of service equal at least 90.

B. Contributions

Minnesota Statutes Chapter 353 sets the rates for employer and employee contributions. Contribution rates can only be modified by the state legislature.

1. General Employees Fund Contributions

Basic Plan members and Coordinated Plan members were required to contribute 9.1 percent and 6.50 percent, respectively, of their annual covered salary in calendar year 2016. The City of Baudette was required to contribute 11.78 percent of pay for Basic Plan members and 7.50 percent for Coordinated Plan members in calendar year 2016. The City of Baudette's contributions to the General Employees Fund for the year ended December 31, 2016, were \$47,319. The City of Baudette's contributions were equal to the required contributions as set by state statute.

2. Police and Fire Fund Contributions

Plan members were required to contribute 10.8 percent of their annual covered salary in calendar year 2016. The City of Baudette was required to contribute 16.20 percent of pay for members in calendar year 2016. The City of Baudette's contributions to the Police and Fire Fund for the year ended December 31, 2016, were \$24,914. The City of Baudette's contributions were equal to the required contributions as set by state statute.

C. Pension Costs

1. General Employees Fund Pension Costs

At December 31, 2016, the City of Baudette reported a liability of \$820,070 for its proportionate share of the General Employees Fund's net pension liability. The City of Baudette's net pension liability reflected a reduction due to the State of Minnesota's contribution of \$6 million to the fund in 2016. The State of Minnesota considered a non-employer contributing entity and the State's contribution meets the definition of a special funding situation. The State of Minnesota's proportionate share of the net pension liability associated with the City of Baudette totaled \$10,677.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

III. Defined Benefit Pension Plans

C. Pension Costs

1. General Employees Fund Pension Costs (Continued)

The net pension liability was measured as of June 30, 2016 and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of the date. The City of Baudette's proportion share was .0101 percent which was an increase of .0002 percent from its proportion measured as of June 30, 2016.

There were no provision changes during the measurement period.

At December 31, 2016, the City of Baudette reported its proportionate share of the General Employees Plan's deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual economic experience	\$ -	\$ 66,270
Changes in actuarial assumptions	160,570	-
Difference between projected and actual investment earnings	154,916	-
Changes in proportion	7,774	-
Contributions paid to PERA subsequent to the measurement date	23,556	-
Total	\$ 346,816	\$ 66,270

\$23,556 reported as deferred outflows of resources related to pensions resulting from the City of Baudette's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2017. Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended December 31:	Pension Expense Amount
2017	72,645
2018	72,645
2019	82,078
2020	29,623
2021	-

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

III. Defined Benefit Pension Plans (Continued)

2. Police and Fire Fund Pension Costs

At December 31, 2016, The City of Baudette reported a liability of \$642,108 for its proportionate share of the Police and Fire Fund's net pension liability. The net pension liability was measured as of June 30, 2016, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The City of Baudette's proportion of the net pension liability was based on the City of Baudette's contributions received by PERA during the measurement period for employer payroll paid dates from July 1, 2016, through June 30, 2016, relative to the total employer contributions received from all PERA's participating employers. At June 30, 2016, the City of Baudette's proportion was .016 percent which was unchanged from its proportion measured as of June 30, 2016.

There were no provision changes during the measurement period.

For the year ended December 31, 2016, the City of Baudette recognized pension expense of \$109,184 for its proportionate share of the Police and Fire Plan's pension expense. The City of Baudette also recognized \$1,440 for the year ended December 31, 2016 as pension expense (and an offsetting reduction of net pension liability) for its proportionate share of the State of Minnesota's on-behalf contributions to the Police and fire Fund. Legislation passed in 2013 required the State of Minnesota begin contribution \$9 million to the Police and Fire Fund each year, starting in fiscal year 2014.

As of December 31, 2016, the City of Baudette reported its proportionate share of the Police and Fire Plan's deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual economic experience	\$ -	\$ 69,732
Changes in actuarial assumptions	353,380	-
Difference between projected and actual investment earnings	97,990	-
Changes in proportion	12,001	-
Contributions paid to PERA subsequent to the measurement date	12,719	-
Total	\$ 476,090	\$ 69,732

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

III. Defined Benefit Pension Plans

2. Police and Fire Fund Pension Costs (Continued)

\$12,719 reported as deferred outflows of resources related to pensions resulting from the City of Baudette's contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2017. Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended December 31:	Pension Expense Amount
2017	123,752
2018	123,752
2019	127,578
2020	18,557
2021	-

D. Actuarial Assumptions

The total pension liability in the June 30, 2016, actuarial valuation determined using the following actuarial assumptions:

Inflation	2.50% per year
Active Member Payroll Growth	3.25% per year
Investment Rate of Return	7.50%

Salary increases were based on a service-related table. Mortality rates for active members, retirees, survivors and disabilitants were based on RP-2014 tables for the General Employees Plan and RP-2000 tables for the Police and Fire Plan for males and females, as appropriate, with slight adjustments. Cost of living benefit increases for retirees are assumed to be: 1 percent per year for all future years for the General Employees Plan and Police and fire Plan.

Actuarial assumptions used in the June 30, 2016 valuation were based on the results of actuarial experience studies. The most recent four-year experience study in the General Employees Plan was completed in 2016. The experience study for Police and fire Plan was for the period July 1, 2004 through June 30, 2009.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

III. Defined Benefit Pension Plans

D. Actuarial Assumptions (Continued)

The following changes in actuarial assumptions occurred in 2016:

General Employees Fund

1. The assumed post-retirement benefit increase rate was changed from 1.0% per year through 2035 and 2.5% per year thereafter to 1.0% per year for all future years.
2. The assumed investment return was changed from 7.9% to 7.5%. The single discount rate was changed from 7.9% to 7.5%.
3. Other assumptions were changed pursuant to the experience study dated June 30, 2016. The assumed future salary increases, payroll growth, and inflation were decreased by 0.25% to 3.25% for payroll growth and 2.5% for inflation.

Police and Fire Fund

1. The assumed post-retirement benefit increase rate was changed from 1.0% per year through 2037 and 2.5% thereafter to 1.0% per year for all future years.
2. The assumed investment return was changed from 7.9% to 7.5%. The single discount rate changed from 7.9% to 5.6%.
3. The assumed future salary increases, payroll growth, and inflation were decreased by 0.25% to 3.25% for payroll growth and 2.50% for inflation.

The State Board of Investment, which manages the investments of PERA, prepares an analysis of the reasonableness of the long-term expected rate of return on a regular basis using a building-block method in which best-estimate ranges of expected future rates of return are developed for each major asset class. These ranges are combined to produce an expected long-term rate of return by weighting the expected future rates of return by the target asset allocation percentages. The target allocation and best estimates of geometric real rates of return for each major asset class are summarized in the following table:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
Domestic Stocks	45%	5.50%
International Stocks	15%	6.00%
Bonds	18%	1.45%
Alternative Assets	20%	6.40%
Cash	2%	0.50%

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

III. Defined Benefit Pension Plans (Continued)

E. Discount Rate

The discount rate used to measure the total pension liability in 2016 was 7.50%, a reduction from the 7.9% used in 2016. The projection of cash flows used to determine the discount rate assumed that contributions from plan members and employers will be made at rates set in Minnesota Statutes. Based on these assumptions, the fiduciary net position of the General Employees Fund was projected to be available to make all projected 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 liability.

In the Police and Fire Fund, the fiduciary net position was projected to be available to make all projected future benefit payments of current plan members through June 30, 2056 and June 30, 2058 respectively. Beginning in fiscal years ended June 30, 2057 for the Police and Fire Fund, when projected benefit payments exceed the funds' projected fiduciary net position, benefit payments were discounted at the municipal bond rate of 2.85% based on an index of 20-year general obligation bonds with an average AA credit rating at the measurement date. An equivalent single discount rate of 5.60% for the Police and Fire Fund was determined that produced approximately the same present value of projected benefits when applied to all years of projected benefits as the present value of projected benefits using 7.50% applied to all years of projected benefits through the point of asset depletion and 2.85% thereafter.

F. Pension Liability Sensitivity

The following presents the City of Baudette's proportionate share of the net pension liability for all plans it participates in, calculated using the discount rate disclosed in the preceding paragraph, as well as what the City of Baudette's proportionate share of the net pension liability would be if it were calculated using a discount rate one percentage point lower or one percentage point higher than the current discount rate:

Sensitivity of Net Pension Liability at Current Single Discount Rate General Employees Fund			
City of Baudette	1% Decrease in Discount Rate (6.50%)	Discount Rate (7.50%)	1% Increase in Discount Rate (8.50%)
Proportionate share of Net Pension Liability	\$ 1,164,742	\$ 820,070	\$ 536,154

Sensitivity of Net Pension Liability at Current Single Discount Rate Police and Fire Fund			
City of Baudette	1% Decrease in Discount Rate (4.60%)	Discount Rate (5.60%)	1% Increase in Discount Rate (6.60%)
Proportionate share of Net Pension Liability	\$ 898,666	\$ 642,108	\$ 432,317

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

III. Defined Benefit Pension Plans (Continued)

G. Pension Plan Fiduciary Net Position

Detailed information about each pension plan's fiduciary net position is available in a separately-issued PERA financial report that includes financial statements and required supplementary information. That report may be obtained on the internet at www.mnpera.org.

IV. Summary of Significant Contingencies and Other Items

A. Claims and Litigation

The City, in connection with the normal conduct of its affairs, may be involved in various claims, judgments, and litigation. The City Council estimates that the potential claims against the City not covered by insurance resulting from such litigation would not materially affect the financial statements of the City.

B. Risk Management

The City is exposed to various risks of loss related to torts; theft of, damage, or destruction of assets; errors or omissions; injuries to employees; employee health coverage; or natural disasters. The City has entered into a joint powers agreement with other Minnesota cities to form the League of Minnesota Cities Insurance Trust (LMCIT) to cover workers' compensation and property and casualty liabilities. There were no significant reductions in insurance from the prior year. The amount of settlements did not exceed insurance coverage for each of the past three fiscal years.

The League of Minnesota Cities Insurance Trust is a public entity risk pool currently operated as a common risk management and insurance program for its members. The City pays an annual premium based on its annual payroll and an experience modification factor for workers' compensation coverage.

C. Northern Municipal Power Agency

The City of Baudette is a member of the Northern Municipal Power Agency. The Power Agency was incorporated on December 14, 1976, and is a municipal corporation and political subdivision of the State of Minnesota composed of ten Minnesota and two North Dakota cities. The Power Agency was organized for the purpose of providing its members with electrical power pursuant to Minnesota Statutes, Section 453. The Power Agency has issued Electrical System Revenue Bonds, Series 1981, dated April 1, 1981, in the amount of \$268,000,000 to finance the purchase of a 30 percent interest in the Coyote Station Unit No. 1 electrical generating plant near Beulah, North Dakota. Under the Statute, the bonds are not the obligation of the member cities but of Northern Municipal Power Agency and are secured and payable solely from the revenues from the sale of electricity to member cities and to Minnkota Power Cooperative, Inc.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

IV. Summary of Significant Contingencies and Other Items (Continued)

D. Baudette-Lake of the Woods Airport Commission

In 1974, the City entered into a joint airport agreement with Lake of the Woods County to create a Baudette-Lake of the Woods Airport Commission for the purpose of joint operation of the Baudette International Airport.

In accordance with the agreement, the City and County shall each pay 50 percent of all net expenses incurred by the Airport. The City's contribution for 2016 was \$31,500. The City has no significant equity interest in the Airport, and accordingly neither assets nor liabilities of the Airport have been recorded in the City's financial statements. Audited financial information for the Baudette-Lake of the Woods Airport Commission can be obtained by contacting the City Clerk-Treasurer at P.O. Box 548, Baudette, Minnesota 56623.

REQUIRED SUPPLEMENTARY INFORMATION

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

Schedule 1

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2016**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues				
Property taxes	\$ 328,220	\$ 332,220	\$ 354,023	\$ 21,803
Licenses and permits	5,750	5,750	4,663	(1,087)
Intergovernmental	319,632	347,632	352,988	5,356
Charges for services	66,500	70,400	51,920	(18,480)
Fines and forfeitures	5,000	5,000	5,182	182
Gifts and contributions	25,200	17,200	16,450	(750)
Investment earnings	1,500	1,500	-	(1,500)
Miscellaneous	99,990	117,490	70,532	(46,958)
Total Revenues	\$ 851,792	\$ 897,192	\$ 855,758	\$ (41,434)
Expenditures				
Current				
General government				
Mayor/council	\$ 26,030	\$ 26,030	\$ 23,235	\$ 2,795
Administration	107,739	111,339	108,482	2,857
Elections	3,000	3,000	1,900	1,100
Professional services	10,000	20,000	16,952	3,048
Insurance	13,730	13,730	2,250	11,480
Cemetery	13,677	13,677	9,757	3,920
Planning and zoning	-	-	11,232	(11,232)
Buildings and grounds	20,988	20,988	15,511	5,477
Other general government	6,910	6,910	2,494	4,416
Total general government	\$ 202,074	\$ 215,674	\$ 191,813	\$ 23,861
Public safety				
Police	\$ 250,858	\$ 258,258	\$ 266,060	\$ (7,802)
Fire	77,160	77,160	63,267	13,893
Firefighters relief association	-	23,000	23,792	(792)
Other public safety	750	750	1,358	(608)
Total public safety	\$ 328,768	\$ 359,168	\$ 354,477	\$ 4,691
Highways and streets				
Streets and alleys	\$ 140,231	\$ 204,281	\$ 213,474	\$ (9,193)
Snow and ice removal	25,393	20,193	19,280	913
Street lighting	11,234	16,134	16,980	(846)
Total highways and streets	\$ 176,858	\$ 240,608	\$ 249,734	\$ (9,126)

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

***Schedule 1
(Continued)***

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2016**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget Positive (Negative)
	Original	Final		
Expenditures				
Current (continued)				
Culture and recreation				
Parks	\$ 80,797	\$ 62,197	\$ 62,035	\$ 162
Library	101,778	94,678	98,563	(3,885)
Total culture and recreation	\$ 182,575	\$ 156,875	\$ 160,598	\$ (3,723)
Economic development				
Airport	\$ 31,500	\$ 31,500	\$ 31,500	\$ -
Other economic development	35,450	60,450	56,854	3,596
Total economic development	\$ 66,950	\$ 91,950	\$ 88,354	\$ 3,596
Debt service				
Principal retirement	\$ -	\$ -	\$ 15,961	\$ (15,961)
Interest	-	-	7,976	(7,976)
Total debt service	\$ -	\$ -	\$ 23,937	\$ (23,937)
Capital outlay				
Public safety	30,100	36,900	38,456	(1,556)
Highways and streets	\$ 244,470	\$ 371,470	\$ 354,983	\$ 16,487
Culture and recreation	10,000	46,000	88,994	(42,994)
Total capital outlay	\$ 284,570	\$ 454,370	\$ 482,433	\$ (28,063)
Total Expenditures	\$ 1,241,795	\$ 1,518,645	\$ 1,551,346	\$ (32,701)
Excess of Revenues Over (Under)				
Expenditures	\$ (390,003)	\$ (621,453)	\$ (695,588)	\$ (74,135)
Other Financing Sources				
Transfers in	\$ 390,000	\$ 370,000	\$ 370,000	\$ -
Proceeds from issuance of debt	-	-	400,929	400,929
Total Other Financing Sources (Uses)	\$ 390,000	\$ 370,000	\$ 770,929	\$ 400,929
Net Change in Fund Balance	\$ (3)	\$ (251,453)	\$ 75,341	\$ 326,794
Fund Balance - January 1	1,209,441	1,209,441	1,209,441	-
Fund Balance - December 31	\$ 1,209,438	\$ 957,988	\$ 1,284,782	\$ 326,794

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

Schedule 2

**SCHEDULE OF CONTRIBUTIONS
PUBLIC EMPLOYEES RETIREMENT ASSOCIATION OF MINNESOTA
FOR THE YEAR ENDED DECEMBER 31, 2016**

GENERAL EMPLOYEES RETIREMENT FUND PENSION PLAN

Fiscal Year Ending	Statutorily Required Contribution	Contributions in Relation to the Statutorily Required Contribution	Contribution Deficiency (Excess)	Covered- Payroll	Contributions as a Percentage of Covered Payroll
December 31, 2016	\$ 47,319	\$ 47,319	\$ -	\$ 630,913	7.5%
December 31, 2015	\$ 45,992	\$ 45,992	\$ -	\$ 613,223	7.5%

PUBLIC EMPLOYEES POLICE AND FIRE FUND PENSION PLAN

Fiscal Year Ending	Statutorily Required Contribution	Contributions in Relation to the Statutorily Required Contribution	Contribution Deficiency (Excess)	Covered- Payroll	Contributions as a Percentage of Covered Payroll
December 31, 2016	\$ 24,914	\$ 24,914	\$ -	\$ 153,789	16.2%
December 31, 2015	\$ 24,554	\$ 24,554	\$ -	\$ 151,568	16.2%

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

Schedule 3

**SCHEDULE OF PROPORTIONATE SHARE OF NET PENSION LIABILITY
PUBLIC EMPLOYEES RETIREMENT ASSOCIATION
FOR THE YEAR ENDED DECEMBER 31, 2016**

GENERAL EMPLOYEES RETIREMENT FUND PENSION PLAN

<u>Fiscal Year Ending</u>	<u>Employer's Proportion of the Net Pension Liability</u>	<u>Employer's Proportionate Share of the Net Pension Liability</u>	<u>Employer's Proportionate Share of the State of Minnesota's Proportionate Share of the Net Pension Liability</u>	<u>Employer's Proportionate Share of the Net Pension Liability and the Employer's Proportionate Share of the State of Minnesota's Share of the Net Pension Liability</u>	<u>Covered Payroll</u>	<u>Proportionate Share of the Net Pension Liability as a Percentage of its Covered Payroll</u>	<u>Plan Fiduciary Net Position as a Percentage of the Total Pension Liability</u>
June 30, 2016	0.0101%	\$ 820,070	\$ 10,677	\$ 830,747	\$ 620,132	132.24%	68.90%
June 30, 2015	0.0099%	\$ 513,069	\$ -	\$ 513,069	\$ 600,264	85.47%	78.20%

PUBLIC EMPLOYEES POLICE AND FIRE FUND PENSION PLAN

<u>Fiscal Year Ending</u>	<u>Employer's Proportion of the Net Pension Liability</u>	<u>Employer's Proportionate Share of the Net Pension Liability</u>	<u>Employer's Proportionate Share of the State of Minnesota's Proportionate Share of the Net Pension Liability</u>	<u>Employer's Proportionate Share of the Net Pension Liability and the Employer's Proportionate Share of the State of Minnesota's Share of the Net Pension Liability</u>	<u>Covered Payroll</u>	<u>Proportionate Share of the Net Pension Liability as a Percentage of its Covered Payroll</u>	<u>Plan Fiduciary Net Position as a Percentage of the Total Pension Liability</u>
June 30, 2016	0.0040%	\$ 160,527	\$ 1,440	\$ 161,967	\$ 151,229	106.15%	63.90%
June 30, 2015	0.0160%	\$ 151,206	\$ 1,260	\$ 152,466	\$ 150,904	100.20%	86.60%

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION
AS OF AND FOR THE YEAR ENDED DECEMBER 31, 2016

I. Budgetary Information

Annual budgets are adopted on a basis consistent with accounting principles generally accepted in the United States of America. All annual appropriations lapse at fiscal year-end.

In September of each year, the City Council drafts a preliminary budget after giving interested citizens a reasonable opportunity to be heard. The final budget is approved in December and a certified levy is sent to Lake of the Woods County. Truth in taxation requires that a final levy may not exceed a preliminary levy.

The appropriated budget is prepared by fund, function, and department. The legal level of budgetary control (i.e., the level at which expenditures may not legally exceed appropriations) is the departmental level.

II. Excess of Expenditures Over Budget

The following departments had expenditures in excess of budget for the year ended December 31, 2016:

	<u>Expenditures</u>	<u>Budget</u>	<u>Excess</u>
General Fund			
General government			
Planning and zoning	\$ 11,232	\$ -	\$ (11,232)
Public safety			
Police	266,060	258,858	(7,202)
Firefighters relief association	23,792	23,000	(792)
Other public safety	1,358	750	(608)
Highways and streets			
Streets and alleys	213,474	204,281	(9,193)
Street lighting	16,980	16,134	(846)
Culture and recreation			
Library	98,563	94,678	(3,885)
Debt service			
Principal retirement	15,961	-	(15,961)
Interest	7,976	-	(7,976)
Capital outlay			
Public safety	38,456	36,900	(1,556)
Culture and recreation	88,994	46,000	(42,994)

III. Net Pension Liability

The information presented in the required supplementary schedules was used in the actuarial valuation for purposes of determining the actuarially determined contribution rates. Changes in actuarial assumptions are discussed in Note III to the Financial Statements. The assumptions and methods used for this actuarial valuation were recommend by PERA and adopted by the City Council.

OTHER SCHEDULES

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

Schedule 4

**SCHEDULE OF INTERGOVERNMENTAL REVENUE
FOR THE YEAR ENDED DECEMBER 31, 2016**

Shared Revenue

State

Firefighters relief association (supplemental benefits)	\$	1,000
Fire state aid		19,938
Local government aid		301,822
Market value credit		388
Police state aid		16,538
PERA rate reimbursement		<u>2,760</u>
Total Shared Revenue	\$	<u>342,446</u>

State

Minnesota Department/Board of

Peace Officer Standards and Training	\$	1,251
Transportation		<u>1,500</u>

Total Grants **\$** 2,751

Federal

Department of Housing and Economic Development	\$	1,520
Department of Transportation		<u>6,271</u>

Total Federal **\$** 7,791

Total Grants **\$** 10,542

Total Intergovernmental Revenue **\$** 352,988

MANAGEMENT AND COMPLIANCE SECTION

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

SCHEDULE OF FINDINGS AND RECOMMENDATIONS
FOR THE YEAR ENDED DECEMBER 31, 2016

Schedule 5

**FINDINGS RELATED TO FINANCIAL STATEMENTS AUDITED IN ACCORDANCE
WITH GOVERNMENT AUDITING STANDARDS**

INTERNAL CONTROL

PREVIOUSLY REPORTED ITEMS NOT RESOLVED

2011-001 Segregation of Duties

Criteria: Management is responsible for establishing and maintaining internal control. This responsibility includes the internal controls over the various accounting cycles, the fair presentation of the financial statements and related notes, and the accuracy and completeness of all financial records and related information. Adequate segregation of duties is a key internal control in an organization's accounting system.

Condition: Due to the limited number of personnel within the City of Baudette, segregation of the accounting functions necessary to ensure adequate internal accounting control is not possible. Generally, one person is responsible for billing, collecting, depositing, and recording receipts as well as reconciling bank accounts.

Context: The small size and available staffing within the City limits the internal control that management can design and implement into the organization.

Effect: Without adequate segregation of duties, opportunities for errors and irregularities or fraudulent activities to occur are created and may not be detected in a timely manner.

Cause: This is not unusual in operations the size of the City, where, because of staffing limitations, it is impractical to achieve a desirable level of segregation of duties. Management has determined that, given limited resources, it is not feasible to achieve the desired level of segregation of duties.

Recommendation: Management should continually be aware that segregation of duties is not adequate from an internal control point of view. We recommend the City Council be aware that limited staffing causes inherent risks in safeguarding the City's assets and the proper reporting of financial activity. We recommend the City Council continue to implement oversight procedures and monitor those procedures to determine if they are still effective internal controls.

**CITY OF BAUDETTE
BAUDETTE, MINNESOTA**

Schedule 5
(Continued)

2011-002 Internal Controls

Criteria: The financial statements are the responsibility of the City of Baudette's management. Internal control over financial reporting is a process designed to provide reliable assurance about the achievement of the City's objectives with regard to reliability of financial reporting, and compliance with applicable laws and regulations. These controls must include a process for monitoring to ensure, effectiveness and efficiency of operations.

Condition: Internal controls over financial reporting and the safeguarding of assets against unauthorized acquisition, use, or disposition include controls related to financial reporting and operational objectives. The City does not have a process for monitoring to ensure the internal controls are effective.

Context: Although the City of Baudette has a system of internal control in spite of limited staff, they do not have written documentation of the process for monitoring those controls.

Effect: Without a documented process for monitoring internal controls, the City cannot provide assurance about the reliability of financial reporting or the effectiveness and efficiency of operations.

Cause: The City of Baudette has never formalized its policies and procedures for internal controls and monitoring of those controls into a written comprehensive document.

Recommendation: We recommend the City formalize written documentation of their internal controls and the monitoring process to ensure the reliability of financial reporting and the effectiveness and efficiency of operations.

ITEMS ARISING THIS YEAR

2016-001 Accounting and Financial Reporting for Pensions

Criteria: The Governmental Accounting Standards Board (GASB) issued Statement No. 68, *Accounting and Financial Reporting for Pensions*, which provides accounting and reporting standards for pensions offered to retirees. GASB Statement 68 was applicable to the City of Baudette for the year ended December 31, 2015.

Condition: GASB Statement 68 has not yet been fully implemented by the City of Baudette as required. The City has reported net pension liability for City employees, but this does not include members of the Fire Relief Association. The City Fire Relief Association has not undergone an actuarial study to determine its net pension liability.

Context: The City should encourage the Fire Relief Association to obtain an actuarial study to determine its net pension liability for its inclusion in the City's financial statements.

Effect: Because the City of Baudette has not fully complied with the requirements of GASB Statement 68, a qualified opinion is issued on the government-wide financial statements.

Cause: The Fire Relief Association has not hired an actuary to determine its net pension liability to meet the requirements for financial reporting under GASB Statement 68.

Recommendation: We recommend the City Council encourage the Fire Relief Association to obtain an actuarial study to determine its net pension liability for inclusion in the City's financial statements.

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

Independent Auditor's Report

City Council
City of Baudette

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 remaining fund information of the City of Baudette as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated June 13, 2017.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City of Baudette'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.

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. *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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section 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. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Findings and Responses as items 2011-001 and 2011-002, that we consider to be significant deficiencies.

Compliance and Other Matters

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

Minnesota Legal Compliance

The *Minnesota Legal Compliance Audit Guide for Cities*, promulgated by the State Auditor pursuant to Minnesota Statute, § 6.65, contains seven categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, miscellaneous provisions, and tax increment financing. Our audit considered all of the listed categories, except we did not test for compliance with the provisions for tax increment financing because the City of Baudette has no tax increment financing districts.

In connection with our audit, nothing came to our attention that caused us to believe that the City failed to comply with the provisions of the *Minnesota Legal Compliance Audit Guide for Cities*. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the City's noncompliance with the above referenced provisions.

City's Responses to Findings

The City's responses to the findings identified in our audit have been included in the accompanying Schedule of Findings and Recommendations. The City's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control, compliance and the provisions of the *Minnesota Legal Compliance Audit Guide for Cities*, and the result 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.



Hoffman, Philipp, & Knutson, PLLC

June 13, 2017