

**MUNICIPALITY OF MONTROSE
MONTROSE, SOUTH DAKOTA**

AUDIT REPORT

FOR THE YEAR JANUARY 1, 2012 TO DECEMBER 31, 2012

AND

FOR THE YEAR JANUARY 1, 2013 TO DECEMBER 31, 2013

Schoenfish & Co., Inc.

CERTIFIED PUBLIC ACCOUNTANTS

P.O. Box 247

105 EAST MAIN, PARKSTON, SOUTH DAKOTA 57366

MUNICIPALITY OF MONTROSE

MUNICIPAL OFFICIALS
DECEMBER 31, 2013

MAYOR:

Doris Sager

GOVERNING BOARD:

Karla Hopkins – President
Peggy Jesse – Vice-President
Jessica Rowley
Lenice Wingen

FINANCE OFFICER:

Linda Hentges

ATTORNEY:

Jerry Lammers

Schoenfish & Co., Inc.

CERTIFIED PUBLIC ACCOUNTANTS

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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

Governing Board
Municipality of Montrose
Montrose, 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 modified cash basis of accounting financial statements of the governmental activities, the business-type activities, and each major fund of the Municipality of Montrose, South Dakota (Municipality), as of December 31, 2013 and for each of the years in the biennial period then ended, and the related notes to the financial statements, which collectively comprise the Municipality's basic financial statements and have issued our report thereon dated June 10, 2014, which was qualified for the business-type activities and the water fund because interfund services were not recorded and was qualified for all opinion units because interest was not recorded in the fund making the investment.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Municipality'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 Municipality's internal control. Accordingly, we do not express an opinion on the effectiveness of the Municipality'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 Current Audit Findings and Questioned Costs, we identified certain deficiencies in internal control that we consider to be material weaknesses.

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 combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Municipality'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 Current Audit Findings and Questioned Costs as item 2013-001 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Municipality's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws,

regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Municipality's Response to Findings

The Municipality's response to the finding identified in our audit is described in the accompanying Schedule of Current Audit Findings and Questioned Costs. The Municipality's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

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 Municipality'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. As required by South Dakota Codified Law 4-11-11, this report is a matter of public record and its distribution is not limited.



Schoenfish & Co., Inc.
Certified Public Accountants
June 10, 2014

Schoenfish & Co., Inc.

CERTIFIED PUBLIC ACCOUNTANTS
P.O. Box 247
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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR
FEDERAL PROGRAM AND REPORT ON INTERNAL CONTROL
OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

Governing Board
Municipality of Montrose
Montrose, South Dakota

Report on Compliance for Each Major Federal Program

We have audited the Municipality of Montrose, South Dakota (Municipality) compliance with the types of compliance requirements described in the *U. S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the Municipality's major federal programs for the biennial period ended December 31, 2013. The Municipality's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Current Audit Findings and Questioned Costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the Municipality's major federal programs 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 OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of 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 Municipality's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination on the Municipality's compliance.

Opinion on Each Major Federal Program

In our opinion, the Municipality of Montrose complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the biennial period ended December 31, 2013.

Report on Internal Control Over Compliance

Management of the Municipality is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Municipality's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, 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 Municipality's internal control over compliance.

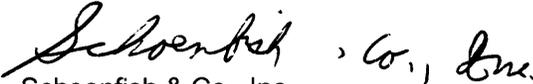
Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, and therefore, material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

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 combination of deficiencies, in internal control over compliance, such that there is reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies in internal control over compliance described in the accompanying Schedule of Current Audit Findings and Questioned Costs as item 2013-001 to be a material weakness.

The Municipality's response to the noncompliance finding identified in our audit is described in the accompanying Schedule of Current Audit Findings and Questioned Costs. The Municipality's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Purpose of this Report

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 OMB Circular A-133. Accordingly, this report is not suitable for any other purposes. As required by South Dakota Codified Law 4-11-11, this report and our report on compliance for each major federal program are matters of public record and their distribution is not limited.


Schoenfish & Co., Inc.
Certified Public Accountants
June 10, 2014

Schoenfish & Co., Inc.

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SCHEDULE OF PRIOR AUDIT FINDINGS

PRIOR AUDIT FINDINGS:

Finding Number 2011-01:

A material weakness in internal controls was noted due to a lack of proper segregation of duties for revenues. This comment has not been corrected and is restated as current audit finding number 2013-001.

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SCHEDULE OF CURRENT AUDIT FINDINGS AND QUESTIONED COSTSSummary of the Independent Auditor's Results:Financial Statements:

- a. A qualified opinion on the financial statements of each opinion unit was issued because interest was not recorded in the fund making the investment and a qualified opinion was issued for the business-type activities and the water fund because interfund services were not recorded.
- b. A material weakness was disclosed by our audit of the financial statements for internal control and record keeping as discussed in finding number 2013-001.
- c. Our audit did not disclose any noncompliance which was material to the financial statements.

Federal Awards:

- d. A material weakness was disclosed for internal control over major federal programs for a lack of segregation of duties affecting the reporting compliance requirement category as discussed in finding number 2013-001.
- e. An unqualified opinion was issued on compliance with the requirements applicable to major programs.
- f. Our audit disclosed audit findings that need to be disclosed in accordance with the Office of Management and Budget Circular A-133, Section .510(a). See finding number 2013-001.
- g. The federal awards tested as major programs were:
 1. Capitalization Grants for Clean Water State Revolving Funds (Recovery Act) CFDA No. 66.458
 2. Capitalization Grants for Drinking Water State Revolving Funds (Recovery Act) CFDA No. 66.468
- h. The dollar threshold used to distinguish between Type A and Type B federal award programs was \$300,000.
- i. The Municipality of Montrose did not qualify as a low-risk auditee.

CURRENT FEDERAL AUDIT FINDINGS:Internal Control – Related Finding – Material Weakness:Finding Number 2013-001:

A material weakness in internal controls was noted due to a lack of proper segregation of duties for revenues. This comment affects the reporting compliance requirement for Capitalization Grants for Clean Water State Revolving Funds (Recovery Act), CFDA No. 66.458 and Capitalization Grants for Drinking Water State Revolving Funds (Recovery Act), CFDA No. 66.468. This is the fifth consecutive audit in which this comment has occurred.

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SCHEDULE OF CURRENT AUDIT FINDINGS AND QUESTIONED COSTS
(Continued)

Criteria:

Proper segregation of duties results in increased reliability of reported financial data and decreased potential for the loss of public assets.

Condition:

The Finance Officer processes all revenue transactions from beginning to end. The Finance Officer also receives money, issues receipts, records receipts, posts receipts in the accounting records, prepares bank deposits, reconciles bank statements, and prepares financial statements.

Effect:

As a result, there is an increased likelihood that errors could occur and not be detected in a timely manner by employees in the ordinary course of performing their duties.

Recommendation:

1. We recommend that the Municipality of Montrose officials be cognizant of this lack of segregation of duties for revenues and attempt to provide compensating internal controls whenever, and wherever, possible and practical.

Corrective Action Plan:

The Municipality of Montrose Mayor, Doris Sager, is the contact person responsible for the corrective action plan for this comment. This comment is due to the size of the Municipality of Montrose, which precludes staffing at a level sufficient to provide an ideal environment for internal controls. We are aware of this problem and are attempting to provide compensating controls.

CURRENT OTHER AUDIT FINDINGS:

There are no current other audit findings to report except for the findings presented in Current Federal Audit Finding Number 2013-001.

CLOSING CONFERENCE

The audit findings were discussed with the officials during the course of the audit and with the Mayor and Finance Officer on May 30, 2014.

Schoenfish & Co., Inc.

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INDEPENDENT AUDITOR'S REPORT

Governing Board
Municipality of Montrose
Montrose, South Dakota

Report on the Financial Statements

We have audited the accompanying modified cash basis of accounting financial statements of the governmental activities, the business-type activities, and each major fund of the Municipality of Montrose, South Dakota, (Municipality) as of December 31, 2013 and for each of the years in the biennial period then ended, and the related notes to the financial statements, which collectively comprise the Municipality's basic financial statements as listed in the Table of Contents.

Management's Responsibility for the Financial Statements

The Municipality's 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.c.; 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 responsible for the design, implementation, and maintenance of internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error.

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Municipality'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 Municipality's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Basis for Qualified Opinions

The Municipality does not record the amounts of interfund services provided and used. We were unable to determine if these amounts are material.

Interest income for funds other than the General Fund was not recognized in the fund reporting the investment. The amounts of this subject are not reasonably determinable.

Qualified Opinions

In our opinion, except for the effects, if any, of the items reported in previous paragraphs, the financial statements referred to above present fairly, in all material respects, the respective financial position, modified cash basis, of the business-type activities and the water fund of the Municipality of Montrose as of December 31, 2013, and the respective changes in financial position and cash flows, modified cash basis, where applicable, thereof for each of the years in the biennial period then ended in conformity with the modified cash basis of accounting described in Note 1.c to the financial statements.

In addition, in our opinion, except for the effects, if any, of not reporting interest income in the proper funds, the financial statements referred to above present fairly, in all material respects, the respective financial position, modified cash basis, of the governmental activities and each major fund, except the water fund, of the Municipality of Montrose as of December 31, 2013, and the respective changes in financial position, modified cash basis, where applicable, thereof for each of the years in the biennial period then ended in conformity with the modified cash basis of accounting described in Note 1.c to the financial statements.

Basis of Accounting

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

Other Matters

Supplementary Information

Our audit was conducted for the purpose of forming opinions on the modified cash basis of accounting financial statements that collectively comprise the Municipality's basic financial statements. The Schedule of Expenditures of Federal Awards, which as required by the U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, the Budgetary Comparison Schedules, and the Schedule of Long-Term Debt listed in the Table of Contents are presented for purposes of additional analysis and are not a required part of the basic 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

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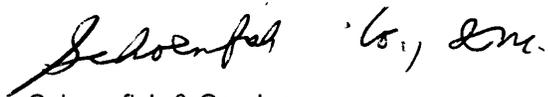
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information is fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated June 10, 2014 on our consideration of the Municipality's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Municipality's internal control over financial reporting and compliance.



Schoenfish & Co., Inc.
Certified Public Accountants
June 10, 2014

Schoenfish & Co., Inc.

CERTIFIED PUBLIC ACCOUNTANTS

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MUNICIPALITY OF MONTROSE
STATEMENT OF NET ASSETS - MODIFIED CASH BASIS
December 31, 2013

	Primary Government		Total
	Governmental Activities	Business-Type Activities	
ASSETS:			
Cash and Cash Equivalents	519,182.93	30,545.76	549,728.69
Investments	271,613.55	105,050.73	376,664.28
TOTAL ASSETS	790,796.48	135,596.49	926,392.97
NET POSITION:			
Unrestricted	790,796.48	135,596.49	926,392.97
TOTAL NET POSITION	790,796.48	135,596.49	926,392.97

The notes to the financial statements are an integral part of this statement.

MUNICIPALITY OF MONTROSE
STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS
For the Year Ended December 31, 2013

Functions/Programs	Expenses	Program Revenues		Net (Expense) Revenue and Changes in Net Position			
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Government		
					Governmental Activities	Business-Type Activities	Total
Primary Government:							
Governmental Activities:							
General Government	83,587.72	10,572.72			(73,015.00)		(73,015.00)
Public Safety	25,242.20				(25,242.20)		(25,242.20)
Public Works	119,046.42	36,241.89	19,556.22	982.26	(62,266.05)		(62,266.05)
Culture and Recreation	93,314.65	18,325.34			(74,989.31)		(74,989.31)
Conservation and Development	90,588.73	93,454.60			2,865.87		2,865.87
Miscellaneous Expenditures		5,400.05			5,400.05		5,400.05
Total Governmental Activities	411,779.72	163,994.60	19,556.22	982.26	(227,246.64)		(227,246.64)
Business-type Activities:							
Water	69,250.28	79,299.15	1,000.00			11,048.87	11,048.87
Sewer	47,527.44	71,968.61				24,441.17	24,441.17
Total Business-Type Activities	116,777.72	151,267.76	1,000.00	0.00		35,490.04	35,490.04
Total Primary Government	528,557.44	315,262.36	20,556.22	982.26	(227,246.64)	35,490.04	(191,756.60)
General Revenues:							
Taxes:							
Property Taxes					104,085.58		104,085.58
Sales Taxes					69,264.10		69,264.10
State Shared Revenues					3,263.64		3,263.64
Unrestricted Investment Earnings					2,856.03		2,856.03
Debt Issued						14,448.00	14,448.00
Miscellaneous Revenue					5,319.67		5,319.67
Transfers					49,421.01	(49,421.01)	0.00
Total General Revenues and Transfers					234,210.03	(34,973.01)	199,237.02
Change in Net Position					6,963.39	517.03	7,480.42
Net Position - Beginning					783,833.09	135,079.46	918,912.55
NET POSITION - ENDING					790,796.48	135,596.49	926,392.97

The notes to the financial statements are an integral part of this statement.

MUNICIPALITY OF MONTROSE
BALANCE SHEET - MODIFIED CASH BASIS
GOVERNMENTAL FUNDS
December 31, 2013

	<u>General Fund</u>
ASSETS:	
Cash and Cash Equivalents	519,182.93
Investments	<u>271,613.55</u>
 TOTAL ASSETS	 <u><u>790,796.48</u></u>
 FUND BALANCES:	
Unassigned	<u>790,796.48</u>
 TOTAL FUND BALANCES	 <u><u>790,796.48</u></u>

The notes to the financial statements are an integral part of this statement.

MUNICIPALITY OF MONTROSE
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCES - MODIFIED CASH BASIS
GOVERNMENTAL FUNDS
For the Year Ended December 31, 2013

	General Fund
Revenues:	
Taxes:	
General Property Taxes	103,485.15
General Sales and Use Taxes	69,264.10
Amusement Tax	72.00
Penalties & Interest on Delinquent Taxes	528.43
Total Taxes	173,349.68
Licenses and Permits	632.72
Intergovernmental Revenue:	
State Shared Revenue:	
Bank Franchise Tax	227.44
Liquor Tax Reversion	3,036.20
Motor Vehicle Licenses	6,220.67
Local Government Highway and Bridge Fund	10,785.34
County Shared Revenue:	
County Road Tax	454.53
County Wheel Tax	2,095.68
Total Intergovernmental Revenue	22,819.86
Charges for Goods and Services:	
Sanitation	36,241.89
Culture and Recreation	18,325.34
Day Care Fees	93,454.60
Total Charges for Goods and Services	148,021.83
Miscellaneous Revenue:	
Investment Earnings	2,856.03
Rentals	9,940.00
Special Assessments	982.26
Liquor Operating Agreement Income	5,400.05
Other	5,319.67
Total Miscellaneous Revenue	24,498.01
Total Revenue	369,322.10

The notes to the financial statements are an integral part of this statement.

MUNICIPALITY OF MONTROSE
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCES - MODIFIED CASH BASIS
GOVERNMENTAL FUNDS
For the Year Ended December 31, 2013

	General Fund
Expenditures:	
General Government:	
Legislative	30,873.17
Elections	30.79
Financial Administration	38,926.95
Other	13,756.81
Total General Government	83,587.72
Public Safety:	
Police	16,120.20
Fire	9,122.00
Total Public Safety	25,242.20
Public Works:	
Highways and Streets	84,810.22
Sanitation	34,236.20
Total Public Works	119,046.42
Culture and Recreation:	
Recreation	33,854.97
Parks	26,172.85
Total Culture and Recreation	60,027.82
Conservation and Development:	
Economic Opportunity - Day Care Centers	90,588.73
Total Conservation and Development	90,588.73
Capital Outlay	33,286.83
Total Expenditures	411,779.72
Excess Revenue Over (Under) Expenditures	(42,457.62)
Other Financing Sources (Uses):	
Transfers In	49,421.01
Total Other Financing Sources (Uses)	49,421.01
Net Change in Fund Balance	6,963.39
Fund Balance - Beginning	783,833.09
FUND BALANCE - ENDING	790,796.48

The notes to the financial statements are an integral part of this statement.

MUNICIPALITY OF MONTROSE
STATEMENT OF NET POSITION - MODIFIED CASH BASIS
PROPRIETARY FUNDS
December 31, 2013

	<u>Enterprise Funds</u>		<u>Totals</u>
	<u>Water Fund</u>	<u>Sewer Fund</u>	
ASSETS:			
Current Assets:			
Cash and Cash Equivalents		30,545.76	30,545.76
Investments	31,720.70	73,330.03	105,050.73
Total Current Assets	<u>31,720.70</u>	<u>103,875.79</u>	<u>135,596.49</u>
 TOTAL ASSETS	 <u>31,720.70</u>	 <u>103,875.79</u>	 <u>135,596.49</u>
 NET POSITION:			
Unrestricted	<u>31,720.70</u>	<u>103,875.79</u>	<u>135,596.49</u>
 TOTAL NET POSITION	 <u><u>31,720.70</u></u>	 <u><u>103,875.79</u></u>	 <u><u>135,596.49</u></u>

The notes to the financial statements are an integral part of this statement.

MUNICIPALITY OF MONTROSE
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN
FUND NET POSITION - MODIFIED CASH BASIS
PROPRIETARY FUNDS
For the Year Ended December 31, 2013

	Enterprise Funds		Totals
	Water Fund	Sewer Fund	
Operating Revenue:			
Charges for Goods and Services	31,848.35	29,190.65	61,039.00
Revenue Dedicated to Servicing Debt	47,450.80	41,520.91	88,971.71
Miscellaneous		1,257.05	1,257.05
Total Operating Revenue	79,299.15	71,968.61	151,267.76
Operating Expenses:			
Personal Services	6,815.72	3,344.98	10,160.70
Other Current Expense	8,940.89	16,300.62	25,241.51
Materials	35,265.45		35,265.45
Total Operating Expenses	51,022.06	19,645.60	70,667.66
Operating Income (Loss)	28,277.09	52,323.01	80,600.10
Nonoperating Revenue (Expense):			
Operating Grants	1,000.00		1,000.00
Debt Service (Principal)	(2,998.56)	(10,969.96)	(13,968.52)
Interest Expense	(15,229.66)	(16,911.88)	(32,141.54)
Long-Term Debt Issued	14,448.00		14,448.00
Total Nonoperating Revenue (Expense)	(2,780.22)	(27,881.84)	(30,662.06)
Income (Loss) Before Transfers	25,496.87	24,441.17	49,938.04
Transfers Out	(25,323.26)	(24,097.75)	(49,421.01)
Change in Net Position	173.61	343.42	517.03
Net Position - Beginning	31,547.09	103,532.37	135,079.46
NET POSITION - ENDING	31,720.70	103,875.79	135,596.49

The notes to the financial statements are an integral part of this statement.

MUNICIPALITY OF MONTROSE
STATEMENT OF NET ASSETS - MODIFIED CASH BASIS
December 31, 2012

	Primary Government		
	Governmental Activities	Business-Type Activities	Total
ASSETS:			
Cash and Cash Equivalents	513,973.68	30,499.46	544,473.14
Investments	269,859.41	104,580.00	374,439.41
TOTAL ASSETS	783,833.09	135,079.46	918,912.55
NET POSITION:			
Unrestricted	783,833.09	135,079.46	918,912.55
TOTAL NET POSITION	783,833.09	135,079.46	918,912.55

The notes to the financial statements are an integral part of this statement.

MUNICIPALITY OF MONTROSE
STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS
For the Year Ended December 31, 2012

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Position		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-Type Activities	Total
Primary Government:							
Governmental Activities:							
General Government	88,444.85	11,161.50	458.34		(76,825.01)		(76,825.01)
Public Safety	40,185.14				(40,185.14)		(40,185.14)
Public Works	105,713.23	36,759.16	18,807.47	1,665.79	(48,480.81)		(48,480.81)
Health and Welfare	200.00				(200.00)		(200.00)
Culture and Recreation	49,305.17	15,652.76			(33,652.41)		(33,652.41)
Conservation and Development	94,611.31	99,560.68			4,949.37		4,949.37
Miscellaneous Expenditures		5,276.19			5,276.19		5,276.19
Total Governmental Activities	378,459.70	168,410.29	19,265.81	1,665.79	(189,117.81)		(189,117.81)
Business-type Activities:							
Water	1,204,415.54	83,397.29		257,500.00		(863,518.25)	(863,518.25)
Sewer	550,417.05	69,021.67				(481,395.38)	(481,395.38)
Total Business-Type Activities	1,754,832.59	152,418.96	0.00	257,500.00		(1,344,913.63)	(1,344,913.63)
Total Primary Government	2,133,292.29	320,829.25	19,265.81	259,165.79	(189,117.81)	(1,344,913.63)	(1,534,031.44)
General Revenues:							
Taxes:							
Property Taxes					102,255.63		102,255.63
Sales Taxes					80,138.64		80,138.64
State Shared Revenues					3,293.78		3,293.78
Unrestricted Investment Earnings					4,229.94		4,229.94
Debt Issued						1,448,790.00	1,448,790.00
Miscellaneous Revenue					3,100.81	570.87	3,671.68
Transfers					85,115.94	(85,115.94)	0.00
Total General Revenues and Transfers					278,134.74	1,364,244.93	1,642,379.67
Change in Net Position					89,016.93	19,331.30	108,348.23
Net Position - Beginning					694,816.16	115,748.16	810,564.32
NET POSITION - ENDING					783,833.09	135,079.46	918,912.55

The notes to the financial statements are an integral part of this statement.

MUNICIPALITY OF MONTROSE
BALANCE SHEET - MODIFIED CASH BASIS
GOVERNMENTAL FUNDS
December 31, 2012

	General Fund
ASSETS:	
Cash and Cash Equivalents	513,973.68
Investments	<u>269,859.41</u>
 TOTAL ASSETS	 <u><u>783,833.09</u></u>
 FUND BALANCES:	
Unassigned	<u>783,833.09</u>
 TOTAL FUND BALANCES	 <u><u>783,833.09</u></u>

The notes to the financial statements are an integral part of this statement.

MUNICIPALITY OF MONTROSE
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCES - MODIFIED CASH BASIS
GOVERNMENTAL FUNDS
For the Year Ended December 31, 2012

	<u>General Fund</u>
Revenues:	
Taxes:	
General Property Taxes	101,858.70
General Sales and Use Taxes	80,138.64
Amusement Tax	60.00
Penalties & Interest on Delinquent Taxes	336.93
Total Taxes	182,394.27
Licenses and Permits	667.00
Intergovernmental Revenue:	
Federal Grants	458.34
State Shared Revenue:	
Bank Franchise Tax	232.33
Liquor Tax Reversion	3,061.45
Motor Vehicle Licenses	5,724.34
Local Government Highway and Bridge Fund	10,576.70
County Shared Revenue:	
County Road Tax	454.53
County Wheel Tax	2,051.90
Total Intergovernmental Revenue	22,559.59
Charges for Goods and Services:	
Sanitation	36,759.16
Culture and Recreation	15,652.76
Day Care Fees	99,560.68
Total Charges for Goods and Services	151,972.60
Miscellaneous Revenue:	
Investment Earnings	4,229.94
Rentals	10,494.50
Special Assessments	1,665.79
Liquor Operating Agreement Income	5,276.19
Other	3,100.81
Total Miscellaneous Revenue	24,767.23
Total Revenue	382,360.69

The notes to the financial statements are an integral part of this statement.

MUNICIPALITY OF MONTROSE
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCES - MODIFIED CASH BASIS
GOVERNMENTAL FUNDS
For the Year Ended December 31, 2012

	General Fund
Expenditures:	
General Government:	
Legislative	14,568.41
Financial Administration	37,809.77
Other	36,066.67
Total General Government	88,444.85
Public Safety:	
Police	16,120.20
Fire	24,064.94
Total Public Safety	40,185.14
Public Works:	
Highways and Streets	73,135.86
Sanitation	32,577.37
Total Public Works	105,713.23
Health and Welfare:	
Health	200.00
Total Health and Welfare	200.00
Culture and Recreation:	
Recreation	34,149.93
Parks	15,155.24
Total Culture and Recreation	49,305.17
Conservation and Development:	
Economic Opportunity - Day Care Centers	94,611.31
Total Conservation and Development	94,611.31
Total Expenditures	378,459.70
Excess Revenue Over (Under) Expenditures	3,900.99
Other Financing Sources (Uses):	
Transfers In	85,115.94
Total Other Financing Sources (Uses)	85,115.94
Net Change in Fund Balance	89,016.93
Fund Balance - Beginning	694,816.16
FUND BALANCE - ENDING	783,833.09

The notes to the financial statements are an integral part of this statement.

MUNICIPALITY OF MONTROSE
STATEMENT OF NET POSITION - MODIFIED CASH BASIS
PROPRIETARY FUNDS
December 31, 2012

	Enterprise Funds		Totals
	Water Fund	Sewer Fund	
ASSETS:			
Current Assets:			
Cash and Cash Equivalents		30,499.46	30,499.46
Investments	31,547.09	73,032.91	104,580.00
Total Current Assets	31,547.09	103,532.37	135,079.46
 TOTAL ASSETS	 31,547.09	 103,532.37	 135,079.46
 NET POSITION:			
Unrestricted	31,547.09	103,532.37	135,079.46
 TOTAL NET POSITION	 31,547.09	 103,532.37	 135,079.46

The notes to the financial statements are an integral part of this statement.

MUNICIPALITY OF MONTROSE
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN
FUND NET POSITION - MODIFIED CASH BASIS
PROPRIETARY FUNDS
For the Year Ended December 31, 2012

	Enterprise Funds		Totals
	Water Fund	Sewer Fund	
Operating Revenue:			
Charges for Goods and Services	37,919.34	27,122.62	65,041.96
Revenue Dedicated to Servicing Debt	45,477.95	41,899.05	87,377.00
Miscellaneous	570.87		570.87
Total Operating Revenue	83,968.16	69,021.67	152,989.83
Operating Expenses:			
Personal Services	12,220.64	4,938.47	17,159.11
Other Current Expense	13,662.39	8,367.98	22,030.37
Materials	40,613.15		40,613.15
Capital Assets	1,137,919.36	496,795.86	1,634,715.22
Total Operating Expenses	1,204,415.54	510,102.31	1,714,517.85
Operating Income (Loss)	(1,120,447.38)	(441,080.64)	(1,561,528.02)
Nonoperating Revenue (Expense):			
Debt Service (Principal)		(27,545.62)	(27,545.62)
Interest Expense		(12,769.12)	(12,769.12)
Long-Term Debt Issued	848,377.00	600,413.00	1,448,790.00
Total Nonoperating Revenue (Expense)	848,377.00	560,098.26	1,408,475.26
Income (Loss) Before Contributions and Transfers	(272,070.38)	119,017.62	(153,052.76)
Capital Contributions	257,500.00		257,500.00
Transfers In	14,883.74		14,883.74
Transfers Out		(99,999.68)	(99,999.68)
Change in Net Position	313.36	19,017.94	19,331.30
Net Position - Beginning	31,233.73	84,514.43	115,748.16
NET POSITION - ENDING	31,547.09	103,532.37	135,079.46

The notes to the financial statements are an integral part of this statement.

NOTES TO THE MODIFIED CASH BASIS FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

As discussed further in Note 1.c, these 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 Municipality of Montrose (Municipality) 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 except for fiduciary funds. The statements distinguish between governmental and business-type activities and discretely presented component units. 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 Municipality and for each function of the Municipality's governmental activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function. Program revenues include (a) charges paid by recipients of goods and services offered by the programs and (b) grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues.

Fund Financial Statements:

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

See Independent Auditor's Report.

NOTES TO THE MODIFIED CASH BASIS FINANCIAL STATEMENTS
(Continued)

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 Municipality financial reporting entity are described below:

Governmental Funds:

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

Proprietary Funds:

Enterprise Funds – Enterprise funds may be used to report any activity for which a fee is charged to external users for goods or services. Activities are required to be reported as enterprise funds if any one of the following criteria is met. Governments should apply each of these criteria in the context of the activity's principal revenue sources.

- a. The activity is financed with debt that is secured solely by a pledge of the net revenues from fees and charges of the activity. Debt that is secured by a pledge of net revenues from fees and charges and the full faith and credit of a related primary government or component unit—even if that government is not expected to make any payments—is not payable solely from fees and charges of the activity. (Some debt may be secured, in part, by a portion of its own proceeds but should be considered as payable "solely" from the revenues of the activity.)
- b. Laws or regulations require that the activity's costs of providing services, including capital costs (such as depreciation or debt service), be recovered with fees and charges, rather than with taxes or similar revenues.
- c. The pricing policies of the activity establish fees and charges designed to recover its costs, including capital costs (such as depreciation or debt service).

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.

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.

The Municipality's basis of accounting is the modified cash basis, which is a basis of accounting other than USGAAP. Under USGAAP, transactions are recorded in the accounts when revenues are earned and liabilities are incurred. Under the modified cash basis, transactions are recorded when cash is received or disbursed.

NOTES TO THE MODIFIED CASH BASIS FINANCIAL STATEMENTS
(Continued)

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 used, applied with the limitations of the modified cash basis of accounting.

Basis of Accounting:

In the Government-wide Statement of Net Position and Statement of Activities and the fund financial statements, governmental and business-type activities are presented using a modified cash basis of accounting.

The modified cash basis of accounting involves the measurement of cash and cash equivalents and changes in cash and cash equivalents resulting from cash receipt and disbursement transactions. Under the modified cash basis of accounting, transactions are recorded in the accounts when cash and/or cash equivalents are received or disbursed and assets and liabilities are recognized to the extent that cash has been received or disbursed. Acceptable modifications to the cash basis of accounting implemented by the Municipality in these financial statements are:

- a. Recording long-term investments in marketable securities (those with maturities more than 90-days (three months) from the date of acquisition) acquired with cash assets at cost.

As a result of the use of this modified cash basis of accounting, certain assets and their related revenues (such as accounts receivable and revenue for billed or provided services not yet collected) and certain liabilities and their related expenses (such as accounts payable and expenses for goods or services received but not yet paid, and accrued expenses and liabilities) are not recorded in these financial statements.

If the Municipality applied USGAAP, the fund financial statements for governmental funds would use the modified accrual basis of accounting, while the fund financial statements for proprietary fund types would use the accrual basis of accounting. All government-wide financial statements would be presented on the accrual basis of accounting.

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 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. Long-Term Liabilities:

Long-term liabilities include, but are not limited to, Revenue Bonds.

NOTES TO THE MODIFIED CASH BASIS FINANCIAL STATEMENTS
(Continued)

As discussed in Note 1c. above, the government-wide Statement of Net Position and Statement of Activities and the fund financial statements, governmental and business-type activities are presented using a modified cash basis of accounting. The Municipality has not elected to modify their cash basis presentation by recording long-term debt arising from cash transactions so any outstanding indebtedness is not reported on the financial statements of the Municipality. The Municipality does report the principal and interest payments on long-term debt as Debt Service expenditures on the Statement of Revenues, Expenditures and Changes in Fund Balances. On the Statement of Activities the principal portion of these Debt Service payments are reported within the appropriate expense function while the interest portion is reported as Interest on Long-Term Debt.

The Municipality has presented as Supplementary Information a Schedule of Changes in Long-Term Debt along with related notes that include details of any outstanding Long-Term Debt.

f. Revenue Received in Advance:

Under the modified cash basis of accounting, cash may have been received in advance of the Municipality's providing a good or service to a customer. These amounts are reported in the financial statements, as applicable.

g. Program Revenues:

Program revenues derive directly from the program itself or from parties other than the Municipality'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.

h. 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 and expenses.

i. Cash and Cash Equivalents:

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

NOTES TO THE MODIFIED CASH BASIS FINANCIAL STATEMENTS
(Continued)

j. Equity Classifications:

Government-wide Statements:

Equity is classified as net position and is displayed in one component.

1. Unrestricted net position – All other net position that do not meet the definition of "restricted" or "net investment in capital assets."

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.

k. Application of Net Position:

It is the Municipality'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.

l. Fund Balance Classification Policies and Procedures:

In accordance with Government Accounting Standards Board (GASB) No. 54, Fund Balance Reporting and Governmental Fund Type Definitions, the Municipality classifies governmental fund balances 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.
- 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 Finance Officer.
- Unassigned – includes positive fund balance within the General Fund which has not been classified within the above mentioned categories and negative fund balances in other governmental funds.

The Municipality 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 a grant agreement requiring dollar for dollar spending. Additionally, the Municipality would first use committed, then assigned, and lastly unassigned amounts for unrestricted fund balance when expenditures are made.

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

NOTES TO THE MODIFIED CASH BASIS FINANCIAL STATEMENTS
(Continued)

2. VIOLATIONS OF FINANCE-RELATED LEGAL AND CONTRACTUAL PROVISIONS:

The Municipality is prohibited by statute from spending in excess of appropriated amounts at the department level. The following represents the significant overdrafts to the disbursements compared to appropriations:

	<u>12/31/2013</u>	<u>12/31/2012</u>
General Fund:		
General Government - Other		\$ 15,966.67
Fire		\$ 14,054.94
Health		\$ 200.00
Parks	\$ 29,959.68	

The Municipality plans to take the following actions to address these violations: use contingency transfers and supplements when needed.

3. DEPOSITS AND INVESTMENTS, CREDIT RISK, CONCENTRATIONS OF CREDIT RISK AND INTEREST RATE RISK

The Municipality 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 Municipality'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 authorized to do business in South Dakota.

Deposits are reported at cost plus interest, if the account is of the add-on type.

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

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

Concentration of Credit Risk – The Municipality places no limit on the amount that may be invested in any one issuer.

NOTES TO THE MODIFIED CASH BASIS FINANCIAL STATEMENTS
(Continued)

Interest Rate Risk – The Municipality 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.

Assignment of Investment Income – State law allows income from deposits and investments to be credited to either the General Fund or the fund making the investment. The Municipality’s policy is to credit all income from investments to the General Fund.

4. 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 Municipality is permitted by several state statutes to levy varying amounts of taxes per \$1,000 of taxable valuation on taxable property in the Municipality.

5. SIGNIFICANT COMMITMENTS

The Municipality of Montrose entered into a forty year agreement with Kingbrook Rural Water System to provide water to the Municipality. A monthly service charge in the amount of \$1,080.00 is paid by the Municipality to Kingbrook Rural Water System along with a charge of \$2.25 per 1,000 gallons of water consumed over 760,000 gallons per month. The monthly service charge represents a contribution by the Municipality to aid Kingbrook Rural Water System in the construction of the facilities necessary to provide the Municipality with water. The Municipality will not acquire ownership of any of these water facilities through these payments. Payments are made from the Municipality's Water Fund.

6. INTERFUND TRANSFERS

Interfund transfers for the year ended December 31, 2013 were as follows:

<u>Transfers From:</u>	<u>Transfers to:</u> <u>General Fund</u>
Water Fund	\$ 25,323.26
Sewer Fund	24,097.75
	<u>\$ 49,421.01</u>

Interfund transfers for the year ended December 31, 2012 were as follows:

<u>Transfers From:</u>	<u>Transfers to:</u>		<u>Total</u>
	<u>General Fund</u>	<u>Water Fund</u>	
Sewer Fund	\$ 85,115.94	\$ 14,883.74	<u>\$ 99,999.68</u>

The Municipality typically budgets transfers to conduct the indispensable functions of the Municipality.

NOTES TO THE MODIFIED CASH BASIS FINANCIAL STATEMENTS
(Continued)

7. SIGNIFICANT CONTINGENCIES – LITIGATION

At December 31, 2013, the Municipality was not involved in any litigation.

8. RISK MANAGEMENT

The Municipality 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, 2013, the Municipality managed its risks as follows:

Liability Insurance:

The Municipality 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 Municipality'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 Municipality. The Municipality pays an annual premium, to provide liability coverage detailed below, under a claims-made policy and the premiums are accrued based on the ultimate cost of the experience to date of the SDPAA member, based on their exposure or type of coverage. The Municipality pays an annual premium to the pool to provide coverage for torts, theft or damage to real and personal property, along with errors and omissions of public officials. 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 Municipality would be eligible to receive a refund for the percentage of the amount allocated to the cumulative reserve fund on the following basis:

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

As of December 31, 2013, the Municipality has vested balance in the cumulative reserve fund of \$9,600.59. This amount is not reported on the modified cash basis financial statements.

The Municipality carries a \$250 deductible for the property coverage and \$0 deductible for the errors and omissions coverage.

The Municipality 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 during the past three years.

Workmen's Compensation:

The Municipality joined the South Dakota Municipal League Worker's Compensation Fund (Fund), a public entity risk pool currently operating as a common risk management and insurance program for South Dakota local government entities. The objective of the Fund is to formulate, develop, and administer, on behalf of the

NOTES TO THE MODIFIED CASH BASIS FINANCIAL STATEMENTS
(Continued)

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 Municipality'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 Municipality pays an annual premium, to provide worker's compensation coverage for its employees, under a retrospectively rated policy and the premiums are accrued based on the ultimate cost of the experience to date of the Fund members. Coverage limits are set by state statute. The pool pays the first \$650,000 of any claim per individual and has reinsurance which covers up to an additional \$2,000,000 per individual per incident.

The Municipality 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 during the past three years.

Unemployment Benefits:

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

SUPPLEMENTARY INFORMATION
MUNICIPALITY OF MONTROSE
BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS
GENERAL FUND
For the Year Ended December 31, 2013

	Budgeted Amounts		Actual Amounts (Budgetary Basis)	Variance with Final Budget - Positive (Negative)
	Original	Final		
Revenues:				
Taxes:				
General Property Taxes	104,500.00	104,500.00	103,485.15	(1,014.85)
General Sales and Use Taxes	70,000.00	70,000.00	69,264.10	(735.90)
Amusement Taxes	144.00	144.00	72.00	(72.00)
Penalties & Interest on Delinquent Taxes	250.00	250.00	528.43	278.43
Total Taxes	174,894.00	174,894.00	173,349.68	(1,544.32)
Licenses and Permits	750.00	750.00	632.72	(117.28)
Intergovernmental Revenue:				
State Shared Revenue:				
Bank Franchise Tax	220.00	220.00	227.44	7.44
Liquor Tax Reversion	3,000.00	3,000.00	3,036.20	36.20
Motor Vehicle Licenses	5,000.00	5,000.00	6,220.67	1,220.67
Local Government Highway and Bridge Fund	6,500.00	6,500.00	10,785.34	4,285.34
County Shared Revenue:				
County Road Tax	400.00	400.00	454.53	54.53
County Wheel Tax	2,000.00	2,000.00	2,095.68	95.68
Total Intergovernmental Revenue	17,120.00	17,120.00	22,819.86	5,699.86
Charges for Goods and Services:				
Sanitation	38,370.00	38,370.00	36,241.89	(2,128.11)
Culture and Recreation	28,250.00	28,250.00	18,325.34	(9,924.66)
Other - Day Care Fees	121,100.00	121,100.00	93,454.60	(27,645.40)
Total Charges for Goods & Services	187,720.00	187,720.00	148,021.83	(39,698.17)
Miscellaneous Revenue:				
Investment Earnings	6,000.00	6,000.00	2,856.03	(3,143.97)
Rentals	11,600.00	11,600.00	9,940.00	(1,660.00)
Special Assessments	0.00	0.00	982.26	982.26
Liquor Operating Agreement Income	4,015.00	4,015.00	5,400.05	1,385.05
Other	500.00	500.00	5,319.67	4,819.67
Total Miscellaneous Revenue	22,115.00	22,115.00	24,498.01	2,383.01
Total Revenue	402,599.00	402,599.00	369,322.10	(33,276.90)

SUPPLEMENTARY INFORMATION
MUNICIPALITY OF MONTROSE
BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS
GENERAL FUND
For the Year Ended December 31, 2013

	Budgeted Amounts		Actual Amounts (Budgetary Basis)	Variance with Final Budget - Positive (Negative)
	Original	Final		
Expenditures:				
General Government:				
Legislative	35,200.00	35,200.00	30,873.17	4,326.83
Contingency	20,000.00	20,000.00		
Amount Transferred		0.00		20,000.00
Elections	950.00	950.00	30.79	919.21
Financial Administration	42,047.00	42,047.00	38,926.95	3,120.05
Other	18,340.00	18,340.00	13,756.81	4,583.19
Total General Government	116,537.00	116,537.00	83,587.72	32,949.28
Public Safety:				
Police	16,125.00	16,125.00	16,120.20	4.80
Fire	10,400.00	10,400.00	9,122.00	1,278.00
Total Public Safety	26,525.00	26,525.00	25,242.20	1,282.80
Public Works:				
Highways and Streets	72,798.00	92,798.00	84,810.22	7,987.78
Sanitation	37,400.00	37,400.00	34,236.20	3,163.80
Total Public Works	110,198.00	130,198.00	119,046.42	11,151.58
Culture and Recreation:				
Recreation	34,250.00	34,250.00	33,854.97	395.03
Parks	29,500.00	29,500.00	59,459.68	(29,959.68)
Total Culture and Recreation	63,750.00	63,750.00	93,314.65	(29,564.65)
Conservation and Development:				
Economic Opportunity - Day Care Centers	114,626.00	114,626.00	90,588.73	24,037.27
Total Conservation and Development	114,626.00	114,626.00	90,588.73	24,037.27
Total Expenditures	431,636.00	451,636.00	411,779.72	39,856.28
Excess of Revenue Over (Under) Expenditures	(29,037.00)	(49,037.00)	(42,457.62)	6,579.38
Other Financing Sources (Uses):				
Transfers In	13,624.00	13,624.00	49,421.01	35,797.01
Total Other Financing Sources (Uses)	13,624.00	13,624.00	49,421.01	35,797.01
Net Change in Fund Balances	(15,413.00)	(35,413.00)	6,963.39	42,376.39
Fund Balance - Beginning	783,833.09	783,833.09	783,833.09	0.00
FUND BALANCE - ENDING	768,420.09	748,420.09	790,796.48	42,376.39

SUPPLEMENTARY INFORMATION
MUNICIPALITY OF MONTROSE
BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS
GENERAL FUND
For the Year Ended December 31, 2012

	Budgeted Amounts		Actual Amounts (Budgetary Basis)	Variance with
	Original	Final		Final Budget - Positive (Negative)
Revenues:				
Taxes:				
General Property Taxes	98,824.00	98,824.00	101,858.70	3,034.70
General Sales and Use Taxes	64,500.00	64,500.00	80,138.64	15,638.64
Amusement Taxes	144.00	144.00	60.00	(84.00)
Penalties & Interest on Delinquent Taxes	167.00	167.00	336.93	169.93
Total Taxes	<u>163,635.00</u>	<u>163,635.00</u>	<u>182,394.27</u>	<u>18,759.27</u>
Licenses and Permits	<u>850.00</u>	<u>850.00</u>	<u>667.00</u>	<u>(183.00)</u>
Intergovernmental Revenue:				
Federal Grants	0.00	0.00	458.34	458.34
State Shared Revenue:				
Bank Franchise Tax	220.00	220.00	232.33	12.33
Liquor Tax Reversion	2,750.00	2,750.00	3,061.45	311.45
Motor Vehicle Licenses	3,200.00	3,200.00	5,724.34	2,524.34
Local Government Highway and Bridge Fund	3,800.00	3,800.00	10,576.70	6,776.70
County Shared Revenue:				
County Road Tax	400.00	400.00	454.53	54.53
County Highway and Bridge Reserve Tax	4,000.00	4,000.00	0.00	(4,000.00)
County Wheel Tax	2,000.00	2,000.00	2,051.90	51.90
Total Intergovernmental Revenue	<u>16,370.00</u>	<u>16,370.00</u>	<u>22,559.59</u>	<u>6,189.59</u>
Charges for Goods and Services:				
Sanitation	38,270.00	38,270.00	36,759.16	(1,510.84)
Culture and Recreation	18,477.00	18,477.00	15,652.76	(2,824.24)
Other - Day Care Fees	123,076.00	123,076.00	99,560.68	(23,515.32)
Total Charges for Goods & Services	<u>179,823.00</u>	<u>179,823.00</u>	<u>151,972.60</u>	<u>(27,850.40)</u>
Miscellaneous Revenue:				
Investment Earnings	12,000.00	12,000.00	4,229.94	(7,770.06)
Rentals	12,350.00	12,350.00	10,494.50	(1,855.50)
Special Assessments	1,540.00	1,540.00	1,665.79	125.79
Liquor Operating Agreement Income	4,699.00	4,699.00	5,276.19	577.19
Other	0.00	0.00	3,100.81	3,100.81
Total Miscellaneous Revenue	<u>30,589.00</u>	<u>30,589.00</u>	<u>24,767.23</u>	<u>(5,821.77)</u>
Total Revenue	<u>391,267.00</u>	<u>391,267.00</u>	<u>382,360.69</u>	<u>(8,906.31)</u>

SUPPLEMENTARY INFORMATION
MUNICIPALITY OF MONTROSE
BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS
GENERAL FUND
For the Year Ended December 31, 2012

	Budgeted Amounts		Actual Amounts (Budgetary Basis)	Variance with Final Budget - Positive (Negative)
	Original	Final		
Expenditures:				
General Government:				
Legislative	15,200.00	15,200.00	14,568.41	631.59
Contingency	20,000.00	20,000.00		
Amount Transferred		0.00		20,000.00
Elections	950.00	950.00	0.00	950.00
Financial Administration	46,247.00	46,247.00	37,809.77	8,437.23
Other	20,100.00	20,100.00	36,066.67	(15,966.67)
Total General Government	<u>102,497.00</u>	<u>102,497.00</u>	<u>88,444.85</u>	<u>14,052.15</u>
Public Safety:				
Police	16,120.00	16,120.00	16,120.20	(0.20)
Fire	10,010.00	10,010.00	24,064.94	(14,054.94)
Total Public Safety	<u>26,130.00</u>	<u>26,130.00</u>	<u>40,185.14</u>	<u>(14,055.14)</u>
Public Works:				
Highways and Streets	80,736.00	80,736.00	73,135.86	7,600.14
Sanitation	37,400.00	37,400.00	32,577.37	4,822.63
Total Public Works	<u>118,136.00</u>	<u>118,136.00</u>	<u>105,713.23</u>	<u>12,422.77</u>
Health and Welfare:				
Health	0.00	0.00	200.00	(200.00)
Total Health and Welfare	<u>0.00</u>	<u>0.00</u>	<u>200.00</u>	<u>(200.00)</u>
Culture and Recreation:				
Recreation	37,925.00	37,925.00	34,149.93	3,775.07
Parks	30,400.00	30,400.00	15,155.24	15,244.76
Total Culture and Recreation	<u>68,325.00</u>	<u>68,325.00</u>	<u>49,305.17</u>	<u>19,019.83</u>
Conservation and Development:				
Economic Opportunity - Day Care Centers	122,166.00	122,166.00	94,611.31	27,554.69
Total Conservation and Development	<u>122,166.00</u>	<u>122,166.00</u>	<u>94,611.31</u>	<u>27,554.69</u>
Total Expenditures	<u>437,254.00</u>	<u>437,254.00</u>	<u>378,459.70</u>	<u>58,794.30</u>
Excess of Revenue Over (Under) Expenditures	<u>(45,987.00)</u>	<u>(45,987.00)</u>	<u>3,900.99</u>	<u>49,887.99</u>
Other Financing Sources (Uses):				
Transfers In	45,574.00	45,574.00	85,115.94	39,541.94
Transfers Out	(15,000.00)	(15,000.00)	0.00	15,000.00
Total Other Financing Sources (Uses)	<u>30,574.00</u>	<u>30,574.00</u>	<u>85,115.94</u>	<u>54,541.94</u>
Net Change in Fund Balances	<u>(15,413.00)</u>	<u>(15,413.00)</u>	<u>89,016.93</u>	<u>104,429.93</u>
Fund Balance - Beginning	<u>694,816.16</u>	<u>694,816.16</u>	<u>694,816.16</u>	<u>0.00</u>
FUND BALANCE - ENDING	<u>679,403.16</u>	<u>679,403.16</u>	<u>783,833.09</u>	<u>104,429.93</u>

NOTES TO THE SUPPLEMENTARY INFORMATION

Schedules of Budgetary Comparisons for the General Fund
and for each major Special Revenue Fund with a legally required budget.

Note 1. Budgets and Budgetary Accounting:

The Municipality followed 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 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 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. Unexpected appropriations lapse at year end unless encumbered by resolution of the Governing Board.

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.

The Municipality did not encumber any amounts at December 31, 2012 or December 31, 2013.

6. Formal budgetary integration is employed as a management control device during the year for the General Fund and special revenue funds.
7. Budgets for the General Fund and special revenue funds are adopted on a basis consistent with the modified cash basis of accounting.

NOTE 2. GAAP/Budgetary Accounting Basis Differences:

The Municipality's budgetary process accounts for certain transactions on a basis other than GAAP. The major differences between the budgetary basis and the GAAP basis lie in the manner in which revenues and expenditures are recorded. Under the budgetary basis, revenue and expenditures are recognized on a modified cash basis. Utilizing the modified cash basis, revenues are recorded when received in cash and expenditures are recorded when paid. Under the GAAP basis, revenues and expenditures are recorded on the modified accrual basis of accounting on the governmental fund statements and on the full accrual basis on the government-wide statements.

MUNICIPALITY OF MONTROSE
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Two Years Ended December 31, 2013

Federal Grantor/Pass-Through Grantor Program or Cluster Title	Federal CFDA Number	Expenditures	
		2012	2013
US Department of Housing and Urban Development: CDBG - State-Administered CDBG Cluster: Indirect Federal Funding: SD Governor's Office of Economic Development, Community Development Block Grant/State's Program and Non-Entitlement Grants in Hawaii	14.228	257,500.00	
Total US Department of Housing and Urban Development		257,500.00	0.00
US General Services Administration: Indirect Federal Funding: SD Federal Property Agency, Donation of Federal Surplus Personal Property (Note 4)	39.003	130.47	
Total US General Services Administration		130.47	0.00
US Environmental Protection Agency: Indirect Federal Funding: SD Department of Environment and Natural Resources, Capitalization Grants for Clean Water State Revolving Funds (ARRA) (Federal Portion) (Note 2) Capitalization Grants for Drinking Water State Revolving Funds (ARRA) (Federal Portion) (Note 2)	66.458 66.468	122,675.00 364,632.00	
Total US Environmental Protection Agency		487,307.00	0.00
US Department of Homeland Security: Indirect Federal Funding: SD Department of Public Safety, Office of Emergency Management, Emergency Management Performance Grants	97.042	458.34	
Total US Department of Homeland Security		458.34	0.00
GRAND TOTAL		745,395.81	0.00

Note 1: This accompanying schedule of expenditures of federal awards includes the federal grant activity of the municipality and is presented on the modified cash basis of accounting unless otherwise noted. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

Note 2: This represents a Major Federal Financial Assistance Program.

Note 3: The Municipality had the following loan balances outstanding at December 31, 2012 and 2013. The loan balances outstanding which have continuing compliance requirements are also included in the federal expenditures presented in the schedule.

Cluster/Program Title	Federal CFDA Number	Year Ending	Amount Outstanding	Included as Federal Expenditure on this Schedule
Capitalization Grants for Clean Water State Revolving Funds	66.458	12/31/2012	604,061.37	122,675.00
		12/31/2013	593,091.41	0.00
Capitalization Grants for Drinking Water State Revolving Funds	66.468	12/31/2012	284,207.00	364,632.00
		12/31/2013	286,048.44	0.00

Note 4: The amount reported represents 23.3% of the original acquisition cost of the federal surplus property received by the municipality.

SUPPLEMENTARY INFORMATION

LONG-TERM DEBT

A summary of changes in long-term debt follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Deletions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Primary Government:					
Business-Type Activities:					
Bonds Payable:					
Revenue - State Revolving Fund - Clean Water #1	24,816.99		24,816.99	0.00	0.00
Revenue - State Revolving Fund - Clean Water #2	166,777.00	600,413.00	174,098.59	593,091.41	13,048.53
Revenue - State Revolving Fund - Drinking Water #1	0.00	862,825.00	576,776.56	286,048.44	6,133.24
Total Primary Government	<u>191,593.99</u>	<u>1,463,238.00</u>	<u>775,692.14</u>	<u>879,139.85</u>	<u>19,181.77</u>

Debt payable at December 31, 2013, is comprised of the following:

Revenue Bonds:

State Revolving Fund Loan Program
Clean Water # 2, Maturity Date 1-15-2042,
Interest Rate 3.25%, Paid by Sewer Fund \$ 593,091.47

State Revolving Fund Loan Program
Drinking Water # 1, Maturity Date 4-15-2043,
Interest Rate 2.5%, Paid by Water Fund \$ 286,048.44

The annual requirements to amortize all debt outstanding as of December 31, 2013, are as follows:

Annual Requirements to Amortize Long-Term Debt December 31, 2013						
Year Ending Dec. 31,	Clean Water State Revolving Fund Loan Program # 2		Drinking Water State Revolving Fund Loan Program # 1		Totals	
	Principal	Interest	Principal	Interest	Principal	Interest
2014	13,048.53	19,117.51	6,133.24	8,512.88	19,181.77	27,630.39
2015	13,477.79	18,688.25	6,319.31	8,326.81	19,797.10	27,015.06
2016	13,921.20	18,244.84	6,511.04	8,135.08	20,432.24	26,379.92
2017	14,379.18	17,786.86	6,708.57	7,937.55	21,087.75	25,724.41
2018	14,852.23	17,313.81	6,912.11	7,734.01	21,764.34	25,047.82
2019-2023	81,919.84	78,910.36	37,836.34	35,394.26	119,756.18	114,304.62
2024-2028	96,311.21	64,518.99	43,934.96	29,295.64	140,246.17	93,814.63
2029-2033	113,230.79	47,599.41	51,016.57	22,214.03	164,247.36	69,813.44
2034-2038	133,122.74	27,707.46	59,239.64	13,990.96	192,362.38	41,698.42
2039-2043	98,827.90	5,711.73	61,436.66	4,470.88	160,264.56	10,182.61
Totals	<u>593,091.41</u>	<u>315,599.22</u>	<u>286,048.44</u>	<u>146,012.10</u>	<u>879,139.85</u>	<u>461,611.32</u>