



CITY OF CUSTER

FINANCIAL STATEMENTS AND INDEPENDENT AUDITOR'S REPORT
DECEMBER 31, 2015



Ketel Thorstenson, LLP
Certified Public Accountants/Business & Personal Consultants

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CITY OF CUSTER

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INDEPENDENT AUDITOR'S REPORT

City Council
City of Custer
Custer, South Dakota

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, and each major fund of the **CITY OF CUSTER** (the City), as of and for the year ended December 31, 2015, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, and each major fund of the City, as of December 31, 2015, 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.

City Council

Other Matters - Required Supplementary Information

Accounting principles generally accepted in the United States of America require that management's discussion and analysis on pages 3 through 11, budgetary comparison information on pages 41 through 44, pension information on pages 45 and 46, and notes to required supplementary information on page 47 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 Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated May 2, 2016 on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's internal control over financial reporting and compliance.



KETEL THORSTENSON, LLP
Certified Public Accountants

May 2, 2016

CITY OF CUSTER

MANAGEMENT'S DISCUSSION AND ANALYSIS DECEMBER 31, 2015

This section of the City of Custer (the City) annual financial report presents our discussion and analysis of the City's financial performance during the year ended December 31, 2015. Please read it in conjunction with the City's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

The City's net position from governmental and business-type activities increased by \$586,086, primarily due to the increase in capital assets with the largest being the Montgomery & Sixth Street Project; in addition sales tax revenue was up; and some expenditures that were anticipated were not incurred, with the largest being the hospital sales tax subsidy. Due to the 2014 and 2015 hospital sales tax subsidies being placed on hold, there is a \$694,000 asset that has been set aside.

During the year, the City's revenues generated from charges for services, taxes and other revenues of the governmental programs were \$3,477,770, and the governmental program expenditures were \$2,786,310.

The City's proprietary funds' expenses exceeded revenues by \$105,374 primarily due to general expenses such as supplies, utilities, repairs, etc. for both water and sewer being higher and revenue only slightly increasing.

The general fund reported a \$339,443 current year increase due to the hospital sales tax subsidy being placed on hold for another year and some general fund expenditures being down.

OVERVIEW OF THE FINANCIAL STATEMENTS

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

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

The first two statements are government-wide financial statements that provide both long-term and short-term information about the City's overall financial status.

The remaining statements are fund financial statements that focus on individual parts of the City government, reporting the City's operations in more detail than the government-wide statements.

The governmental funds statements tell how general government services, like public safety, were financed in the short-term, as well as what remains for future spending.

Proprietary fund statements offer short- and long-term financial information about the activities that the City operates like businesses. The City has three proprietary funds – the Water Fund, the Sewer Fund, and the Solid Waste Fund.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of required supplementary information that further explains and supports the information in the financial statements.

CITY OF CUSTER

**MANAGEMENT’S DISCUSSION AND ANALYSIS (CONTINUED)
DECEMBER 31, 2015**

OVERVIEW OF THE FINANCIAL STATEMENTS (CONTINUED)

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

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

CITY OF CUSTER

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED) DECEMBER 31, 2015

OVERVIEW OF THE FINANCIAL STATEMENTS (CONCLUDED)

Government-wide Statements

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

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

Increases or decreases in the City's net position are an indicator of whether its financial health is improving or deteriorating, respectively.

To assess the overall health of the City, you need to consider additional non-financial factors, such as changes in the City's property tax base and changes in the sales tax revenue base.

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

Governmental Activities -- This category includes most of the City's basic services, such as police, fire, public works, parks department and general administration. Property taxes, sales taxes, charges for services, state grants and interest earnings finance most of these activities.

Business-type Activities -- The City charges a fee to customers to help cover the costs of certain services it provides. The City's water, sewer, and solid waste program are included here.

Fund Financial Statements

The fund financial statements provide more detailed information about the City's most significant funds – not the City as a whole. Funds are accounting devices that the City uses to keep track of specific sources of funding and spending for particular purposes.

State law requires some of the funds. The City Council establishes other funds to control and manage money for particular purposes or to show that it is properly using certain taxes and grants.

The City has two kinds of funds:

Governmental Funds – Most of the City's basic services are included in the governmental funds, which focus on (1) how cash and other financial assets that can be readily converted to cash flow in and out and (2) the balances left at the end of the year that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs. Because this information does not encompass the additional long-term focus of the government-wide statements, we provide additional information at the bottom of the governmental funds statements, or on the subsequent page, that explains the relationship (or differences) between them.

Proprietary Funds – Services for which the City charges customers a fee are generally reported in proprietary funds. Proprietary funds, like the government-wide statements, provide both short- and long-term financial information. The City's proprietary funds are the same as its business-type activities, but provide more detail and additional information, such as cash flows.

CITY OF CUSTER

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
DECEMBER 31, 2015**

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

The City's combined net position increased by 3.03 percent between 2014 and 2015 – increasing by \$586,086.

Table A-1 Statement of Net Position						
	Governmental Activities		Business-Type Activities		Total	
	2014	2015	2014	2015	2014	2015
Current & Other Assets	\$ 3,457,774	\$ 3,929,253	\$ 2,861,386	\$ 3,060,796	\$ 6,319,160	\$ 6,990,049
Capital Assets	9,417,428	9,714,889	11,076,076	10,704,245	20,493,504	20,419,134
Total Assets	\$ 12,875,202	\$ 13,644,142	\$ 13,937,462	\$ 13,765,041	\$ 26,812,664	\$ 27,409,183
Pension Related Deferred Outflows	\$ -	\$ 197,133	\$ -	\$ 68,163	\$ -	\$ 265,296
Long-Term Debt	\$ 4,243,454	\$ 4,230,879	\$ 3,310,611	\$ 3,206,521	\$ 7,554,065	\$ 7,437,400
Other Liabilities	24,422	26,044	41,779	48,247	66,201	74,291
Total Liabilities	\$ 4,267,876	\$ 4,256,923	\$ 3,352,390	\$ 3,254,768	\$ 7,620,266	\$ 7,511,691
Pension Related Deferred Inflows	\$ -	\$ 155,689	\$ -	\$ 53,832	\$ -	\$ 209,521
Net Position:						
Net Investment in						
Capital Assets	\$ 5,217,686	\$ 5,523,354	\$ 7,825,313	\$ 7,558,564	\$ 13,042,999	\$ 13,081,918
Restricted	225,497	403,329	106,920	157,735	332,417	561,064
Unrestricted	3,164,143	3,501,980	2,652,839	2,808,305	5,816,982	6,310,285
Total Net Position	\$ 8,607,326	\$ 9,428,663	\$ 10,585,072	\$ 10,524,604	\$ 19,192,398	\$ 19,953,267
Beginning Net Position	\$ 7,220,883	\$ 8,607,326	\$ 10,730,223	\$ 10,585,072	\$ 17,951,106	\$ 19,192,398
Change in Accounting Principle	-	129,877	-	44,906	-	174,783
Change in Net Position	1,386,443	691,460	(145,151)	(105,374)	1,241,292	586,086
Percentage of Change						
Net Position	19.20%	7.91%	-1.35%	-0.99%	6.91%	3.03%

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

CITY OF CUSTER

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
DECEMBER 31, 2015**

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONTINUED)

The City's revenues totaled \$4,873,237. See Figure A-1 below for various sources of revenue. The total revenue decreased while the expenditures increased. The City's expenses cover a range of services, including public works, general government, and utility services for water, sewer, and sanitation (See Figure A-2).

Figure A-1: Revenue Sources for 2015

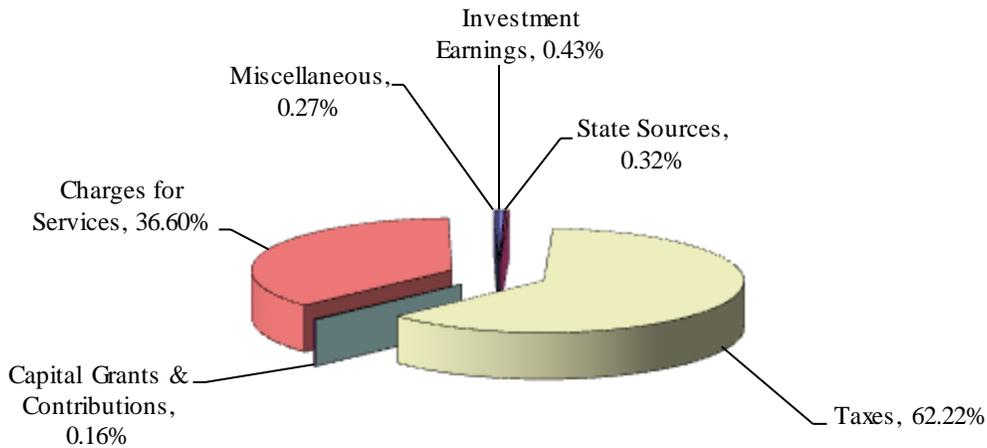
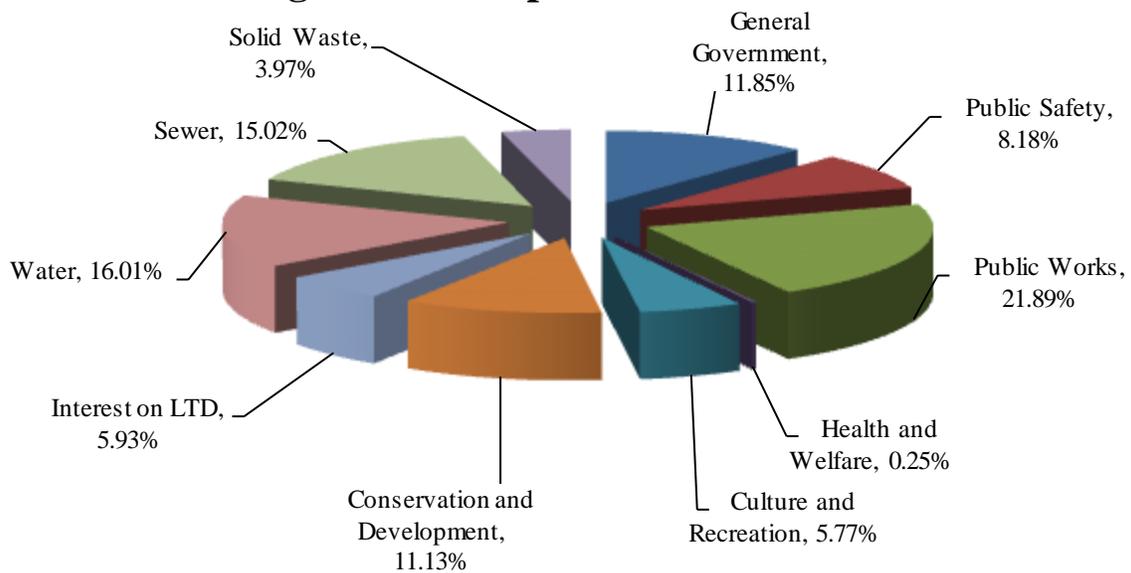


Figure A-2: Expenditures for 2015



CITY OF CUSTER

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
DECEMBER 31, 2015

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONTINUED)

Table A-2						
Statement of Activities						
	Total Governmental Activities		Total Business-Type Activities		Grand Total	
	2014	2015	2014	2015	2014	2015
Revenues						
<i>Program Revenues</i>						
Charges for Services	\$ 411,154	\$ 402,477	\$ 1,349,951	\$ 1,381,369	\$ 1,761,105	\$ 1,783,846
Capital Grants and Contributions	612,697	3,797	-	4,100	612,697	7,897
<i>General Revenues</i>						
Taxes	2,865,366	3,031,976	-	-	2,865,366	3,031,976
Revenue State Sources	14,143	15,460	-	-	14,143	15,460
Unrestricted Investment Earnings	9,557	10,968	10,441	9,998	19,998	20,966
Other	119,810	13,092	19,799	-	139,609	13,092
Total Revenues	\$ 4,032,727	\$ 3,477,770	\$ 1,380,191	\$ 1,395,467	\$ 5,412,918	\$ 4,873,237
Expenses						
General Government	\$ 492,822	\$ 507,931	\$ -	\$ -	\$ 492,822	\$ 507,931
Public Safety	353,091	350,583	-	-	353,091	350,583
Public Works	838,972	938,373	-	-	838,972	938,373
Health and Welfare	8,223	10,602	-	-	8,223	10,602
Culture and Recreation	244,190	247,372	-	-	244,190	247,372
Conservation and Development	443,437	477,311	-	-	443,437	477,311
Interest on Long-Term Debt	265,549	254,138	-	-	265,549	254,138
Water Services	-	-	707,040	686,471	707,040	686,471
Sewer Services	-	-	638,930	644,108	638,930	644,108
Solid Waste	-	-	179,372	170,262	179,372	170,262
Total Expenses	\$ 2,646,284	\$ 2,786,310	\$ 1,525,342	\$ 1,500,841	\$ 4,171,626	\$ 4,287,151
Increase (Decrease) in						
Net Position	\$ 1,386,443	\$ 691,460	\$ (145,151)	\$ (105,374)	\$ 1,241,292	\$ 586,086
Net Position - Beginning	\$ 7,220,883	\$ 8,607,326	\$ 10,730,223	\$ 10,585,072	\$ 17,951,106	\$ 19,192,398
Change in Accounting Principle	-	129,877	-	44,906	-	174,783
Net Position - Ending	\$ 8,607,326	\$ 9,428,663	\$ 10,585,072	\$ 10,524,604	\$ 19,192,398	\$ 19,953,267

CITY OF CUSTER

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
DECEMBER 31, 2015**

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONCLUDED)

Governmental Activities

Revenue of the City's governmental activities exceeded expenses by \$691,460. Factors contributing to these results included:

- Hospital sales tax subsidy expenditure was placed on hold for another year, so no money was paid out.
- An increase in sales tax revenue.
- Several general fund function expenditures were down.

Business-Type Activities

Expenses of the City's business-type activities exceeded revenues by \$105,374. The factor contributing to these results included the general expenses such as supplies, utilities, repairs, etc. for both water and sewer being higher while revenue only slightly increased.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

The financial analysis of the City's funds mirror those highlighted in the analysis of governmental and business-type activities presented above. The City maintains several governmental funds and three business-type funds.

GENERAL FUND BUDGETARY HIGHLIGHTS

Over the course of the year, the City Council revised the City budget one time. The amendment increased appropriations by contingency transfer to prevent budget overruns.

CITY OF CUSTER

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
DECEMBER 31, 2015**

CAPITAL ASSET ADMINISTRATION

By the end of 2015, the City had invested \$20,419,134 in a broad range of capital assets, including land, buildings, and various machinery and equipment. (See Table A-3.) This amount represents a net decrease (including additions and deductions) of \$74,370. This decrease was due to the increase in depreciation from sewer projects completed in the last couple years.

	Governmental Activities		Business-type Activities	
	2014	2015	2014	2015
Land	\$ 1,070,706	\$ 1,070,706	\$ 568,035	\$ 568,035
Buildings	1,472,500	1,447,090	642,671	613,298
Improvements	6,233,383	6,398,656	9,379,433	9,098,275
Machinery and Equipment	412,971	418,390	485,937	405,619
Construction Work in Progress	227,868	380,047	-	19,018
Total	\$ 9,417,428	\$ 9,714,889	\$ 11,076,076	\$ 10,704,245

LONG-TERM DEBT

	Governmental Activities		Business-type Activities	
	2014	2015	2014	2015
Compensated Absences	\$ 43,712	\$ 39,344	\$ 59,848	\$ 60,840
TIF #1 - Boothill	665,465	665,465	-	-
Accrued Interest - TIF #1	51,869	33,965	-	-
TIF #2 - Stonehill	1,569,901	1,569,901	-	-
Accrued Interest - TIF #2	594,895	680,526	-	-
TIF #4 - Downtown	1,025,699	968,441	-	-
TIF #5 - Pamida	291,913	273,237	-	-
Water Revenue Bonds	-	-	2,330,736	2,260,351
Sewer Revenue Bonds	-	-	920,027	885,330
Total	\$ 4,243,454	\$ 4,230,879	\$ 3,310,611	\$ 3,206,521

The City made scheduled payments on long-term debt.

CITY OF CUSTER

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONCLUDED)
DECEMBER 31, 2015**

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The City's current economic position has shown continued improvement. The City will experience an increase in total property valuation of \$2,372,628, up 2 percent from the prior year, thus increasing total property tax revenue by approximately \$15,000. Under the state-mandated property tax freeze, property taxes from one year to the next may increase three percent or an amount based on the CPI, whichever is lower.

One of the primary sources of revenue to the City is based on taxable retail sales in the community (sales tax). The City has experienced an increase in sales tax of 5.84 percent over the prior year and has budgeted for a \$164,000 decrease in sales tax revenue from the 2015 actual for the next year.

The City's adopted General Fund budget for the next fiscal year will increase to \$4,498,055. The largest portion of this increase is due to the hospital sales tax subsidy that has been previously on hold and capital improvement projects.

The City's adopted business-type budget for the next fiscal year will increase to \$2,370,240. This increase is due to personnel expenditures, capital improvements, sewer debt repayment and the increase in sewer fund depreciation expense.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the City's finances and to demonstrate the City's accountability for the money it receives. If you have questions about this report or need additional information, contact the City of Custer Finance Office, 622 Crook Street, Custer, SD 57730.

CITY OF CUSTER

**STATEMENT OF NET POSITION
DECEMBER 31, 2015**

	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTAL
ASSETS			
Cash and Investments (Note 2)	\$ 3,579,967	\$ 2,753,217	\$ 6,333,184
Restricted Investments (Notes 3 and 7)	-	106,920	106,920
Receivables	205,464	164,175	369,639
Other Assets (Note 9)	38,308	-	38,308
Net Pension Asset (Note 8)	105,514	36,484	141,998
Capital Assets (Note 6):			
Land and Construction in Progress	1,450,753	587,053	2,037,806
Other Capital Assets, Net of Depreciation	8,264,136	10,117,192	18,381,328
TOTAL ASSETS	13,644,142	13,765,041	27,409,183
DEFERRED OUTFLOWS OF RESOURCES			
Pension Related Deferred Outflows of Resources (Note 8)	197,133	68,163	265,296
TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	\$ 13,841,275	\$ 13,833,204	\$ 27,674,479
LIABILITIES			
Accounts Payable	\$ 11,008	\$ 7,059	\$ 18,067
Other Current Liabilities	15,036	41,188	56,224
Long-Term Liabilities (Note 7):			
Due Within One Year	238,272	169,371	407,643
Due in More Than One Year	3,992,607	3,037,150	7,029,757
TOTAL LIABILITIES	4,256,923	3,254,768	7,511,691
DEFERRED INFLOWS OF RESOURCES			
Pension Related Deferred Inflows of Resources (Note 8)	155,689	53,832	209,521
NET POSITION			
Net Investment in Capital Assets	5,523,354	7,558,564	13,081,918
Restricted for:			
Debt Service	5,434	106,920	112,354
Business Improvement District	52,841	-	52,841
Promoting the City	92,447	-	92,447
SDPAA (Note 9)	26,385	-	26,385
SDRS Pension (Note 8)	146,958	50,815	197,773
Permanently Restricted Purposes:			
Expendable	29,264	-	29,264
Nonexpendable	50,000	-	50,000
Unrestricted	3,501,980	2,808,305	6,310,285
TOTAL NET POSITION	9,428,663	10,524,604	19,953,267
TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION	\$ 13,841,275	\$ 13,833,204	\$ 27,674,479

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

CITY OF CUSTER

STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2015

Functions/Programs	Expenses	--- Program Revenues ---		Net (Expense) Revenue and		Total
		Charges for Services	Capital Grants and Contributions	Governmental Activities	Business-Type Activities	
Primary Government						
Governmental Activities:						
General Government	\$ 507,931	\$ 83,426	\$ -	\$ (424,505)	\$ -	\$ (424,505)
Public Safety	350,583	740	-	(349,843)	-	(349,843)
Public Works	938,373	99,887	-	(838,486)	-	(838,486)
Health and Welfare	10,602	-	-	(10,602)	-	(10,602)
Culture and Recreation	247,372	14,230	3,797	(229,345)	-	(229,345)
Conservation and Development	477,311	-	-	(477,311)	-	(477,311)
Miscellaneous	-	204,194	-	204,194	-	204,194
Interest on Long-Term Debt	254,138	-	-	(254,138)	-	(254,138)
Total Governmental Activities	2,786,310	402,477	3,797	(2,380,036)	-	(2,380,036)
Business-Type Activities:						
Water	686,471	642,148	-	-	(44,323)	(44,323)
Sewer	644,108	550,153	4,100	-	(89,855)	(89,855)
Solid Waste	170,262	189,068	-	-	18,806	18,806
Total Business-Type Activities	1,500,841	1,381,369	4,100	-	(115,372)	(115,372)
Total Primary Government	\$ 4,287,151	\$ 1,783,846	\$ 7,897	(2,380,036)	(115,372)	(2,495,408)
General Revenues:						
Taxes:						
Property Taxes				1,102,023	-	1,102,023
Sales Taxes				1,929,953	-	1,929,953
State Shared Revenue				15,460	-	15,460
Unrestricted Investment Earnings				10,968	9,998	20,966
Miscellaneous Revenue				13,092	-	13,092
Total General Revenue				3,071,496	9,998	3,081,494
Change in Net Position				691,460	(105,374)	586,086
Net Position, Beginning				8,607,326	10,585,072	19,192,398
Change in Accounting Principle (Note 11)				129,877	44,906	174,783
Net Position, Beginning, as Restated				8,737,203	10,629,978	19,367,181
Net Position, Ending				\$ 9,428,663	\$ 10,524,604	\$ 19,953,267

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

CITY OF CUSTER

**BALANCE SHEET
GOVERNMENTAL FUNDS
DECEMBER 31, 2015**

	General Fund	Third Penny (Promotion) Fund	BID Fund
Assets			
101 Cash and Cash Equivalents (Note 2)	\$ 1,593,481	\$ 88,195	\$ 55,609
105 Investments (Note 2)	1,760,730	2,797	-
108 Property Taxes Receivable - Delinquent	38,865	-	-
110 Sales Taxes Receivable	118,903	7,274	-
115 Accounts Receivable	33,514	-	1,042
135 Interest Receivable	323	-	-
154.1 Restricted Deposits (Note 9)	26,385	-	-
155 Prepaid Expenses	11,923	-	-
Total Assets	\$ 3,584,124	\$ 98,266	\$ 56,651
Liabilities, Deferred Inflows of Resources and Fund Balances			
<i>Liabilities</i>			
202 Accounts Payable	\$ 1,379	\$ 5,819	\$ 3,810
216 Accrued Wages Payable	9,258	-	-
220 Customer Deposits	1,540	-	-
Total Liabilities	12,177	5,819	3,810
<i>Deferred Inflows of Resources (Note 4)</i>			
245 Unavailable Revenue - Property Taxes	19,064	-	-
Total Deferred Inflows of Resources	19,064	-	-
<i>Fund Balances</i>			
<i>263 Nonspendable:</i>			
263.51 Perpetual Care Cemetery	-	-	-
263.02 Prepaid Expenses	11,923	-	-
263.49 SDPAA Reserve (Note 9)	26,385	-	-
<i>264 Restricted:</i>			
264.01 Debt Service	-	-	-
264.03 Perpetual Care Cemetery	-	-	-
264.04 Promoting the City	-	92,447	-
264.09 Business Improvement District	-	-	52,841
<i>265 Committed:</i>			
265.99 Capital Reserve Fund	250,000	-	-
<i>266 Assigned:</i>			
266.01 Subsequent Year's Budget	558,912	-	-
266.02 Hospital Sales Tax	694,000	-	-
267 Unassigned	2,011,663	-	-
Total Fund Balances	3,552,883	92,447	52,841
Total Liabilities, Deferred Inflows of Resources and Fund Balances	\$ 3,584,124	\$ 98,266	\$ 56,651

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

TIF Debt Service Fund	Cemetery Perpetual Care Fund	Total Governmental Funds
\$ -	\$ 14,940	\$ 1,752,225
-	64,215	1,827,742
-	-	38,865
-	-	126,177
5,434	-	39,990
-	109	432
-	-	26,385
-	-	11,923
\$ 5,434	\$ 79,264	\$ 3,823,739

\$ -	\$ -	\$ 11,008
-	-	9,258
-	-	1,540
-	-	21,806

-	-	19,064
-	-	19,064

-	50,000	50,000
-	-	11,923
-	-	26,385
5,434	-	5,434
-	29,264	29,264
-	-	92,447
-	-	52,841
-	-	250,000
-	-	558,912
-	-	694,000
-	-	2,011,663
5,434	79,264	3,782,869

\$ 5,434	\$ 79,264	\$ 3,823,739
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CITY OF CUSTER

**RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO THE
GOVERNMENT-WIDE STATEMENT OF NET POSITION
DECEMBER 31, 2015**

Total Fund Balances - Governmental Funds \$ 3,782,869

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

Capital assets used in governmental activities are not financial resources and
therefore are not reported in the funds. 9,714,889

Long-term liabilities are not due and payable in the current period and therefore
not reported in the funds. (4,230,879)

Net pension asset reported in governmental activities is not an available financial
resource and therefore is not reported in the funds. 105,514

Pension related deferred outflows are components of pension asset and therefore
are not reported in the funds. 197,133

Pension related deferred outflows are components of pension asset and therefore
are not reported in the funds. (155,689)

Accrued interest is not due and payable in the current period and therefore is
not reported in the funds. (4,238)

Assets such as delinquent taxes receivable and grants receivable are not available
to pay for current period expenditures and therefore are deferred in the funds. 19,064

Total Net Position - Governmental Funds \$ 9,428,663

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

CITY OF CUSTER

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2015**

		General Fund	Third Penny (Promotion) Fund	BID Fund	TIF Debt Service Fund
Revenue					
<i>Taxes:</i>					
311	General Property Taxes	\$ 835,145	\$ -	\$ -	\$ 265,311
313	General Sales and Use Taxes	1,530,024	239,707	160,222	-
315	Amusement Taxes	480	-	-	-
319	Penalties and Interest on Delinquent Taxes	1,861	-	-	-
320	Licenses and Permits	74,325	-	-	-
<i>State Shared Revenue:</i>					
335.01	Bank Franchise Tax	2,567	-	-	-
335.03	Liquor Tax Reversion	12,893	-	-	-
335.04	Motor Vehicle Licenses (5%)	34,299	-	-	-
335.08	Local Government Highway and Bridge Fund	33,291	-	-	-
<i>County Shared Revenue:</i>					
338.02	County HBR Tax	28,097	-	-	-
<i>Charges for Goods and Services:</i>					
341	General Government	9,101	-	-	-
346	Culture and Recreation	14,230	-	-	-
348	Cemeteries	2,000	-	-	-
350	Fines and Forfeits	740	-	-	-
<i>Miscellaneous Revenue:</i>					
361	Earnings on Deposits and Investments	10,578	133	-	-
362	Rentals	5,320	-	-	-
368	Liquor Operating Agreement Income	204,194	-	-	-
369	Other	7,772	-	-	-
Total Revenue		2,806,917	239,840	160,222	265,311

Cemetery Perpetual Care Fund	Total Governmental Funds
\$ -	\$ 1,100,456
-	1,929,953
-	480
-	1,861
-	74,325
-	2,567
-	12,893
-	34,299
-	33,291
-	28,097
-	9,101
-	14,230
2,200	4,200
-	740
257	10,968
-	5,320
-	204,194
-	7,772
<u>2,457</u>	<u>3,474,747</u>

CITY OF CUSTER

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES (CONTINUED)
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2015**

	General Fund	Third Penny (Promotion) Fund	BID Fund	TIF Debt Service Fund
Expenditures				
<i>General Government:</i>				
411 Legislative	83,298	-	-	-
413 Elections	650	-	-	-
414 Financial Administration	148,612	-	-	-
419 Other	229,810	-	-	-
<i>Public Safety:</i>				
421 Police	350,583	-	-	-
<i>Public Works:</i>				
431 Highways and Streets	411,786	-	-	-
437 Cemeteries	25,291	-	-	-
<i>Health and Welfare:</i>				
444 Humane Society	10,602	-	-	-
<i>Culture and Recreation:</i>				
451 Custer Cruisin'	10,266	-	-	-
451 Swimming	39,441	-	-	-
452 Parks	112,460	-	-	-
<i>Conservation and Development:</i>				
465 Economic Development and Assistance	97,500	197,898	181,913	-
470 Debt Service	-	-	-	263,036
485 Capital Outlay	947,175	-	-	-
Total Expenditures	2,467,474	197,898	181,913	263,036
Net Change in Fund Balances	339,443	41,942	(21,691)	2,275
Fund Balances - December 31, 2014	3,213,440	50,505	74,532	3,159
Fund Balances - December 31, 2015	\$ 3,552,883	\$ 92,447	\$ 52,841	\$ 5,434

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

Cemetery Perpetual Care Fund	Total Governmental Funds
-	83,298
-	650
-	148,612
-	229,810
-	350,583
-	411,786
-	25,291
-	10,602
-	10,266
-	39,441
-	112,460
-	477,311
-	263,036
-	947,175
-	3,110,321
2,457	364,426
76,807	3,418,443
\$ 79,264	\$ 3,782,869

CITY OF CUSTER

RECONCILIATION OF THE GOVERNMENTAL FUNDS STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES TO THE GOVERNMENT-WIDE STATEMENT OF ACTIVITIES FOR THE YEAR ENDED DECEMBER 31, 2015

Net Change in Fund Balances - Total Government Funds \$ 364,426

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

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

Capital Asset Purchases Capitalized	947,175
Depreciation Expense	(541,661)

Capital assets contributed to the City, which are included in the Statement of Activities.	3,797
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Reduction of capital assets for projects that will not be completed.	(111,850)
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The governmental fund financial statement property tax accruals differ from the government-wide statement property tax accruals in that the fund financial statements require the amounts to be "available."	(774)
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Payment of principal on long-term debt is an expenditure in the governmental funds but the payment reduces long-term liabilities in the Statement of Net Position.	189,424
--	---------

Increases to the interest accrual on TIFs #1 and #2 does not require the use of current financial resources and therefore is not reported as expenditures in governmental funds.	(181,217)
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Accrued interest expense, excluding TIFs #1 and #2, reported in the Statement of Activities does not require the use of current financial resources and therefore is not reported as expenditures in governmental funds.	691
--	-----

Pension expense reported in the Statement of Activities does not require the use of current financial resources and are not reported as expenditures in the governmental funds.	(11,519)
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Changes in the pension related deferred outflows/inflows are direct components of pension asset and are not reflected in the governmental funds.	28,600
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Governmental funds do not reflect the change in accrued leave, but the Statement of Activities reflects the change in accrued leave through expenditures.	4,368
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Change in Net Position of Governmental Activities	\$ 691,460
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The accompanying notes are an integral part of the financial statements.

CITY OF CUSTER

**STATEMENT OF NET POSITION
PROPRIETARY FUNDS
DECEMBER 31, 2015**

	Water Fund	Sewer Fund	Solid Waste Fund	Total Proprietary Funds
Assets				
Current Assets				
101 Cash and Cash Equivalents (Note 2)	\$ 1,049,120	\$ 386,435	\$ 78,429	\$ 1,513,984
105 Investments (Note 2)	330,657	904,781	3,795	1,239,233
115 Accounts Receivable, Net	66,271	70,191	27,488	163,950
135 Interest Receivable	98	127	-	225
Total Current Assets	1,446,146	1,361,534	109,712	2,917,392
Noncurrent Assets				
107 Restricted Investments (Notes 3 and 7)	106,920	-	-	106,920
189 Net Pension Asset (Note 8)	17,737	18,747	-	36,484
Capital Assets (Note 6)				
160 Land	46,262	521,773	-	568,035
162 Buildings	926,269	546,755	-	1,473,024
163 Accumulated Depreciation (AD) - Buildings	(530,444)	(329,282)	-	(859,726)
164 Improvements Other Than Buildings	7,876,053	6,309,611	-	14,185,664
165 AD - Improvements Other Than Buildings	(2,713,979)	(2,373,410)	-	(5,087,389)
166 Machinery and Equipment	383,652	1,074,276	-	1,457,928
168 Construction Work in Progress	-	19,018	-	19,018
167 AD - Machinery and Equipment	(327,814)	(724,495)	-	(1,052,309)
Total Noncurrent Assets	5,784,656	5,062,993	-	10,847,649
Total Assets	7,230,802	6,424,527	109,712	13,765,041
Deferred Outflows of Resources				
196 Pension Related Deferred Outflows (Note 8)	33,138	35,025	-	68,163
Total Assets and Deferred Outflows of Resources	\$ 7,263,940	\$ 6,459,552	\$ 109,712	\$ 13,833,204

	Water Fund	Sewer Fund	Solid Waste Fund	Total Proprietary Funds
Liabilities and Net Position				
Current Liabilities				
202 Accounts Payable	\$ 292	\$ 5,832	\$ 935	\$ 7,059
205 Current Portion of Long-Term Debt (Note 7)	72,783	35,748	-	108,531
215 Accrued Interest Payable	4,600	6,235	-	10,835
216 Accrued Wages	2,613	2,745	-	5,358
220 Customer Deposits	24,995	-	-	24,995
233 Accrued Leave Payable (Note 7)	30,420	30,420	-	60,840
Total Current Liabilities	135,703	80,980	935	217,618
Long-Term Liabilities				
237 Long-Term Debt, Net of Current Portion (Note 7)	2,187,568	849,582	-	3,037,150
Total Liabilities	2,323,271	930,562	935	3,254,768
Deferred Inflows of Resources				
248 Pension Related Deferred Inflows (Note 8)	26,171	27,661	-	53,832
Net Position				
253.1 Net Investment in Capital Assets	3,399,648	4,158,916	-	7,558,564
253.21 Restricted for Debt Service	106,920	-	-	106,920
235.29 Restricted for SDRS Pension Purposes (Note 8)	24,704	26,111	-	50,815
262.0 Unrestricted	1,383,226	1,316,302	108,777	2,808,305
Total Net Position	4,914,498	5,501,329	108,777	10,524,604
Total Liabilities, Deferred Inflows of Resources, and Net Position	\$ 7,263,940	\$ 6,459,552	\$ 109,712	\$ 13,833,204

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

CITY OF CUSTER

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION
 PROPRIETARY FUNDS
 FOR THE YEAR ENDED DECEMBER 31, 2015**

	Water Fund	Sewer Fund	Solid Waste Fund	Total Proprietary Funds
Operating Revenue				
380 Charges for Goods and Services	\$ 642,148	\$ 550,153	\$ 189,068	\$ 1,381,369
Operating Expenses				
410 Personal Services	204,741	213,956	-	418,697
420 Other Current Expenses	173,990	127,394	170,262	471,646
457 Depreciation	215,369	272,871	-	488,240
Total Operating Expenses	594,100	614,221	170,262	1,378,583
Operating Income (Loss)	48,048	(64,068)	18,806	2,786
Non-Operating Income (Expense)				
361 Earnings on Deposits and Investments	4,645	5,202	151	9,998
470 Interest Expense	(92,371)	(29,887)	-	(122,258)
Total Non-Operating Income (Expense)	(87,726)	(24,685)	151	(112,260)
Income before Contributions	(39,678)	(88,753)	18,957	(109,474)
391.07 Capital Contributions	-	4,100	-	4,100
Change in Net Position	(39,678)	(84,653)	18,957	(105,374)
Net Position - December 31, 2014	4,932,345	5,562,907	89,820	10,585,072
Change in Accounting Principle (Note 11)	21,831	23,075	-	44,906
Net Position - December 31, 2014, as Restated	4,954,176	5,585,982	89,820	10,629,978
Net Position - December 31, 2015	\$ 4,914,498	\$ 5,501,329	\$ 108,777	\$ 10,524,604

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

CITY OF CUSTER

**STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2015**

	Water Fund	Sewer Fund	Solid Waste Fund	Total Proprietary Funds
Cash Flows from Operating Activities:				
Receipts from Customers	\$ 653,500	\$ 550,865	\$ 189,302	\$ 1,393,667
Payments to Suppliers	(174,673)	(126,953)	(170,256)	(471,882)
Payments to Employees	(206,356)	(215,663)	-	(422,019)
Net Cash Flows Provided by Operating Activities	272,471	208,249	19,046	499,766
Cash Flows from Capital and Related Financing Activities:				
Purchase of Capital Assets	(25,480)	(86,829)	-	(112,309)
Principal Paid on Capital Debt	(70,385)	(34,697)	-	(105,082)
Interest Paid	(92,496)	(27,213)	-	(119,709)
Net Cash Flows Used in Capital and Related Financing Activities	(188,361)	(148,739)	-	(337,100)
Cash Flows Provided by Investing Activities:				
Interest Received	4,600	5,197	151	9,948
Increase in Cash and Investments	88,710	64,707	19,197	172,614
Cash and Investments - December 31, 2014	1,397,987	1,226,509	63,027	2,687,523
Cash and Investments - December 31, 2015	\$ 1,486,697	\$ 1,291,216	\$ 82,224	\$ 2,860,137
Reconciliation of Operating Income to Net Cash Flows Provided by Operating Activities				
Operating Income (Loss)	\$ 48,048	\$ (64,068)	\$ 18,806	\$ 2,786
<i>Adjustments to Reconcile Operating Income (Loss) to Net Cash Flows Provided by Operating Activities:</i>				
Depreciation Expense	215,369	272,871	-	488,240
Change in Assets and Liabilities:				
Change in Receivables	8,792	712	234	9,738
Change in Pension Asset	15,860	16,765	-	32,625
Change in Pension Related Deferred Outflows	(5,993)	(6,333)	-	(12,326)
Change in Accounts Payable	(683)	441	6	(236)
Change in Accrued Wages	762	833	-	1,595
Change in Customer Deposits	2,560	-	-	2,560
Change in Accrued Leave Payable	496	496	-	992
Change in Pension Related Deferred Inflows	(12,740)	(13,468)	-	(26,208)
Net Cash Flows Provided by Operating Activities	\$ 272,471	\$ 208,249	\$ 19,046	\$ 499,766
Noncash Capital and Related Financing Activities				
Capital Assets Contributed	\$ -	\$ 4,100	\$ -	\$ 4,100

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

CITY OF CUSTER

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2015

(1) Summary of Significant Accounting Policies

a. Reporting Entity

The reporting entity of the City of Custer (the City), consists of the primary government (which includes all of the funds, organizations, institutions, agencies, departments, and offices that make up the legal entity, plus those funds for which the primary government has a fiduciary responsibility, even though those fiduciary funds may represent organizations that do not meet the criteria for inclusion in the financial reporting entity); those organizations for which the primary government is financially accountable; and other organizations for which the nature and significance of their relationship with the primary government are such that their exclusion would cause the financial reporting entity's financial statements to be misleading or incomplete.

b. Basis of Presentation

Government-wide Financial Statements:

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

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

Fund Financial Statements:

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

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

CITY OF CUSTER

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2015

(1) Summary of Significant Accounting Policies (Continued)

b. Basis of Presentation (Continued)

Fund Financial Statements (Continued):

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

Governmental Funds:

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

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

Third Penny Sales Tax Fund – A fund allowed by SDCL 10-52-8 to be used for the purpose of land acquisition, architectural fees, construction costs, payments for civic center, auditorium or athletic facility buildings, including the maintenance, staffing and operations of such facilities, and the staffing and operation of the Custer Chamber of Commerce. This fund is a major fund.

Business Improvement District (BID) Fund – A fund allowed by SDCL 9-55 to account for a \$2 per night occupancy fee charged to motel guests. Motel operators determine how the proceeds are to be spent, usually on advertising to promote the city. This fund is a major fund.

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

TIF Debt Service Fund – TIF funds are Tax Increment Financing Districts allowed by SDCL 11-9-24 to account for the proceeds of incremental property taxes, restricted for the payment of principal and interest on debt issued to finance a public improvement. Separate accounts are maintained for TIF District #1, #2, #4, and #5 revenues and expenditures. This fund is a major fund.

Permanent Funds – permanent funds are used to account for assets that are permanently set aside and from which only the income from its investments can be used for its stated legal purpose. The City has the following permanent fund:

Cemetery Perpetual Care Fund – A fund allowed by SDCL 9-31-18 to account for payments received for perpetual care of cemeteries. The payments are permanently set aside and only the income from the investments can be used for the care and maintenance of the cemetery. The Cemetery Perpetual Care Fund is a major fund.

Proprietary Funds:

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

CITY OF CUSTER

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2015**

(1) Summary of Significant Accounting Policies (Continued)

b. Basis of Presentation (Concluded)

Fund Financial Statements (Concluded):

Water Fund – A fund established by SDCL 9-47-1 to account for the operation of the City of Custer’s waterworks systems and related facilities and is financed primarily by user charges. The water fund is a major fund.

Sewer Fund – A fund established by SDCL 9-48-2 to account for the operation of the City of Custer’s sanitary sewer system and related facilities and is financed primarily by user charges. The sewer fund is a major fund.

Solid Waste Fund – A fund established by SDCL 9-32-11 and 34A-6 to account for the City of Custer’s collection and disposal of solid waste and is financed primarily by user charges. The solid waste collection fund is a major fund.

Fiduciary Funds:

Fiduciary fund types are used to account for assets held by a governmental unit in a trustee capacity or as an agent for individuals, private organizations, or other governmental units. Fiduciary funds are never considered major funds. The City has no fiduciary funds.

c. Measurement Focus and Basis of Accounting

Measurement focus is a term used to describe how transactions are recorded within the various financial statements. Basis of accounting refers to when revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements, regardless of the measurement focus.

Measurement Focus:

Government-wide Financial Statements:

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

Fund Financial Statements:

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

CITY OF CUSTER

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2015

(1) Summary of Significant Accounting Policies (Continued)

c. Measurement Focus and Basis of Accounting (Continued)

Basis of Accounting:

Government-wide Financial Statements:

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

Fund Financial Statements:

All governmental funds are accounted for using the modified-accrual basis of accounting. Their revenues, including property taxes, are recognized when they become measurable and available. Available means resources are collected or to be collected soon enough after the end of the fiscal year that they can be used to pay the bills of the current period. The accrual period does not exceed one bill-paying cycle, and for the City, the length of that cycle is 30 days. The revenues which are accrued at December 31, 2015, are property and sales tax.

d. Cash and Cash Equivalents

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

e. Capital Assets

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

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

Government-wide Financial Statements:

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

CITY OF CUSTER

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2015**

(1) Summary of Significant Accounting Policies (Continued)

e. Capital Assets (Continued)

Government-wide Financial Statements (Continued):

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

Construction-period interest for capital assets used in governmental activities is not capitalized in accordance with USGAAP; however, construction period interest for capital assets used in business-type activities/proprietary fund's operations, is capitalized in accordance with USGAAP. There was no capitalized interest for the year ended December 31, 2015.

Depreciation of all exhaustible capital assets is recorded as an allocated expense in the government-wide Statement of Activities, with net capital assets reflected in the Statement of Net Position. Accumulated depreciation is reported on the government-wide Statement of Net Position and on each proprietary fund's Statement of Net Position.

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

	<u>Capitalization Threshold</u>	<u>Depreciation Method</u>	<u>Estimated Useful Life</u>
Land	\$ -0-	----N/A----	----N/A----
Improvements Other Than Buildings	\$ 5,000	Straight-line	15-100 years
Buildings	\$ 5,000	Straight-line	33-50 years
Machinery and Equipment	\$ 5,000	Straight-line	5-25 years

Land is an inexhaustible capital asset and is not depreciated.

Fund Financial Statements:

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

f. Long-Term Liabilities

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

All long-term liabilities to be repaid from governmental and business-type resources are reported as liabilities in the government-wide statements. The long-term liabilities primarily consist of TIF obligations, water and sewer revenue bonds, and compensated absences.

CITY OF CUSTER

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2015

(1) Summary of Significant Accounting Policies (Continued)

f. Long-Term Liabilities (Continued)

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

g. Program Revenues

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

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

h. Proprietary Funds Revenue and Expense Classifications

In the proprietary fund's Statement of Activities, revenues and expenses are classified in a manner consistent with how they are classified in the Statement of Cash Flows. That is, transactions for which related cash flows are reported as capital and related financing activities, non-capital financing activities, or investing activities are not reported as components of operating revenues or expenses.

i. Equity Classifications

Government-wide Financial Statements:

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

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

CITY OF CUSTER

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2015

(1) Summary of Significant Accounting Policies (Concluded)

i. Equity Classifications (Continued)

Fund Financial Statements:

The City classifies governmental fund balance as follows:

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

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

Committed – includes fund balance amounts that are constrained for specific purposes that are internally imposed by the government through formal action of the highest level of decision making authority and does not lapse at year-end. The City has one committed fund balance for the year ended December 31, 2015. The General Fund created a Capital Reserve Replacement by the City Council passing Ordinance #722. The commitment was established to set funds aside for future capital asset replacements exceeding a cost of \$30,000, up to a maximum commitment of \$250,000. The City Council is the highest decision-making authority and would have to pass an ordinance to remove the commitment.

Assigned – includes fund balance amounts that are intended to be used for specific purposes that are neither considered restricted or committed. Fund balance may be assigned by the City Council, Mayor, or Finance Officer. The Subsequent Year's Budget assignment was established by the City Council when it passed the 2015 Appropriations Ordinance for the City's 2015 budget. The Hospital Sales Tax Subsidy was established by the City Council when it passed Resolution #02-01-16A.

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.

With regard to the City's governmental funds, the City uses restricted amounts first when both restricted and unrestricted fund balances are available unless there are legal documents/contracts that prohibit doing this, such as a grant agreement requiring dollar-for-dollar spending. Additionally, the City would first use committed, then assigned, and lastly unassigned amounts of unrestricted fund balance when expenditures are made. The City does not have a formal minimum fund balance policy.

Proprietary fund equity is classified the same as in the government-wide financial statements. With regard to the City's proprietary funds, it is the City's policy to first use restricted net position, prior to the use of unrestricted net position, when an expense is incurred for purposes for which both restricted and unrestricted net position are available.

j. Compensated Absences

Eligible employees earn sick leave after six years of employment, and will be paid a maximum of 240 hours upon termination. Eligible employees can earn vacation leave based on years of service, and will be paid upon termination, up to a maximum of 240 hours.

k. Accounts Receivable

Included in utility accounts receivable at December 31, 2015, are unbilled accounts receivable totaling approximately \$39,000, \$36,000, and \$16,000 for the water, wastewater, and solid waste funds, respectively.

CITY OF CUSTER

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2015**

(2) Deposits and Investments

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

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

Investments – In General, SDCL 4-5-6 permits City funds to be invested in (a) securities of the United States and securities guaranteed by the United States government either directly or indirectly including, without limitation, United States treasury bills, notes, bonds, and other obligations issued or directly or indirectly guaranteed by the United States government, or otherwise directly or indirectly backed by the full faith and credit of the United States government; provided that, for other than permanent, trust, retirement, building, and depreciation reserve funds, such securities shall either mature within eighteen months from the date of purchase or be redeemable at the option of the holder within eighteen months from the date of purchase; or (b) repurchase agreements fully collateralized by securities described in (a) and meeting the requirements of § 4-5-9, if the repurchase agreements are entered into only with those primary reporting dealers that report to the Federal Reserve Bank of New York and with the one hundred largest United States commercial banks, as measured by domestic deposits; or (c) in shares of an open-end, no-load fund administered by an investment company registered under the Federal Investment Company Act of 1940, whose shares are registered under the Federal Securities Act of 1933 and whose only investments are in securities described in (a) and repurchase agreements described in (b).

Also, SDCL 4-5-9 requires investments to be in the physical custody of the City or deposited with any bank or trust account designated by the City as its fiscal agent.

As of December 31, 2015, the City had the following investments:

Investment	Credit Rating	Maturity	Fair Value
Money Market	Unrated	N/A	\$ 271,687
U.S. Government Securities			
US Treasury Strips - 0%	AAA	3-6 years	817,357
US Treasury Notes - 0.75% - 1.375%	AAA	2-6 years	174,156
External Investment Pools:			
SDFIT	Unrated	N/A	177,191
			1,440,391
Nonnegotiable Certificates of Deposit			2,182,383
Total Investments			\$ 3,622,774

The South Dakota Public Fund Investment Trust (SDFIT) is an external investment pool created for South Dakota local government investing. It is regulated by a nine-member board with representation from municipalities, school districts, and counties. The net asset value of the SDFIT money market account (GCR) is kept at one dollar per share by adjusting the rate of return on a daily basis. Earnings are credited to each account on a monthly basis.

CITY OF CUSTER

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2015**

(2) Deposits and Investments (Continued)

Interest Rate Risk:

The City will minimize interest rate risk, which is the risk that the market value of securities in the portfolio will fall due to changes in market interest rates, by structuring the portfolio to meet the cash requirements of ongoing operations, thereby mitigating the need to liquidate securities at a loss prior to maturity.

Credit Risk:

State law limits eligible investments for the City, as discussed above. The City has no investment policy that would further limit its investment choices.

Custodial Credit Risk:

The risk that, in the event of a depository failure, the City’s deposits may not be returned to it. The City has a policy to follow state law depository requirements. As of December 31, 2015, none of the City’s deposits were exposed to custodial credit risk. The bank balances at December 31, 2015 are as follows, excluding SDFIT, described below:

	<u>Bank Balance</u>
Insured - FDIC	\$ 1,067,294
Uninsured, collateralized in accordance with SDCL 4-6A-3	3,938,585
Total Deposits	\$ 5,005,879

Concentration of Credit Risk

The City does not allow more than 75 percent be invested in any one issuer. Additionally, investment maturities will be staggered in such a manner that all investments will not come due at the same time. Unless matched with specific cash flow, the City will not directly invest in securities maturing more than eight years from the date of purchase. The City only has cash, certificates of deposit, money market funds, and government securities.

State law allows income from deposits and investments to be credited to either the General Fund or the fund making the investment. The City’s policy is to credit all income from investments to the fund making the investment, except for the Cemetery Perpetual Care Fund income, which is credited to the General Fund as required by SDCL 9-32-18.

(3) Restricted Investments

Assets restricted to use for a specific purpose through segregation of balances in separate accounts are as follows:

<u>Amount</u>	<u>Purpose:</u>
\$106,920	Water Fund Debt Service, by debt covenants (Note 7)

(4) Deferred Inflows and Outflows of Resources

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

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

CITY OF CUSTER

NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2015

(5) Property Taxes

Property taxes attach as an enforceable lien on property as of January 1 of each year. Taxes are levied on or before October 1 and payable in two installments before April 30 and October 31 of the following year. The county bills and collects the taxes and remits them to the City. The City is permitted by several state statutes to levy varying amounts of taxes per \$1,000 of taxable valuation on taxable real property in the City.

(6) Changes in Capital Assets

A summary of changes in capital assets for the year ending December 31, 2015 is as follows:

<i>Governmental Activities:</i>	Balance 12/31/2014	Additions	Transfers/ Deletions	Balance 12/31/2015
Capital Assets, not being Depreciated:				
Land	\$ 1,070,706	\$ -	\$ -	\$ 1,070,706
Construction Work in Progress	227,868	264,029	(111,850)	380,047
Total Capital Assets, not being Depreciated	1,298,574	264,029	(111,850)	1,450,753
Capital Assets, being Depreciated:				
Buildings	1,966,625	11,925	-	1,978,550
Improvements Other Than Buildings	8,271,135	589,021	(29,030)	8,831,126
Machinery and Equipment	1,334,152	85,997	-	1,420,149
Total Capital Assets, being Depreciated	11,571,912	686,943	(29,030)	12,229,825
Less Accumulated Depreciation for:				
Buildings	494,125	37,335	-	531,460
Improvements Other Than Buildings	2,037,752	423,748	(29,030)	2,432,470
Machinery and Equipment	921,181	80,578	-	1,001,759
Total Accumulated Depreciation	3,453,058	541,661	(29,030)	3,965,689
Total Governmental Activities Capital Assets, being Depreciated, Net	8,118,854	145,282	-	8,264,136
Total Governmental Capital Assets, Net	\$ 9,417,428	\$ 409,311	\$ (111,850)	\$ 9,714,889

Depreciation expense was charged to functions as follows:

Public Works	\$ 396,378
Culture and Recreation	87,451
General Government	57,832
Total Depreciation Expense - Governmental	\$ 541,661

As of December 31, 2015, there are approximately \$259,000 of commitments associated with construction projects in progress. Completion of such projects will be funded through cash reserves.

CITY OF CUSTER

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2015**

(6) Changes in Capital Assets (Continued)

	Balance 12/31/2014	Additions	Transfers	Balance 12/31/2015
<i>Business-Type Activities:</i>				
Capital Assets, not being Depreciated:				
Land	\$ 568,035	\$ -	\$ -	\$ 568,035
Construction Work in Progress	-	19,018	-	19,018
Total Capital Assets, not being Depreciated	568,035	19,018	-	587,053
Capital Assets, being Depreciated:				
Buildings	1,473,024	-	-	1,473,024
Improvements Other Than Buildings	14,139,235	46,429	-	14,185,664
Machinery and Equipment	1,406,966	50,962	-	1,457,928
Total Capital Assets, being Depreciated	17,019,225	97,391	-	17,116,616
Less Accumulated Depreciation for:				
Buildings	830,353	29,373	-	859,726
Improvements Other Than Buildings	4,759,802	327,587	-	5,087,389
Machinery and Equipment	921,029	131,280	-	1,052,309
Total Accumulated Depreciation	6,511,184	488,240	-	6,999,424
Total Business-Type Activities Capital Assets, being Depreciated, Net				
	10,508,041	(390,849)	-	10,117,192
Total Business-Type Capital Assets, Net	\$ 11,076,076	\$ (371,831)	\$ -	\$ 10,704,245

Depreciation expense was charged to functions as follows:

Sewer	\$ 272,871
Water	215,369
Total Depreciation Expense - Business-Type	\$ 488,240

CITY OF CUSTER

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2015**

(7) Long-Term Debt

The following is a summary of the long-term debt activity for the year ending December 31, 2015:

	Balance 12/31/2014	Earned/ Borrowings	Used/ Repayments	Balance 12/31/2015	Due Within One Year
Primary Government:					
Governmental Activities:					
TIF #1 - Boothill	\$ 665,465	\$ -	\$ -	\$ 665,465	\$ -
Accrued Interest - TIF #1	51,869	39,927	57,831	33,965	54,854
TIF #2 - Stonehill	1,569,901	-	-	1,569,901	-
Accrued Interest - TIF #2	594,895	141,290	55,659	680,526	65,980
TIF #4 - Downtown (2011 Bonds)	1,025,699	-	57,258	968,441	65,659
TIF #5 - Pamida	291,913	-	18,676	273,237	12,435
Compensated Absences	43,712	38,052	42,420	39,344	39,344
Total Governmental Activities	4,243,454	219,269	231,844	4,230,879	238,272
Business-Type Activities:					
2003 SRF Water Revenue Bond	436,050	-	41,069	394,981	42,530
2007 USDA Water Revenue Bond	1,894,686	-	29,316	1,865,370	30,253
2012 SRF Sewer Revenue Bond	920,027	-	34,697	885,330	35,748
Compensated Absences	59,848	37,350	36,358	60,840	60,840
	3,310,611	37,350	141,440	3,206,521	169,371
Total Primary Government	\$ 7,554,065	\$ 256,619	\$ 373,284	\$ 7,437,400	\$ 407,643

Tax Increment Financing Obligations

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

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

During the year ended December 31, 2015, property tax revenues were \$61,817, \$53,949, \$110,439, and \$39,106 for TIFs #1, #2, #4, and #5, respectively. Interest expenditures, excluding corresponding accruals, related to TIF obligations totaled \$187,102 for the year ended December 31, 2015.

Business-type Activities

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

CITY OF CUSTER

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2015**

(7) Long-Term Debt (Continued)

Business-type Activities (Continued)

Below is a comparison by fund of principal and interest payments and total pledged revenue for the current year.

	<u>Water Fund</u>	<u>Sewer Fund</u>
Current Year Principal and Interest	\$ 162,756	\$ 64,584
Pledged Revenue	642,148	550,153

Long-term debt at December 31, 2015, is comprised of the following:

Revenue Bonds

Series 2003 SRF Water Revenue Bonds, matures in February 2024, interest at 3.00 percent, due in monthly installments of \$4,640. Financed through the Water Fund. \$ 394,981

2007 USDA Water Loan, matures in January 2047, interest at 4.13 percent, due in monthly installments of \$8,910. Financed through the Water Fund. 1,865,370

Series 2012 SRF Sewer Revenue Bonds, matures in July 2034, interest at 3.00 percent, due in quarterly installments of \$15,477. Financed through the Sewer Fund. 885,330

Total Revenue Bonds 3,145,681

Tax Increment Financing Obligations

TIF #1, including interest at 6.00 percent, due in varying semi-annual installments of incremental property taxes collected through 2018. Partial interest payments only were paid in 2015. Financed through the TIF Debt Service Fund. 665,465

TIF #2, including interest at 9.00 percent, due in varying installments within 30 days of property tax collection from the county through 2023. Partial interest payments only were paid in 2015. Financed through the TIF Debt Service Fund. 1,569,901

TIF #4, Series 2011, including variable interest at not less than 4.50 percent, and not to exceed 7.00 percent, due in semi-annual installments of \$56,903 through 2027. Financed through the TIF Debt Service Fund. 968,441

TIF #5, including interest at 7.00 percent, due in varying semi-annual installments of incremental property taxes collected through 2021. Financed through the TIF Debt Service Fund. 273,237

Total Tax Increment Financing Obligations 3,477,044

Compensated Absences

General Fund 39,344

Water Fund 30,420

Sewer Fund 30,420

Total Compensated Absences 100,184

Accrued Interest (TIFs #1 and #2) 714,491

Total Long-Term Debt \$ 7,437,400

CITY OF CUSTER

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2015**

(7) Long-Term Debt (Concluded)

The annual requirements to amortize long-term debt outstanding as of December 31, 2015, except for compensated absences and accrued interest on TIFs #1 and #2, are as follows:

	(a)					
	Revenue Bonds		TIF Obligations		Total	
	Interest	Principal	Interest	Principal	Interest	Principal
2016	\$ 115,982	\$ 108,531	\$ 185,972	\$ 78,094	\$ 301,954	\$ 186,625
2017	112,112	112,401	181,355	82,710	293,467	195,111
2018	108,101	116,412	163,996	748,010	272,097	864,422
2019	103,945	120,569	119,902	89,309	223,847	209,878
2020	99,637	124,876	115,265	93,946	214,902	218,822
2021-2025	431,087	589,406	1,866,732	2,245,577	2,297,819	2,834,983
2026-2030	339,598	504,587	8,136	139,398	347,734	643,985
2031-2035	242,600	524,199	-	-	242,600	524,199
2036-2040	159,327	375,316	-	-	159,327	375,316
2041-2045	73,405	461,238	-	-	73,405	461,238
2046-2047	2,743	108,146	-	-	2,743	108,146
Total	\$ 1,788,537	\$ 3,145,681	\$ 2,641,358	\$ 3,477,044	\$ 4,429,895	\$ 6,622,725

(a) TIF Obligation maturities are based on projected future property tax increments. Actual repayments will vary dependent on property tax increments received.

The City has bond reserves of \$106,920 at December 31, 2015, in accordance with debt covenants on the 2007 USDA Water Revenue bonds. Additionally, the 2012 SRF Sewer Revenue bonds have a covenant requiring the City to keep net sewer revenue available for debt service at 110 percent of debt service expenses each year. The City is out of compliance with such covenant at December 31, 2015, but has received correspondence from South Dakota Department of Environmental Resources that the debt will not be called, and thus does not need presented as a current obligation.

(8) Pension Plan

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

Benefits Provided:

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

CITY OF CUSTER

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2015**

(8) Pension Plan (Continued)

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

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

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

Contributions:

Per SDCL 3-12, contribution requirements of the active employees and the participating employers are established and may be amended by the SDRS Board. Covered employees are required by state statute to contribute the following percentages of their salary to the plan; Class A Members, 6.0 percent of salary; Class B Judicial Members, 9.0 percent of salary; and Class B Public Safety Members, 8.0 percent of salary. State statute also requires the employer to contribute an amount equal to the employee’s contribution. State statute also requires the employer to make an additional contribution in the amount of 6.2 percent for any compensation exceeding the maximum taxable amount for social security for general employees only. The City’s share of contributions to the SDRS for the fiscal years ended December 31, 2015, 2014, and 2013 were **\$38,488**, \$37,180, and \$37,436, respectively, equal to the required contributions each year.

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

At June 30, 2015, SDRS is 104.1 percent funded and accordingly has a net pension asset. The proportionate shares of the components of the net pension asset of South Dakota Retirement System, for the City as of June 30, 2015 are as follows:

	Governmental Activities	Business-Type Activities	Total
Proportionate Share of Net Position Restricted for Pension Benefits	\$ 2,680,982	\$ 927,001	\$ 3,607,983
Less: Proportionate Share of Total Pension Liability	(2,575,468)	(890,517)	(3,465,985)
Proportionate Share of Net Pension Asset	\$ 105,514	\$ 36,484	\$ 141,998

At December 31, 2015, the City reported an asset of \$141,998 for its proportionate share of the net pension asset. The net pension asset was measured as of June 30, 2015 and the total pension asset used to calculate the net pension asset was based on a projection of the City’s share of contributions to the pension plan relative to the contributions of all participating entities. At June 30, 2015, the City’s proportion was .03348000 percent, which is a decrease of .003 percent from its proportion measured as of June 30, 2014.

**CITY OF CUSTER
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2015**

(8) Pension Plan (Continued)

For the year ended December 31, 2015, the City recognized pension expense of \$15,498. At December 31, 2015, the City reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between Expected and Actual Experience	\$ 29,075	\$ -
Changes in Assumption	112,596	-
Net Difference between Projected and Actual Earnings on Pension Plan Investments	86,744	209,521
Changes in Proportion and Difference between City Contributions and Proportionate Share of Contributions	17,521	-
City Contributions Subsequent to the Measurement Date	19,360	-
Total	\$ 265,296	\$ 209,521

Deferred outflow of resources includes \$19,360 resulting from City contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ending December 31, 2016. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense (revenue) as follows:

2016	\$ 24,250
2017	6,729
2018	(18,102)
2019	23,538
	\$ 36,415

Actuarial Assumptions:

The total pension asset in the June 30, 2015 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3.25 percent
Salary Increases	5.83 percent at entry to 3.87 percent after 30 years of service
Investment Rate of Return	7.25 percent through 2016 and 7.50 percent thereafter, net of pension plan investment expense

Mortality rates were based on the RP-2000 Employee Mortality Table for males and females, as appropriate.

The actuarial assumptions used in the June 30, 2015 valuation were based on the results of an actuarial experience study for the period July 1, 2005 through June 30, 2011. The mortality assumptions were revised based on an extension of the experience study including mortality experience through June 30, 2013.

**CITY OF CUSTER
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2015**

(8) Pension Plan (Concluded)

Actuarial Assumptions (Continued):

Investment portfolio management is the statutory responsibility of the South Dakota Investment Council (SDIC), which may utilize the services of external money managers for management of a portion of the portfolio. SDIC is governed by the Prudent Man Rule (i.e., the council should use the same degree of care as a prudent man). Current SDIC investment policies dictate limits on the percentage of assets invested in various types of vehicles (equities, fixed income securities, real estate, cash, private equity, etc.). The long-term expected rate of return on pension plan investments was determined using a method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighing the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. Best estimates of real rates of return for each major asset class included in the pension plan's target asset allocation as of June 30, 2015 (see the discussion of the pension plan's investment policy) are summarized in the following table using geometric means:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
Global Equity	61.0%	4.5%
Fixed Income	27.0%	1.8%
Real Estate	10.0%	5.2%
Cash	2.0%	0.8%
	100.0%	

Discount Rate:

The discount rate used to measure the total pension asset was 7.25 percent through 2016 and 7.50 percent thereafter. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the current contribution rate and that matching employer contributions will be made at rates equal to the member rate. Based on these assumptions, the pension plan's fiduciary net position was projected to be available to make all future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension asset.

Sensitivity of Asset to Changes in the Discount Rate:

The following presents the City's proportionate share of net pension asset calculated using the discount rate of 7.25 percent through 2016 and 7.50 percent thereafter, as well as what the District's proportionate share of the net pension asset would be if it were calculated using a discount rate that is 1-percentage point lower (6.25/6.50 percent) or 1-percentage point higher (8.25/8.50 percent) than the current rate:

	1% Decrease	Current Discount Rate	1% Increase
City's Proportionate Share of the Net Pension Asset	\$ (357,408)	\$ 141,998	\$ 549,221

Pension Plan Fiduciary Net Position:

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

**CITY OF CUSTER
NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2015**

(9) Risk Management

The City is exposed to various risks of loss related to torts; theft; damage or destruction of assets; errors or omissions; injuries to employees; and natural disasters. During the year ending December 31, 2015, the City managed its risks as follows:

Employee Health Insurance:

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

Liability Insurance:

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

The agreement with the SDPAA provides that the above coverages will be provided to a \$2,000,000 limit. Member premiums are used by the pool for payment of claims and to pay for reinsurance for claims in excess of \$250,000 for property coverage and \$500,000 for liability coverage to the upper limit. A portion of the member premiums are also allocated to a cumulative reserve fund. The City would be eligible to receive a refund for a percentage of the amount allocated to the cumulative reserve fund on the following basis:

End of City's First Full Year	50%
End of City's Second Full Year	60%
End of City's Third Full Year	70%
End of City's Fourth Full Year	80%
End of City's Fifth Full Year	90%
End of City's Sixth Full Year and Thereafter	100%

As of December 31, 2015, the City has a vested balance in the cumulative reserve fund of \$26,385.

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

**CITY OF CUSTER
NOTES TO THE FINANCIAL STATEMENTS (CONCLUDED)
DECEMBER 31, 2015**

(9) Risk Management (Continued)

Worker's Compensation:

The City joined the South Dakota Municipal League Worker's Compensation Fund (the Fund), a public entity risk pool currently operating as a common risk management and insurance program for South Dakota local government entities. The objective of the Fund is to formulate, develop, and administer, on behalf of member organizations, a program of worker's compensation coverage, to obtain lower costs for that coverage, and to develop a comprehensive loss control program. The City's responsibility is to initiate and maintain a safety program to give its employees safe and sanitary working conditions and to promptly report to and cooperate with the Fund to resolve any worker's compensation claims. The City pays an annual premium to the pool to provide worker's compensation coverage for its employees, under a self-funded program, and the premiums are accrued based on the ultimate cost of the experience to date of the Fund members. Coverage limits are set by state statute. The pool pays the first \$650,000 of any claim per individual. The pool has reinsurance which covers up to statutory limits in addition to a separate combined employer liability of \$2,000,000 per incident.

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

Unemployment Benefits:

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

(10) Emerging Accounting Standard

In February 2015, the Governmental Accounting Standards Board (GASB) issued Statement No. 72, *Fair Value Measurement and Application*. This statement provides guidance for determining a fair value measurement according to a three level hierarchy for financial reporting purposes. This statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value investments. Management has not yet determined the impact of this statement on the financial statements. This statement is effective for the City's year ending December 31, 2016.

(11) Change in Accounting Principle

In 2015, the City implemented GASB Statement No. 68, *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27*, and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – An Amendment of GASB Statement No. 68*. As a result, beginning net position has been restated to reflect the related net pension asset totaling \$268,978, deferred outflows of resources totaling \$217,326, and deferred inflows of resources totaling (\$311,521) at December 31, 2014. The result was an increase of net position of \$174,783 at December 31, 2014. See Note 8.

REQUIRED SUPPLEMENTARY INFORMATION

CITY OF CUSTER

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND - BUDGETARY BASIS
FOR THE YEAR ENDED DECEMBER 31, 2015**

Revenue	Original Budget	Final Budget	Actual - Budgetary Basis	Variance
<i>Taxes:</i>				
311 General Property Taxes	\$ 833,026	\$ 833,026	\$ 835,145	\$ 2,119
313 General Sales and Use Taxes	1,387,561	1,387,561	1,530,024	142,463
315 Amusement Taxes	500	500	480	(20)
319 Penalties and Interest on Delinquent Taxes	4,500	4,500	1,861	(2,639)
320 Licenses and Permits	42,900	42,900	74,325	31,425
<i>Intergovernmental Revenue:</i>				
<i>State Shared Revenue:</i>				
335.01 Bank Franchise Tax	2,000	2,000	2,567	567
335.02 Motor Vehicle Commercial Prorate	5,000	5,000	-	(5,000)
335.03 Liquor Tax Reversion	12,000	12,000	12,893	893
335.04 Motor Vehicle Licenses (5%)	25,000	25,000	34,299	9,299
335.08 Local Government Highway and Bridge Fund	29,000	29,000	33,291	4,291
<i>County Shared Revenue:</i>				
338.02 County HBR Tax	26,000	26,000	28,097	2,097
<i>Charges for Goods and Services:</i>				
341 General Government	7,200	7,200	9,101	1,901
346 Culture and Recreation	13,000	13,000	14,230	1,230
348 Cemeteries	3,000	3,000	2,000	(1,000)
350 Fines and Forfeits	500	500	740	240
352 Animal Control Fines	1,100	1,100	-	(1,100)
<i>Miscellaneous Revenue:</i>				
361 Earnings on Deposits and Investments	6,000	6,000	10,578	4,578
362 Rentals	4,870	4,870	5,320	450
368 Liquor Operating Agreement Income	182,000	182,000	204,194	22,194
369 Other	17,000	17,000	7,772	(9,228)
Total Revenue	2,602,157	2,602,157	2,806,917	204,760

CITY OF CUSTER

BUDGETARY COMPARISON SCHEDULE (CONTINUED)

GENERAL FUND - BUDGETARY BASIS

FOR THE YEAR ENDED DECEMBER 31, 2015

	Original Budget	Final Budget	Actual - Budgetary Basis	Variance
Expenditures				
<i>General Government:</i>				
411 Legislative	124,840	124,840	83,298	41,542
413 Elections	1,175	1,175	650	525
414 Financial Administration	137,570	151,570	148,612	2,958
419 Other	357,600	477,600	400,437	77,163
<i>Public Safety:</i>				
421 Police	610,322	435,322	405,181	30,141
<i>Public Works:</i>				
431 Highways and Streets	942,845	1,132,845	1,052,796	80,049
437 Cemeteries	27,650	27,650	25,291	2,359
<i>Health and Welfare:</i>				
444 Humane Society	10,330	11,330	10,602	728
447 Hospitals, Nursing Homes, and Rest Homes	347,000	347,000	-	347,000
<i>Culture and Recreation:</i>				
451 Custer Cruisin'	13,000	13,000	10,266	2,734
451 Swimming	62,500	94,500	80,096	14,404
452 Parks	192,295	172,295	152,745	19,550
<i>Conservation and Development:</i>				
465 Economic Development and Assistance	94,500	97,500	97,500	-
Total Expenditures	2,921,627	3,086,627	2,467,474	619,153
Net Change in Fund Balance	(319,470)	(484,470)	339,443	823,913
Fund Balance - December 31, 2014	3,213,440	3,213,440	3,213,440	-
Fund Balance - December 31, 2015	\$ 2,893,970	\$ 2,728,970	\$ 3,552,883	\$ 823,913

The accompanying notes to required supplementary information are an integral part of this statement.

CITY OF CUSTER

**BUDGETARY COMPARISON SCHEDULE
THIRD PENNY (PROMOTION) FUND - BUDGETARY BASIS
FOR THE YEAR ENDED DECEMBER 31, 2015**

	Original Budget	Final Budget	Actual - Budgetary Basis	Variance
Revenue				
<i>Taxes:</i>				
313 General Sales and Use Taxes	\$ 200,000	\$ 220,000	\$ 239,707	\$ 19,707
<i>Miscellaneous Revenue:</i>				
361 Investment Earnings	200	200	133	(67)
Total Revenue	200,200	220,200	239,840	19,640
Expenditures				
<i>Conservation and Development:</i>				
465 Economic Development and Assistance	200,200	220,200	197,898	22,302
Net Change in Fund Balance	-	-	41,942	41,942
Fund Balance - December 31, 2014	50,505	50,505	50,505	-
Fund Balance - December 31, 2015	\$ 50,505	\$ 50,505	\$ 92,447	\$ 41,942

The accompanying notes to required supplementary information are an integral part of this statement.

CITY OF CUSTER

**BUDGETARY COMPARISON SCHEDULE
 BID DISTRICT FUND - BUDGETARY BASIS
 FOR THE YEAR ENDED DECEMBER 31, 2015**

	Original Budget	Final Budget	Actual - Budgetary Basis	Variance
Revenue				
<i>Taxes:</i>				
313 General Sales and Use Taxes	\$ 140,000	\$ 140,000	\$ 160,222	\$ 20,222
Expenditures				
<i>Conservation and Development:</i>				
465 Economic Development and Assistance	140,000	185,000	181,913	3,087
Net Change in Fund Balance	-	(45,000)	(21,691)	23,309
Fund Balance - December 31, 2014	74,532	74,532	74,532	-
Fund Balance - December 31, 2015	\$ 74,532	\$ 29,532	\$ 52,841	\$ 23,309

The accompanying notes to required supplementary information are an integral part of this statement.

CITY OF CUSTER

**SCHEDULE OF THE CITY'S PROPORTIONATE SHARE OF THE NET PENSION ASSET
DECEMBER 31, 2015**

	<u>2015</u>
City's Proportion of the Net Pension Asset	0.03348000%
City's Proportionate Share of Net Pension	\$ 141,998
City's Covered-Employee Payroll	\$ 635,252
City's Proportionate Share of the Net Pension Asset as a Percentage of its Covered-Employee Payroll	22.35%
Plan Fiduciary Net Position as a Percentage of the Total Pension Asset	104.10%

CITY OF CUSTER

**SCHEDULE OF THE CITY CONTRIBUTIONS
DECEMBER 31, 2015**

	<u>2015</u>
Contractually Required Contribution	\$ 38,488
Contributions in Relation to the Contractually Required Contribution	<u>38,488</u>
Contribution Deficiency (Excess)	<u>\$ -</u>
City's Covered-Employee Payroll	\$ 641,477
Contributions as a Percentage of Covered- Employee Payroll	6.0%

CITY OF CUSTER

**NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
DECEMBER 31, 2015**

(1) Budgets and Budgetary Accounting

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

1. At the first regular board meeting in September of each year or within ten days thereafter, the governing board introduces the annual appropriation ordinance for the ensuing fiscal year.
2. After adoption by the governing board, the operating budget is legally binding and actual disbursements for each purpose cannot exceed the amounts budgeted, except as indicated in item number four.
3. A line item for contingencies may be included in the annual budget. Such a line item may not exceed five percent of the total municipal budget and may be transferred by resolution of the governing board to any other budget category that is deemed insufficient during the year.
4. If it is determined during the year that sufficient amounts have not been budgeted, state statute allows the adoption of supplemental budgets.
5. Unexpended appropriations lapse at year-end unless encumbered by resolution of the governing board.
6. The City did not encumber any amounts at December 31, 2015.
7. Formal budgetary integration is employed as a management control device during the year for the general fund and major special revenue funds.
8. Budgets for the general fund and major special revenue funds are adopted on a basis consistent with the modified-cash basis of accounting, except for the following:

The financial statements prepared in conformity with USGAAP present capital outlay expenditure information in a separate category of expenditures. Under the budgetary basis of accounting, capital outlay expenditures are reported within the function to which they relate. For example, the purchase of a new vehicle would be reported as a capital outlay expenditure on the Governmental Funds Statement of Revenues, Expenditures and Changes in Fund Balances; however, in the Budgetary RSI Schedule, the purchase of that vehicle would be reported as an expenditure of the Public Safety function of government, along with all other current Public Safety related expenditures.

OTHER REPORTS



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

City Council
City of Custer
Custer, South Dakota

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, and each major fund of City of Custer (the City) as of and for the year ended December 31, 2015 and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated May 2, 2016.

Internal Control over Financial Reporting

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

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying Schedule of Findings, we identified certain deficiencies in internal control that we consider to be material weaknesses and a significant deficiency.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the City's financial statements will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings as #2015-001 and #2015-002 to be material weaknesses.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying Schedule of Findings as #2015-003 to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed one instance of noncompliance or other matter that is required to be reported under *Government Auditing Standards* and which is described in the accompanying Schedule of Findings, as #2015-003.

City Council

City's Response to Findings

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

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the City's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. However, as required by South Dakota Codified Law 4-11-11, this report is a matter of public record and its distribution is not limited.



KETEL THORSTENSON, LLP
Certified Public Accountants

May 2, 2016

CITY OF CUSTER

**SCHEDULE OF FINDINGS
DECEMBER 31, 2015**

A. Status of Prior Audit Findings and Recommendations

The City has accepted the risk associated with Finding #2014-001 regarding the preparation of the financial statements. The finding, originally issued years ago, is repeated Finding #2015-001 below.

The City properly recorded the property tax receivable/deferred inflow activity in the current year. Thus, Finding #2014-002 will not be repeated for this particular audit adjustment.

B. Current Year Audit Findings and Recommendations

MATERIAL WEAKNESSES

#2015-001 FINDING: Financial Statement Preparation

Condition and Cause: We were requested to draft the audited financial statements and related footnote disclosures as part of our regular audit services. Auditing standards require auditors to communicate this situation to the City Council as an internal control deficiency. Ultimately, it is management's responsibility to provide for the preparation of the City's statements and footnotes, and the responsibility of the auditor to determine the fairness and presentation of those statements. From a practical standpoint, we do both for the City at the same time in connection with our audit. This is not unusual for municipalities of your size.

Criteria and Effect: It is our responsibility to inform the City Council that this deficiency could result in a material misstatement to the financial statements that would not have been prevented or detected by the City's management.

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

Response/Corrective Action Plan: The City has accepted the risk associated with requesting the auditors prepare the financial statements. The Finance Officer, Laurie Woodward, is responsible for the corrective action plan for this finding.

CITY OF CUSTER

**SCHEDULE OF FINDINGS (CONTINUED)
DECEMBER 31, 2015**

B. Current Year Audit Findings and Recommendations (Continued)

MATERIAL WEAKNESSES (CONTINUED)

#2015-002 FINDING: Internal Control over Significant Accounts

Condition and Cause: We were requested to assist with the implementation of GASB 68, *Accounting and Reporting for Pensions*. During the course of our engagement, we also proposed an adjustment to long-term debt, as well as a reclassification entry that had no effect on net position.

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

Recommendation: As in prior years, we have instructed management to review and approve the auditor prepared journal entries in detail for their accuracy. We recommend management record the City's portion of the pension activity per the schedules issued by SDRS, as well as ensuring all debt payments made during the year are properly reflected in the year-end balances.

Response/Corrective Action Plan: The Finance Office, Laurie Woodward, will work towards being more involved with the GASB 68 requirements. She is responsible for the corrective action plan for this finding. The long-term debt adjustment was related to a spreadsheet formula error in the accrued leave at the end of year process. She will make sure to double check those figures in the future. The Finance Officer will make sure to double check those figured from the 2016 end of year process.

SIGNIFICANT DEFICIENCY

#2015-003 FINDING: Compliance with Debt Covenants

Condition and Cause: The City is not in compliance with the debt covenant for the 2012 Sewer Revenue Bonds that require revenues of the sewer fund to be at least 110 percent of debt service requirements.

Criteria and Effect: The City is out of compliance with the requirements of the revenue bond agreements. The bonds could be called as a result of the City's noncompliance. Subsequently, the State did not call the debt.

Recommendation: The City should ensure that it is in compliance with all debt covenants by performing calculations on at least a quarterly basis before changing customer surcharge amounts.

Response/Corrective Action Plan: The City has a reserve amount that has been accumulated for the Sewer SRF Loan, which will remain in place, however the City is currently working through the process to raise the sewer bond charge by \$0.50 to increase the percentage to meet the state's 110% requirement. In 2015 the City was at 103% versus the 110%. At the May 2nd, 2016 Council Meeting the second reading of the ordinance to make this change will take place. If that ordinance passes it will become effective with the June 2016 utility billing. The City Council is responsible for the corrective action plan for this finding.