



Financial Statements  
December 31, 2016  
**City of Hosmer**

City of Hosmer  
Municipal Officials (unaudited)  
December 31, 2016

---

Mayor.....Lew Paulson

Governing Board.....Dale Prezler  
Mike Schwingler  
Dewayne Sowards  
Jerome Malsom  
Dean Schumacher  
Chris Holmes

Finance Officer .....Barb Gienger

Independent Auditor’s Report.....	1
Financial Statements	
Statement of Net Position–Modified Cash Basis .....	3
Statement of Activities–Modified Cash Basis .....	4
Balance Sheet–Modified Cash Basis–Governmental Fund .....	5
Statement of Revenues, Expenditures and Changes in Fund Balance–Modified Cash Basis–Governmental Fund .....	6
Balance Sheet-Modified Cash Basis-Proprietary Funds .....	8
Statement of Revenues, Expenses and Changes in Fund Net Position-Modified Cash Basis-Proprietary Funds ..	9
Statement of Cash Flows-Modified Cash Basis-Proprietary Funds.....	10
Notes to Financial Statements.....	11
Supplementary Information	
Schedule of Changes in Long-Term Debt.....	21
Budgetary Comparison Schedule – General Fund.....	22
Notes to Supplementary Information .....	24
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 <i>Government Auditing Standards</i> .....	25
Independent Auditor’s Report on Compliance for the Major Federal Program; Report on Internal Control Over Compliance; and Report on the Schedule of Expenditures of Federal Awards Required by the Uniform Guidance .....	27
Schedule of Expenditures of Federal Awards.....	30
Schedule of Findings and Questioned Costs.....	31



## Independent Auditor's Report

The Board of Trustees  
City of Hosmer  
Hosmer, South Dakota

### Report on the Financial Statements

We have audited the accompanying modified cash basis financial statements of the governmental activities, the business-type activities and each major fund of the City of Hosmer, as of and for the year ended December 31, 2016, and the notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

### Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the modified cash basis of accounting described in Note 1; this includes determining that the modified cash basis of accounting is an acceptable basis for the preparation of the financial statements in the circumstances. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of the 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 modified cash basis financial statements referred to above present fairly, in all material respects, the respective modified cash basis financial position of the governmental activities, the business-type activities, and each major fund of the City of Hosmer as of December 31, 2016, the respective changes in modified cash basis financial position and, where applicable, cash flows thereof and for the year then ended in accordance with the modified cash basis of accounting described in Note 1.

## **Basis of Accounting**

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

## **Other Matters**

### *Other Information*

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively compromise the City's financial statements. The listing of municipal officers, budgetary comparison schedule, and schedule of changes in long-term debt are presented for purposes of additional analysis and are not a required part of the financial statements.

The schedule of changes in long-term debt and budgetary comparison schedule are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

The listing of municipal officers has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

## **Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated April 3, 2018 on our consideration of the City of Hosmer'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 solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the City of Hosmer's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City of Hosmer's internal control over financial reporting and compliance.



Aberdeen, South Dakota

April 3, 2018

City of Hosmer  
Statement of Net Position—Modified Cash Basis  
December 31, 2016

	Primary Government		
	Governmental Activities	Business-Type Activities	Total
<b>Assets</b>			
Cash and cash equivalents	\$ 550,921	\$ 395,344	\$ 946,265
Investments	18,096	3,000	21,096
Total assets	<u>\$ 569,017</u>	<u>\$ 398,344</u>	<u>\$ 967,361</u>
<b>Net Position</b>			
Restricted for:			
Debt service and short-lived asset replacement	\$ -	\$ 15,450	\$ 15,450
Unrestricted	<u>569,017</u>	<u>382,894</u>	<u>951,911</u>
Total net position	<u>569,017</u>	<u>398,344</u>	<u>967,361</u>
	<u>\$ 569,017</u>	<u>\$ 398,344</u>	<u>\$ 967,361</u>

City of Hosmer  
Statement of Activities—Modified Cash Basis  
Year Ended December 31, 2016

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Position		
		Charges for Services	Operating Grants and Contributions	Capital Grants, Contributions and Loan Proceeds	Primary Government		Total
					Governmental Activities	Business-Type Activities	
<b>Primary Government</b>							
Governmental activities:							
General government	\$ 39,294	\$ 721	\$ 937	\$ -	\$ (37,636)	\$ -	\$ (37,636)
Public works	64,431	4,853	15,445	-	(44,133)	-	(44,133)
Health and welfare	420	-	-	-	(420)	-	(420)
Culture and recreation	707	-	-	-	(707)	-	(707)
Total governmental activities	104,852	5,574	16,382	-	(82,896)	-	(82,896)
Business-type activities:							
Water	52,565	50,928	-	-	-	(1,637)	(1,637)
Sewer	1,817,609	72,601	-	1,764,520	-	19,512	19,512
Liquor	253,423	236,093	-	-	-	(17,330)	(17,330)
Total business-type activities	2,123,597	359,622	-	1,764,520	-	545	545
	<u>\$ 2,228,449</u>	<u>\$ 365,196</u>	<u>\$ 16,382</u>	<u>\$ 1,764,520</u>	<u>(82,896)</u>	<u>545</u>	<u>(82,351)</u>
<b>General Revenues</b>							
Taxes:							
Property taxes					22,887	-	22,887
Sales taxes					52,989	-	52,989
State shared revenues					791	-	791
Unrestricted investment earnings					423	-	423
Miscellaneous revenue					2,856	11,056	13,912
Sale of capital assets					9,698	-	9,698
Total general revenues					89,644	11,056	100,700
Change in Net Position					6,748	11,601	18,349
Net Position - Beginning					562,269	386,743	949,012
Net Position - Ending					<u>\$ 569,017</u>	<u>\$ 398,344</u>	<u>\$ 967,361</u>

City of Hosmer  
Balance Sheet—Modified Cash Basis—Governmental Fund  
December 31, 2016

---

	<u>General Fund</u>
Assets	
Cash and cash equivalents	\$ 550,921
Investments	<u>18,096</u>
	<u>\$ 569,017</u>
Fund Balances	
267 Unassigned	<u>\$ 569,017</u>
	<u>\$ 569,017</u>

City of Hosmer

Statement of Revenues, Expenditures and Changes in Fund Balance—Modified Cash Basis—Governmental Fund  
Year Ended December 31, 2016

---

	General Fund
Revenues	
310 Taxes	
311 General property taxes	\$ 22,785
313 General sales and use taxes	52,989
315 Amusement taxes	48
319 Penalties and interest on delinquent taxes	54
	75,876
Total taxes	75,876
320 Licenses and permits	46
330 Intergovernmental revenue	
331 Federal grants	937
335 State shared revenue	
335.01 Bank franchise tax	791
335.02 Motor vehicle commercial prorate	1,571
335.04 Motor vehicle licenses (5%)	7,586
335.08 Local government highway and bridge fund	4,988
338 County shared revenue	
338.01 County road tax (25%)	308
338.03 County wheel tax	992
	17,173
Total intergovernmental revenue	17,173
340 Charges for goods and services	
344 Sanitation	4,853
	4,853
Total charges for goods and services	4,853
360 Miscellaneous revenue	
361 Investment earnings	423
362 Rentals	675
363 Special assessments	300
369 Other	2,556
	3,954
Total miscellaneous revenue	3,954
Total revenues	101,902

City of Hosmer

Statement of Revenues, Expenditures and Changes in Fund Balances—Modified Cash Basis—Governmental Fund  
Year Ended December 31, 2016

---

	<u>General Fund</u>
Expenditures	
410 General government	
411 Legislative	10,256
414 Financial administration	9,852
419 Other general government	<u>19,186</u>
Total general government	<u>39,294</u>
430 Public works	
431 Highways and streets	20,310
432 Sanitation	<u>1,015</u>
Total public works	<u>21,325</u>
440 Health and welfare:	
441 Health	<u>420</u>
Total health and welfare	<u>420</u>
450 Culture and recreation	
451 Recreation	<u>707</u>
Total culture and recreation	<u>707</u>
485 Capital outlay	<u>43,106</u>
Total expenditures	<u>104,852</u>
Other Financing Sources	
391.03 Sale of municipal property	<u>9,698</u>
Total other financing sources	<u>9,698</u>
Net Change in Fund Balance	6,748
Fund Balance - Beginning	<u>562,269</u>
Fund Balance - Ending	<u><u>\$ 569,017</u></u>

City of Hosmer  
Balance Sheet-Modified Cash Basis-Proprietary Funds  
December 31, 2016

	Enterprise Funds			Totals
	Water Fund	Sewer Fund	Liquor Fund	
Assets				
Current Assets				
Cash and cash equivalents	\$ 84,561	\$ 76,491	\$ 234,292	\$ 395,344
Investments	3,000	-	-	3,000
Total assets	<u>\$ 87,561</u>	<u>\$ 76,491</u>	<u>\$ 234,292</u>	<u>\$ 398,344</u>
Net Position				
253.20 Restricted net position for:				
Debt service and short-lived asset replacement	\$ -	\$ 15,450	\$ -	\$ 15,450
Unrestricted net position	87,561	61,041	234,292	382,894
Total net position	<u>87,561</u>	<u>76,491</u>	<u>234,292</u>	<u>398,344</u>
	<u>\$ 87,561</u>	<u>\$ 76,491</u>	<u>\$ 234,292</u>	<u>\$ 398,344</u>

City of Hosmer

Statement of Revenues, Expenses and Changes in Fund Net Position-Modified Cash Basis-Proprietary Funds  
Year Ended December 31, 2016

	Enterprise Funds			Totals
	Water Fund	Sewer Fund	Liquor Fund	
Operating Revenue				
380 Charges for goods and services	\$ 50,928	\$ 72,601	\$ 236,093	\$ 359,622
369 Miscellaneous	-	373	10,683	11,056
Total operating revenue	<u>50,928</u>	<u>72,974</u>	<u>246,776</u>	<u>370,678</u>
Operating Expenses				
410 Personal services	30,839	29,504	67,178	127,521
420 Other current expense	4,518	4,570	40,255	49,343
426.2 Materials	17,208	658	145,990	163,856
430 Capital assets	-	1,758,237	-	1,758,237
Total operating expenses	<u>52,565</u>	<u>1,792,969</u>	<u>253,423</u>	<u>2,098,957</u>
Operating Loss	<u>(1,637)</u>	<u>(1,719,995)</u>	<u>(6,647)</u>	<u>(1,728,279)</u>
Nonoperating Revenue (Expense)				
331 Federal grants	-	1,010,520	-	1,010,520
391.02 Debt issued	-	754,000	-	754,000
441 Debt service	-	(19,055)	-	(19,055)
442 Interest expense	-	(5,585)	-	(5,585)
Total nonoperating revenue	<u>-</u>	<u>1,739,880</u>	<u>-</u>	<u>1,739,880</u>
Change in Net Position	(1,637)	19,885	(6,647)	11,601
Net Position - Beginning	<u>89,198</u>	<u>56,606</u>	<u>240,939</u>	<u>386,743</u>
Net Position - Ending	<u>\$ 87,561</u>	<u>\$ 76,491</u>	<u>\$ 234,292</u>	<u>\$ 398,344</u>

City of Hosmer  
Statement of Cash Flows-Modified Cash Basis-Proprietary Funds  
Year Ended December 31, 2016

	Enterprise Funds			
	Water Fund	Sewer Fund	Liquor Fund	Totals
Cash Flows from (used for) Operating Activities				
Receipt from customers	\$ 50,928	\$ 72,601	\$ 236,093	\$ 359,622
Payments to suppliers	(21,726)	(5,228)	(186,245)	(213,199)
Payments to employees	(30,839)	(29,504)	(67,178)	(127,521)
Other receipts	-	373	10,683	11,056
Net Cash from (used for) Operating Activities	<u>(1,637)</u>	<u>38,242</u>	<u>(6,647)</u>	<u>29,958</u>
Cash Flows from (used for) Capital and Related Financing Activities				
Capital grants	-	1,010,520	-	1,010,520
Purchase of capital assets	-	(1,758,237)	-	(1,758,237)
Proceeds from long-term debt	-	754,000	-	754,000
Principal paid on capital debt	-	(19,055)	-	(19,055)
Interest paid on capital debt	-	(5,585)	-	(5,585)
Net Cash used for Capital and Related Financing Activities	<u>-</u>	<u>(18,357)</u>	<u>-</u>	<u>(18,357)</u>
Net Change in Cash and Cash Equivalents	(1,637)	19,885	(6,647)	11,601
Cash and Cash Equivalents - Beginning	<u>86,198</u>	<u>56,606</u>	<u>240,939</u>	<u>383,743</u>
Cash and Cash Equivalents - Ending	<u>\$ 84,561</u>	<u>\$ 76,491</u>	<u>\$ 234,292</u>	<u>\$ 395,344</u>

	Enterprise Funds			
	Water Fund	Sewer Fund	Liquor Fund	Totals
Cash and Cash Equivalents Consist of:				
Cash and cash equivalents	\$ 84,561	\$ 76,491	\$ 234,292	\$ 395,344
	<u>\$ 84,561</u>	<u>\$ 76,491</u>	<u>\$ 234,292</u>	<u>\$ 395,344</u>
Reconciliation of Operating Income (Loss) to Net Cash from (used for) Operating Activities				
Operating loss	\$ (1,637)	\$ (1,719,995)	\$ (6,647)	\$ (1,728,279)
Adjustments to reconcile operating income (loss) to net cash from operating activities:				
Purchase of capital assets	-	1,758,237	-	1,758,237
Net Cash from (used for) Operating Activities	<u>\$ (1,637)</u>	<u>\$ 38,242</u>	<u>\$ (6,647)</u>	<u>\$ 29,958</u>

## **Note 1 - Summary of Significant Accounting Policies**

As discussed further in Note 1.C, the financial statements are presented on a modified cash basis of accounting. The modified cash basis of accounting differs from accounting principles generally accepted in the United States of America (GAAP). Generally accepted accounting principles include all relevant Governmental Accounting Standards Board (GASB) pronouncements.

### **A. Financial Reporting Entity**

The reporting entity of the City of Hosmer (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); 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 City's financial statements to be misleading or incomplete.

The reporting entity is comprised of the primary government, City of Hosmer.

Component units are legally separate organizations for which the elected officials of the primary government are financially accountable. The City is financially accountable if its Governing Board appoints a voting majority of another organization's governing body and it has the ability to impose its will on that organization, or there is a potential for that organization to provide specific financial benefits to, or impose specific financial burdens on, the City (primary government). The City may also be financially accountable for another organization if that organization is fiscally dependent on the City.

Based upon the application of these criteria, the City does not have any component units.

### **B. Basis of Presentation**

#### **Government-Wide Financial Statements**

The statement of net position and statement of activities display information about the City as a whole. They include all funds of the City. 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 City are organized into funds, each of which is considered to be a separate accounting entity. Each fund is accounted for by providing a separate set of self-balancing accounts that constitute its assets, liabilities, fund equity, revenues, and expenditures/expenses. Funds are organized into three major categories: governmental, proprietary and fiduciary. An emphasis is placed on major funds within the governmental and proprietary categories. A fund is considered major if it is the primary operating fund of the City or it meets the following criteria:

1. Total assets, liabilities, revenues or expenditures/expenses of the individual governmental or enterprise fund are at least 10% 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% 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.

The funds of the City of Hosmer 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.

### **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) 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.

- **Water Fund** - Financed primarily by user charges, this fund accounts for the construction and operation of the municipal waterworks system and related facilities. (SDCL 9-47-1) This is a major fund.
- **Sewer Fund** - Financed primarily by user charges, this fund accounts for the construction and operation of the municipal sanitary sewer system and related facilities. (SDCL 9-48-2) This is a major fund.
- **Liquor Fund** – Financed primarily by consumer charges, this fund accounts for the construction and operation of the municipal bar and related equipment. This is a major fund.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the City's enterprise funds are charges to customers for sales and services. Operating expenses for enterprise funds include the cost of sales and services and administrative expenses. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

### **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**

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 within the limitations of the modified cash basis of accounting as defined below.

In the fund financial statements, the current financial resources measurement focus or the economic resources measurement focus is applied within the limitations of the modified cash basis of accounting.

#### **Basis of Accounting**

The financial statements are presented in accordance with a modified cash basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America (GAAP) as established by the Governmental Accounting Standards Board. This basis of accounting involved modifications to the cash basis of accounting to report in the statement of net position or balance sheet cash transactions or events that provide a benefit or result in an obligation that covers a period greater than the period in which the cash transaction or event occurred. Such report balances include investments.

This modified cash basis of accounting differs from GAAP primarily because certain assets and their related revenues (such as accounts receivable and revenue for billed or provided services not yet collected, and other accrued revenue and receivables) and certain liabilities and their related expenses or expenditures (such as accounts payable and expenses for goods or services received but not yet paid, and other accrued expenses and liabilities) are not recorded in these financial statements. In addition, other economic assets, deferred outflows, liabilities, and deferred inflows of resources that do not arise from a cash transaction or event that would be reported in GAAP basis financial statements (such as donated assets) are not reported in this modified cash basis presentation, and the measurement of reported assets and liabilities does not involve adjustment to fair value.

### **D. Deposits and Investments**

For the purpose of financial reporting, “cash and cash equivalents” includes all demand and savings accounts and certificates of deposit or short-term investments with a term to maturity at date of acquisition of three months or less. Investments in open-end mutual fund shares or similar investments in external investment pools are also considered to be cash equivalents.

Investments classified in the financial statements consist entirely of certificates of deposit whose term to maturity at date of acquisition exceeds three months and/or those types of investment authorized by South Dakota Codified Laws (SDCL) 4-5-6. Under the modified cash basis of accounting, investments are carried at cost.

## **E. Interfund Eliminations and Reclassifications**

### **Government-Wide Financial Statements**

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

1. The City did not have any interfund receivables and payables that needed to be eliminated as of December 31, 2016.
2. The City did not have internal service fund activity which required elimination as of December 31, 2016.

## **F. Capital Assets**

Under the modified cash basis of accounting, capital assets are expensed when the cash transaction occurs.

## **G. Long-Term Liabilities**

Under the modified cash basis of accounting, cash proceeds from long-term debt issuances are recorded as a receipt, while payments to creditors to reduce long-term debts are recorded as a cost of the program which benefits from the financing. Allocations are made where appropriate. Interest costs are not allocated, but are reported as a separate program cost category.

Long-term debts arising from cash transactions of governmental funds are not reported as liabilities in the fund financial statements. Instead, the debt proceeds are reported as other financing sources and payments of principal and interest are reported as expenditures. Under the modified cash basis, the accounting for long-term debts of proprietary funds is the same in the fund financial statements as it is in the government-wide financial statements.

## **H. Program Revenues**

In the government-wide statement of activities, reported program revenues derive directly from the program itself or from parties other than the City's taxpayers or citizenry, as a whole. Program revenues are classified into three categories, as follows:

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

## **I. Proprietary Funds Revenue and Expense Classifications**

In the proprietary fund's statement of revenues, expenses and changes in fund net position, revenues and expenses are classified in a manner consistent with how they are classified in the statement of cash flows. That is, transactions for which related cash flows are reported as capital and related financing activities, noncapital financing activities, or investing activities are not reported as components of operating revenues or expenses.

## **J. Cash and Cash Equivalents**

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

## **K. Equity Classifications**

### **Government-Wide Statements**

Equity is classified as net position and is comprised of three components, net investment in capital assets; restricted net position; and unrestricted net position. Because capital assets are not reported by the City under the modified cash basis of accounting, only the following components are displayed:

1. Restricted Net Position – Consists of net position with constraints placed on their use either by (a) external groups such as creditors, grantors, contributors or laws and regulations of other governments; or (b) law through constitutional provisions or enabling legislation.
2. Unrestricted Net Position – All other net position that do not meet the definition of “restricted.”

### **Fund Financial Statements**

Governmental fund equity is classified as fund balance, and may distinguish between nonspendable, restricted, committed, assigned and unassigned components. Proprietary fund equity is classified the same as in the government-wide financial statements.

## **L. Application of Net Position and Fund Balance**

The City uses restricted/committed amounts first when both restricted and unrestricted fund balance is available unless there are legal documents/contracts that prohibit doing this, such as grant agreements requiring dollar for dollar spending. Additionally, the government would first use committed, then assigned, and lastly unassigned amounts of unrestricted fund balance when expenditures are made.

## **M. Fund Balance Classification Policies and Procedures**

The following classifications describe the relative strength of the spending constraints:

- Nonspendable Fund Balance - Amounts that are not in nonspendable form are required to be maintained intact.
- Restricted Fund Balance - Amounts constrained to specific purposes by their providers (such as grantors, bondholders, and higher levels of government), through constitutional provisions, or by enabling legislation.
- Committed Fund Balance - Amounts constrained to specific purposes by the City itself, using its highest level of decision-making authority (i.e., Board of Trustees). To be reported as committed, amounts cannot be used for any other purpose unless the City takes the same highest level action to remove or change the constraint.
- Assigned Fund Balance - Amounts the City intends to use for a specific purpose. Intent can be expressed by the Board of Trustees or by an official or body to which the Board of Trustees delegates the authority.
- Unassigned Fund Balance - Amounts that are available for any purpose. Positive amounts are reported only in the General Fund.

The Board of Trustees establishes (and modifies or rescinds) fund balance commitments by passage of an ordinance. An assigned fund balance is established by the Board of Trustees through adoption of a resolution designating a fund balance is intended for specific purpose (such as the purchase of fixed assets, construction, debt service, or for other purposes).

The City does not have a formal minimum fund balance policy.

#### **N. Rounding**

Computer generated rounding variances exist in the basic financial statements and supplementary information. The variances result from values being entered with cents rather than as whole numbers.

#### **Note 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% 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 authorized to do business in South Dakota.

**Custodial Credit Risk – Deposits** – The risk that, in the event of a depository failure, the City's deposits may not be returned to it. The City does not have a deposit policy for custodial credit risk. As of December 31, 2016, the City maintained their deposits in in-state financial institutions which were properly collateralized in accordance with SDCL 4-6A-3.

The actual bank balances at December 31, 2016 are as follows:

	Bank Balance
Insured (FDIC/NCUA)	\$ 271,096
Uninsured, collateral jointly held by State's/Town's agent in the name of the State and the pledging financial institution	860,289
	\$ 1,131,385

The City's carrying amount of deposits at December 31, 2016 is as follows:

Cash and cash equivalents	\$ 946,265
Investments	21,096
	\$ 967,361

### 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).

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 (NAV) 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. The City reports all funds invested in SDFIT as cash equivalents.

**Interest Rate Risk** – The City does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. As of December 31, 2016 all of the City's investments consist of certificates of deposit which have maturities of less than one year.

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

**Custodial Credit Risk** – The risk that, in the event of the counterparty to a transaction, the City will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The City has no investments exposed to custodial credit risk.

Concentration of Credit Risk – The City places no limit on the amount that may be invested in any one issuer. All investments are held with Farmer’s State Bank of Hosmer.

Under the modified cash basis of accounting, investments are stated at cost.

**Note 3 - Property Taxes**

Property taxes are levied on or before October 1 of the year preceding the start of the fiscal year. They attach as an enforceable lien on property and become due and payable as of January 1, the first day of the fiscal year. Taxes are payable in two installments on or before April 30 and October 31 of the fiscal year.

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.

**Note 4 - Significant Contingencies - Litigation**

At December 31, 2016, the City was not involved in any litigation that would be material to the financial statements.

**Note 5 - Restricted Net Position**

Restricted net position for the year ended December 31, 2016 is as follows:

<u>Fund</u>	<u>Restricted By</u>	<u>Amount</u>
Sewer - Debt Service and Other Reserves	Contractual Agreement	\$ 15,450

**Note 6 - Risk Management**

The City is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. During the period ended December 31, 2016, the City managed its risks as follows:

**Employee Health Insurance**

The City does not provide a group health insurance plan for City employees. Each employee is responsible to obtain individual health insurance.

**Liability Insurance**

The City joined the South Dakota Public Assurance Alliance, a public entity risk pool currently operating as a common risk management and insurance program for South Dakota local government entities. The City pays an annual premium to the pool to provide coverage for general liability and automobile liability.

The agreement with the South Dakota Public Assurance Alliance provides that the above coverages will be provided to a \$3,000,000 and \$1,000,000 limit, respectively. Member premiums are used by the pool for payment of claims and to pay for reinsurance for claims in excess of \$500,000 for liability coverage to the upper limit. A portion of the member premiums are also allocated to a cumulative reserve fund. As of December 31, 2016, the City has vested balance in the cumulative reserve fund of \$8,395. The City carries the following deductibles for the coverages listed above:

Coverage	Deductible
General liability	\$ -
Automobile liability	-

The City does not carry additional insurance to cover claims in excess of the upper limit. Settled claims resulting from these risks have never exceeded the liability coverage.

**Worker's Compensation**

The City joined the South Dakota Municipal League Worker's Compensation Fund, a public entity risk pool currently operating as a common risk management and insurance program for South Dakota local government entities. The City pays an annual premium to the pool to provide worker's compensation coverage for its employees. 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 an additional \$2,000,000 per individual per incident.

The City does not carry additional insurance to cover claims in excess of the upper limit. Settled claims resulting from these risks have never exceeded the liability coverage.

**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.

**Note 7 - Commitments**

As December 31, 2016, the City has commitments of approximately \$4,100,000 for costs related to a sewer improvement project, of which \$1,817,542 in payments had been made as of year-end. The project is being funded through a grant and loan totaling \$2,901,000 and \$754,000, respectively, from USDA - Rural Development and a grant for \$515,000 from the U.S. Department of Housing and Urban Development.

**Note 8 - Violations of Finance Related Legal and Contractual Provisions**

The City is prohibited by statute from spending in excess of appropriated amounts at the fund level. The City overspent the public works budget in the General Fund by \$3,813 for the year ended December 31, 2016. The City has excess fund balance to cover the excess spending.

**Note 9 - Subsequent Events**

In October of 2017, the City completed its sewer improvement project which had a total cost of \$3,125,779. This project was funded through loans and grants from USDA – Rural Development and U.S. Department of Housing and Urban Development.



Supplementary Information  
December 31, 2016  
**City of Hosmer**

City of Hosmer  
 Schedule of Changes in Long-Term Debt  
 Year Ended December 31, 2016

<u>Indebtedness</u>	<u>Long-Term Debt 1/1/16</u>	<u>Add New Debt</u>	<u>Less Debt Retired</u>	<u>Long-Term Debt 12/31/16</u>
Enterprise Long-Term Debt				
USDA Rural Development				
Loan - Water	\$ -	\$ 754,000	\$ 19,055	\$ 734,945
Total	<u>\$ -</u>	<u>\$ 754,000</u>	<u>\$ 19,055</u>	<u>\$ 734,945</u>

City of Hosmer  
 Budgetary Comparison Schedule – General Fund  
 Year Ended December 31, 2016

	Budgeted Amounts		Actual Amounts	Variance with Final Budget Positive (Negative)
	Original	Final		
Revenues				
310 Taxes				
311 General property taxes	\$ 24,550	\$ 24,550	\$ 22,785	\$ (1,765)
313 General sales and use taxes	54,000	54,000	52,989	(1,011)
315 Amusement taxes	48	48	48	-
319 Penalties and interest on delinquent taxes	75	75	54	(21)
Total taxes	<u>78,673</u>	<u>78,673</u>	<u>75,876</u>	<u>(2,797)</u>
320 Licenses and permits	<u>100</u>	<u>100</u>	<u>46</u>	<u>(54)</u>
330 Intergovernmental revenue				
331 Federal grants	-	-	937	937
335 State Shared revenue				
335.01 Bank franchise tax	1,725	1,725	791	(934)
335.02 Motor vehicle commercial prorated	1,200	1,200	1,571	371
335.03 Liquor tax reversion	2,050	2,050	-	(2,050)
335.04 Motor vehicle licenses (5%)	6,500	6,500	7,586	1,086
335.08 Local government highway and bridge fund	4,500	4,500	4,988	488
338 County shared revenue				
338.01 County road tax (25%)	-	-	308	308
338.03 County wheel tax	-	-	992	992
Total intergovernmental revenue	<u>15,975</u>	<u>15,975</u>	<u>17,173</u>	<u>1,198</u>
340 Charges for goods and services				
344 Sanitation	<u>4,800</u>	<u>4,800</u>	<u>4,853</u>	<u>53</u>
Total charges for goods and services	<u>4,800</u>	<u>4,800</u>	<u>4,853</u>	<u>53</u>
360 Miscellaneous revenue				
361 Investment earnings	515	515	423	(92)
362 Rentals	3,100	3,100	675	(2,425)
363 Special assessments	1,000	1,000	300	(700)
369 Other	2,700	2,700	2,556	(144)
Total miscellaneous revenue	<u>7,315</u>	<u>7,315</u>	<u>3,954</u>	<u>(3,361)</u>
Total revenues	<u>106,863</u>	<u>106,863</u>	<u>101,902</u>	<u>(4,961)</u>

City of Hosmer  
 Budgetary Comparison Schedule – General Fund  
 December 31, 2016

	Budgeted Amounts		Actual Amounts	Variance with Final Budget Positive (Negative)
	Original	Final		
Expenditures				
410 General government				
411 Legislative	18,130	18,130	10,256	7,874
411.5 Contingency	25,000	25,000	-	25,000
Amount transferred	-	-	-	-
414 Financial administration	15,860	15,860	9,852	6,008
419 Other general government	8,950	8,950	19,186	(10,236)
Total general government	<u>67,940</u>	<u>67,940</u>	<u>39,294</u>	<u>28,646</u>
430 Public works				
431 Highways and streets	59,743	59,743	63,416	(3,673)
432 Sanitation	875	875	1,015	(140)
Total public works	<u>60,618</u>	<u>60,618</u>	<u>64,431</u>	<u>(3,813)</u>
440 Health and welfare				
441 Health	3,150	3,150	420	2,730
Total health and welfare	<u>3,150</u>	<u>3,150</u>	<u>420</u>	<u>2,730</u>
450 Culture and recreation				
451 Recreation	900	900	707	193
Total culture and recreation	<u>900</u>	<u>900</u>	<u>707</u>	<u>193</u>
Total expenditures	<u>132,608</u>	<u>132,608</u>	<u>104,852</u>	<u>27,756</u>
Other Financing Sources (Uses)				
391.03 Sale of municipal property	400	400	9,698	9,298
Total other financing sources (uses)	<u>400</u>	<u>400</u>	<u>9,698</u>	<u>9,298</u>
Excess of Revenue under Expenditures	(25,345)	(25,345)	6,748	32,093
Net Position - Beginning	562,269	562,269	562,269	-
Fund Balance - Ending	<u>\$ 536,924</u>	<u>\$ 536,924</u>	<u>\$ 569,017</u>	<u>\$ 32,093</u>

### **Note 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 City Commission introduces the annual appropriation ordinance for the ensuing fiscal year.
2. After adoption by the City Commission, the operating budget is legally binding and actual expenditures for each purpose cannot exceed the amounts budgeted, except as indicated in Number 4.
3. A line item for contingencies may be included in the annual budget. Such a line item may not exceed 5% of the total municipal budget and may be transferred by resolution of the City Commission 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 City Commission.

Encumbrance accounting, under which purchase orders, contracts and other commitments for the expenditure of monies are recorded in order to reserve that portion of the applicable appropriation, is employed as an extension of formal budgetary integration in the General Fund, special revenue funds and capital projects funds.

The City did not encumber any amounts at December 31, 2016.

6. Formal budgetary integration is employed as a management control device during the year for the General Fund. Formal budgetary integration is not employed for debt service funds because effective budgetary control is alternatively achieved through general obligation bond indenture provisions.
7. Budget for the General Fund is adopted on a basis consistent with a modified cash basis of accounting.

### **Note 2 - Modified Cash Basis/Budgetary Accounting Basis Differences**

The financial statements prepared on the modified cash basis of accounting 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 fire truck 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 comparison schedule, the purchase of a fire truck would be reported as an expenditure of the Public Safety/Fire Department function of government, along with all other current Fire Department related expenditures.



**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***

The Board of Trustees  
City of Hosmer  
Hosmer, South Dakota

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities and each major fund of the City of Hosmer as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the City’s basic financial statements and have issued our report thereon dated April 3, 2018. The statements were prepared on the modified cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

**Internal Control over Financial Reporting**

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting 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 and questioned costs as 2016-A, 2016-B, and 2016-D 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 deficiency described in the accompanying schedule of findings and questioned costs as 2016-C to be a significant deficiency.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed the instance of noncompliance or other matters that are required to be reported under *Government Audit Standards*, which is described in the accompanying schedule of findings and questioned costs as item 2016-C.

**City of Hosmer's Response to Findings**

The City's responses to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. The City's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. 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.



---

Aberdeen, South Dakota  
April 3, 2018



**Independent Auditor's Report on Compliance for the Major Federal Program; Report on Internal Control Over Compliance; and Report on the Schedule of Expenditures of Federal Awards Required by the Uniform Guidance**

To the City Council  
City of Hosmer  
Hosmer, South Dakota

**Report on Compliance for Major Federal Program**

We have audited the City of Hosmer's (the City) compliance with the types of compliance requirements described in the OMB Compliance Supplement that could have a direct and material effect on the City's major federal program for the year ended December 31, 2016. The City's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

**Management's Responsibility**

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

**Auditor's Responsibility**

Our responsibility is to express an opinion on the compliance for the City's major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

**Basis for Qualified Opinion on the Major Federal Program**

As described in the accompanying schedule of findings and questioned costs, the City did not comply with requirements regarding CFDA 10.760 Water and Waste Disposal Systems for Rural Communities as described in finding number 2016-002 for Procurement. Compliance with such requirements is necessary, in our opinion, for the City to comply with the requirements applicable to that program.

**Qualified Opinion**

In our opinion, except for the noncompliance described in the Basis for Qualified Opinion paragraph, the City complied, in all material aspects, with the types of compliance requirements referred to above that could have a direct and material effect on its major Federal program identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs for the year ended December 31, 2016.

## **Other Matters**

City of Hosmer's response to the noncompliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs. City of Hosmer's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

## **Report on Internal Control over Compliance**

Management of the City is responsible for establishing and maintaining effective internal control over compliance with the compliance requirements referred to above. In planning and performing our audit of compliance, we considered the City of Hosmer's internal control over compliance with the types of requirements that could have a direct and material effect on the major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses and significant deficiencies may exist that have not been identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be a material weakness and a significant deficiency.

*A deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement will not be prevented, or detected and corrected, on a timely basis. We consider the deficiency in internal control over compliance described in the accompanying schedule of findings and questioned costs as item 2016-002 to be a material weakness.

*A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. We consider the deficiency in internal control over compliance described in the accompanying schedule of findings and questioned costs as item 2016-001 to be a significant deficiency.

The City's responses to the internal control over compliance findings identified in our audit are described in the accompanying schedule of findings and questions cost and corrective action plan. The City's responses were not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the responses.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose. As required by South Dakota Codified Law 4-11-11, this report is a matter of public record and its distribution is not limited.

**Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance**

We have audited the financial statements of City of Hosmer as of and for the year ended December 31, 2016, and have issued our report thereon dated April 3, 2018, which contained an unmodified opinion on those financial statements. Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the Uniform Guidance and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the financial statements as a whole.

*Eide Bailly LLP*

Aberdeen, South Dakota  
April 3, 2018

City of Hosmer  
Schedule of Expenditures of Federal Awards  
Year Ended December 31, 2016

Federal Grantor/Pass-Through Grantor Program Title	Pass-Through Identification Number	Federal CFDA Number	Expenditures
U.S. Department of Agriculture			
Direct Federal Funding:			
Water and Waste Disposal Systems for Rural Communities	*****	10.760	\$ 1,526,117
Total U.S. Department of Agriculture			<u>1,526,117</u>
U.S. Department of Housing and Urban Development			
Passed through State			
Community Development Block Grants/Entitlement Grants	*****	14.228	<u>224,198</u>
Total U.S. Department of Housing and Urban Development			<u>224,198</u>
Total Federal Financial Assistance			<u><u>\$ 1,750,315</u></u>

\*\*\*\*\* No Pass-Through Entity Identifying Number Given

See Notes to Schedule of Expenditures of Federal Awards

**Note A – Basis of Presentation**

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the City, and is presented on the modified cash basis of accounting. The information in this schedule is presented in accordance with the requirements of the Uniform Guidance. City of Hosmer received federal awards directly from federal agencies and indirectly through pass-through entities. If federal financial assistance is provided to a subrecipient, it is treated as an expenditure when it is paid to the subrecipient. There were no subrecipients relating to these federal awards.

**Note B – Significant Accounting Policies**

Governmental and business type fund types account for the City’s federal grant activity. Expenditures in the schedule of expenditures of federal awards are recognized on the modified cash basis of accounting – transactions are recorded when cash is received or disbursed. The City’s summary of significant accounting policies is presented in Note 1 in the City’s basic financial statements.

The City has not elected to use the 10% de minimus cost rate.

**Note C – Loan Programs**

Expenditures reported in this schedule consist of the beginning of year outstanding loan balance plus eligible expenditures incurred during the year December 31, 2016. The outstanding loan balance at December 31, 2016 was \$734,945 and represents eligible expenditure that have been funded with drawn down proceeds of the federal loan, less principal payments made as of December 31, 2016.

**Section I – Summary of Auditor’s Results**

**FINANCIAL STATEMENTS**

Type of auditor's report issued	Unmodified
Internal control over financial reporting:	
Material weaknesses identified	Yes
Significant deficiencies identified not considered to be material weaknesses	Yes
Noncompliance material to financial statements noted?	No

**FEDERAL AWARDS**

Internal control over major program:	
Material weaknesses identified	Yes
Significant deficiencies identified not considered to be material weaknesses	Yes
Type of auditor's report issued on compliance for major programs:	Qualified
Any audit findings disclosed that are required to be reported in accordance with Uniform Guidance 2 CFR 200.516:	Yes

**Identification of major programs:**

<u>Name of Federal Program</u>	CFDA Number
Water Waste Disposal Systems for Rural Communities	10.760
Dollar threshold used to distinguish between type A and type B programs:	\$ 750,000
Auditee qualified as low-risk auditee?	No

---

**Section II – Financial Statement Findings**

---

**Finding 2016-A - Preparation of Financial Statements, Footnotes and Material Journal Entries**

*Criteria:* The City’s internal control structure should be designed to provide for the preparation of the financial statements and footnotes, which includes having an adequate system for recording and processing entries material to the financial statements being audited in accordance with the modified cash basis of accounting.

*Condition:* City of Hosmer requested the external auditors to prepare the financial statements and related notes for the year ended December 31, 2016. As a part of the financial statement preparation process, at times we propose material audit adjustments that are not identified as a result of the City’s existing internal controls and, therefore, could result in a misstatement of the City’s financial statements.

*Cause:* The City does not have adequate staff trained to prepare financial statements and the related footnotes and could cause the need for auditors to at times propose material journal entries.

*Effect:* This condition may affect the City’s ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

*Recommendation:* This circumstance is not unusual in an organization of this size. It is the responsibility of management and those charged with governance to make the decision whether to accept the degree of risk associated with this condition because of cost or other considerations. Also, a thorough review of the transactions in each fund should take place prior to the beginning of the audit, to ensure that the modified cash basis of accounting has been followed for each fund type, especially for transaction types infrequent in occurrence.

*Views of Responsible Officials:* Management agrees with the finding.

**Finding 2016-B - Lack of Segregation of Duties**

*Criteria:* A good system of internal controls contemplates an adequate segregation of duties so that no one individual handles a transaction from its inception to its completion.

*Condition:* The City of Hosmer has a limited number of office personnel and, accordingly, does not have adequate internal accounting controls in revenue, expenditures, and payroll functions because of a lack of segregation of duties.

*Cause:* The City has an insufficient number of staff to adequately separate duties.

*Effect:* This condition increases the risk of fraud or errors that might occur in the financial reporting process and not be detected.

*Recommendation:* Although it is recognized that number of office staff may not be large enough to permit adequate segregation of duties in all respects, it is important that management and those charged with governance be aware of this condition. We recommend that the Board of Trustees exercise adequate oversight of the accounting function.

*Views of Responsible Officials:* Management agrees with the finding.

**Finding 2016-C – Over-Expending of Fund Budgets**

*Criteria:* City of Hosmer is prohibited by statute from spending in excess of appropriated amounts at the fund level. The City Council has the authority to amend the original budget to realign funds or release additional funds for spending; however, such spending should not occur until approval of such amendments has taken place.

*Condition:* The total expenditures for public works in the general fund exceeded the amounts budgeted for the year ended December 31, 2016.

*Cause:* There is currently no control system in place to prevent unauthorized over-expenditure of budgeted amounts.

*Effect:* This condition violates state statute and does not allow for the budgeting process control to be effective.

*Recommendation:* It is our recommendation that the City Council and management consider the necessary procedures that would allow for appropriate amendments to all fund budgets prior to excess expenditures being made.

*Views of Responsible Officials:* Management agrees with the finding.

**Finding 2016-D – Reconciliation of Bank Deposits**

*Criteria:* A good system of internal controls provides that the bank accounts are reconciled to the amounts recorded in the general ledger at the end of each month and differences are reviewed and corrected in a timely manner.

*Condition:* The Finance Officer, when preparing the month bank reconciliations, did not process the reconciliation all the way through in the accounting software, resulting in misstatements that were corrected through adjusting journal entries.

*Cause:* The Finance Officer, when performing the monthly bank reconciliations, did not compare the reconciled balance to the general ledger and review and correct any differences in a timely manner.

*Effect:* This condition increases the risk that the report amount of cash, revenues, and expenditures could be misstated.

*Recommendation:* We recommend that the Finance Officer reconcile all checking and savings accounts to the general ledger at the end of the month and post correcting entries as needed to bring the general ledger balances into agreement with the reconciled balances. We also recommend that someone other than the preparer review the reconciliations for accuracy, propriety, and agreement to the general ledger.

*Views of Responsible Officials:* Management agrees with the finding.

---

**Section III – Federal Award Findings and Questioned Costs**

---

**2016-001**      **U.S. Department of Agriculture**  
**CFDA # 10.760 For the Year Ended December 31, 2016**  
**Water and Waste Disposal Systems for Rural Communities**

**Reporting**  
**Significant Deficiency in Internal Control**

*Criteria:* 7 CFR section 1780.47 and the program letter of conditions defines the program reporting requirements and reporting requirement deadlines for submission of the required reports. Internal controls are required to be in place to ensure the timeliness and accuracy of the reporting.

*Condition:* Of the two reports required to be submitted, we noted in testing that there was either no review for accuracy of the reported information, or the review for accuracy of the reported information was not timely and took place after the submission of the report and after the reporting deadline.

*Cause:* Internal controls were not adequately designed to ensure that these required reports were reviewed by a second individual for accuracy prior to the submission of the reports to the applicable federal agency.

*Effect:* Lack of internal review of these reports can result in inaccurate information or unsupported information being provided to the federal agency which is being used to satisfy program requirements.

*Questioned Costs:* None reported.

*Context/Sampling:* Sampling was not used, tested 100% of population.

*Repeat Finding from Prior Year(s):* No

*Recommendation:* We recommend that management in cooperation with the City Council institute a review process of these reports and ensure the review takes place prior to submission of the required reports to ensure accuracy and compliance with the applicable requirements.

*Views of Responsible Officials:* Management agrees with the finding.

**2016-002      U.S. Department of Agriculture  
CFDA # 10.760 For the Year Ended December 31, 2016  
Water and Waste Disposal Systems for Rural Communities**

**Procurement  
Material Weakness in Internal Control over Compliance and Noncompliance**

*Criteria:* Uniform Guidance and 2 CFR sections 200.318 through 200.326 set forth the procurement standards non-federal entities other than states must follow when operating federal programs and the procurement procedures required depending on the amount of the transaction.

*Condition:* In our testing of procurement, it was identified that the City did not have a written policy on procurement that satisfied the requirements of 2 CFR sections 200.318 through 200.326 and there was no observable control documentation to directly indicate that a cost or price analysis was performed in connection with one covered transaction. Additionally, the City secured a contract through noncompetitive proposal without meeting one of the allowable circumstances as indicated in 2 CFR section 200.320.

*Cause:* Lack of oversight, awareness, or understanding of all of the specific requirements under the Uniform Guidance and applicable CFR sections and controls were not adequately designed to ensure compliance with all of these requirements.

*Effect:* A lack of documented policies and established controls increase the overall risk that employees are not aware of the specific requirements with contracting and awarding contracts to lower tier entities.

*Questioned Costs:* None reported

*Context/Sampling:* All vendors, which totaled four, were selected for procurement testing.

*Repeat Finding from Prior Year(s):* No

*Recommendation:* We recommend that management establish a written policy that addresses all of the procurement requirements for federal programs as identified in 2 CFR sections 200.318 through 200.326, and maintain adequate supporting documentation and records to document history and methods of procurement and the procedures performed to comply with these CFR sections.

*Views of Responsible Officials:* Management agrees with the finding.

# City of Hosmer

115 West Main Street

PO Box 1

Hosmer, SD 57448

Phone: (605) 283-2748

[berry@valleytel.net](mailto:berry@valleytel.net)



Management's Response to Auditor's Findings:

Corrective Action Plan

December 31, 2016

Prepared by Management of

**City of Hosmer**

***Finding 2016-A- Preparation of Financial Statements, Footnotes and Material Journal Entries***

*Finding Summary:* Eide Bailly LLP prepared our draft financial statements and accompanying notes to the financial statements. They also proposed material audit adjustments that would not have been identified as a result of our existing controls and, therefore, could have resulted in a material misstatement of our financial statements.

*Responsible Individuals:* Barb Gienger, Finance Officer

*Corrective Action Plan:* It is not cost effective to have an internal control system designed to provide for the preparation of the financial statements and accompanying notes. We requested that our auditors, Eide Bailly LLP, prepared the financial statements and the accompanying notes to the financial statements as a part of their annual audit. We have designated a member of management to review the drafted financial statements and accompanying notes, and we have reviewed with and agree with the material adjustments proposed during the audit.

*Anticipated Completion Date:* Ongoing

***Finding 2016-B- Lack of Segregation of Duties***

*Finding Summary:* A good system of internal controls contemplates an adequate segregation of duties so that no one individual handles a transaction from its inception to its completion. City of Hosmer has a limited number of personnel, and accordingly, does not have adequate internal accounting controls in revenue, expenditures, and payroll functions due to lack of segregation of duties.

*Responsible Individuals:* Barb Gienger, Finance Officer

*Corrective Action Plan:* It is not cost effective due to the size of the City and volume of transactions to have an internal control system designed with additional staff to facilitate the segregation of duties from start to finish. Management and the City Council are aware of the condition and accept the relevant risks that are presented by this finding.

*Anticipated Completion Date:* Ongoing

### ***Finding 2016-C- Over Expending of Fund Budgets***

***Finding Summary:*** City of Hosmer is prohibited by statute from spending in excess of appropriated amounts at the fund level. The City Council has the authority to amend the original budget to realign funds or release additional funds for spending; however; such spending should not occur until approval of such amendments has taken place. Total expenditures for public works in the general fund exceeded the amounts budgeted for.

***Responsible Individuals:*** Barb Gienger, Finance Officer

***Corrective Action Plan:*** The City will be overly conscious of budget and take necessary actions to transfer funds to ensure overspending of budgets does not occur.

***Anticipated Completion Date:*** December 31, 2017

### ***Finding 2016-D Reconciliation of Bank Deposit***

***Finding Summary:*** A good system of internal controls provides that the bank accounts are reconciled to the amounts recorded in the general ledger at the end of each month and differences are reviewed and corrected in a timely manner. The Finance Officer, when preparing the month bank reconciliation, did not process the reconciliation all the way through in the accounting software, resulting in misstatements that were corrected through journal entries.

***Responsible Individual:*** Barb Gienger, Finance Officer

***Corrective Action Plan:*** The City will take the necessary steps to ensure that the bank accounts are properly reconciled all the way through in the accounting software.

***Anticipated Completion Date:*** December 31, 2017

### ***Finding 2016-001***

***Federal Agency Name: U.S. Department of Agriculture***

***Program Name: Water and Waste Disposal System for Rural Communities***

***CFDA # 10.760 For the Year Ended December 31, 2016***

***Finding Summary:*** Of the two reports required to be submitted, Eide Bailly LLP noted in testing that there was either no review for accuracy of the reported information, or the review for accuracy of the reported information was not timely and took place after the submission of the report and after the reporting deadline.

***Responsible Individual:*** Barb Gienger, Finance Officer

***Corrective Action Plan:*** The City, due to timing, is unable to correct this finding for the current project, but for future projects the City will have the City Council review reports for accuracy and prior to submission or the required reporting deadlines.

***Anticipated Completion Date:*** Ongoing

***Finding 2016-002***

***Federal Agency Name: U.S. Department of Agriculture***

***Program Name: Water and Waste Disposal System for Rural Communities***

***CFDA # 10.760 For the Year Ended December 31, 2016***

***Finding Summary:***

Eide Bailly LLP, determined in the testing of Uniform Guidance, that the City of Hosmer did not have a written policy on procurement that satisfied the requirements of 2 CFR Sections 200.318 through 200.326 and there was no observable control documentation to directly indicate that a cost or price analysis was performed in connection with one covered transaction. Additionally, the City secured a contract through noncompetitive proposal without meeting one of the allowable circumstances as indicated in 2 CFR section 200.320.

***Responsible Individuals:***

Barb Gienger, Finance Officer

***Corrective Action Plan:***

The City, due to timing, is unable to correct this finding for the current project. The City for future projects will establish a written policy that addresses all of the procurement requirements of the State of South Dakota and those requirements for federal program procurements as identified in 2 CFR sections 200.318 through 200.326 and maintain adequate supporting documentation and records to document history of procurement and the procedures performed to comply with these CFR sections.

***Anticipated Completion Date:***

Ongoing