

**CITY OF DEER RIVER
MINNESOTA**

FINANCIAL STATEMENTS

For the Year Ended December 31, 2018

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Independent Auditor's Report

To the Honorable Mayor and the
Members of the City Council
City of Deer River, MN

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Deer River, Minnesota as of and for the year ended December 31, 2018 and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to the 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 evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Deer River, Minnesota, as of December 31, 2018, and the respective changes in financial position and, where applicable, cash flows thereof and respective budgetary comparison for the general fund and all major special revenue funds for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 14 and the schedules of employer's share of net pension liability and employer contributions and notes on pages 50 through 53 and the schedule of changes in net pension asset and related ratio, city contributions and investment returns and notes on pages 54 and 55 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or prove any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Deer River's basic financial statements. The combining and individual fund statements and schedules are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The combining and individual fund statements and schedules 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 basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the 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 basic financial statements taken as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated June 18, 2019 on our consideration of the City of Deer River's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City of Deer River, Minnesota's internal control over financial reporting and compliance.

Sterle & Co, Ltd

June 18, 2019

CITY OF DEER RIVER, MINNESOTA
Management's Discussion and Analysis
Fiscal Year Ending December 31, 2018

As management of the City of Deer River, we offer readers of the City of Deer River's basic financial statements this narrative overview and analysis of the financial activities of the City as of and for the fiscal year ended December 31, 2018. We encourage readers to consider the information presented here in conjunction with the City's basic financial statements in the financial section of this report.

FINANCIAL HIGHLIGHTS FOR 2018

During 2018, the City approved street, water, and sewer infrastructure upgrades. Construction and engineering costs incurred through December 31, 2018 were in excess of \$2.9 million for the comprehensive project. The portion of the project that related to the water and sewer were transferred to those funds accordingly and is included in the \$1,586,275 reported as a transfer in the North/South capital projects fund in the accompanying financial statements.

To cover the costs of the project, the City issued GO Bonds in the amount of \$3,555,000. As of December 31, 2018, the City has \$739,333 set aside of the remaining bond proceeds for completion of the project in the upcoming year. The bond carries an interest rate of 3% to 4% and will have annual debt service payments ranging from \$80,000 to \$145,000 annually until maturity in February of 2048. The bond requires the City to finance the debt through special assessments levied upon the property specifically benefited by the improvement project and from ad valorem taxes levied.

The City also approved borrowing \$228,000 for the purchase of a new street sweeper. The GO Equipment Certificate of Indebtedness carries an interest rate of 2.95% and has a maturity date of February 1, 2033. Annual required debt service payments range from \$22,000 to \$28,000 until the debt is paid off.

The City's general fund continued to experience cash flow and operating short falls during 2018. Despite approving a budgeted surplus of \$3,111 for the year, the City is reporting an actual operating deficit of \$52,575 for the general fund. Several factors contributed to this deficit spending. One such factor was that the medical insurance pool in which the City was a member was discontinued. The City was forced to investigate other insurance plans and incurred additional costs during the conversion process. The City completed the construction of several sidewalks during the year under the Safe Route to School program in the amount of \$109,301 which is reported as capital outlay in the current year. The current year deficit increased the amount that the fund had to borrow in cash from the Municipal Forest fund to a balance of \$219,516 as of December 31, 2018. In addition, the general fund is reporting an unassigned deficit of \$268,250.

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The Fire fund experienced an increase in its fund balance of \$100,008 for the year ending with a total committed balance of \$534,679. Debt service payments were \$9,790 for the year.

The City continues to monitor the status of the community housing loan program (another major fund of the City). This is a loan forgiveness program which has eight years remaining until the final loan is eligible for forgiveness. The accompanying financial statements report \$526,625 in total loans outstanding with a deferred offset as of December 31, 2018. The City is not anticipating the recognition of cash flow from these loans as the loans most likely will meet the requirements for forgiveness as each year of occupancy passes.

The City's debt service fund reported \$44,950 in revenues through taxes and special assessments. \$43,661 was expended for debt service principal and interest payments. The accompanying statements reflect a transfer of \$66,836 to the fund as the allocable share of the bond issue costs that were incurred by the City for the issuance of the GO bonds during the year. The total proceeds of the bond were reported in the capital projects fund.

The City continues to increase the water and sewer fees in an effort to minimize the impact on the general fund tax levy. The City has been working on a replacement program and schedule to maintain the utility's distribution systems. For 2018, the water fund experienced a net operating loss of \$932 again due in part to water line breaks in the winter months. The sewer fund showed \$146,210 in net operating income primarily due to a one-time connection fee from a user of \$89,250 that was part of a new 28-unit senior facility constructed.

The license bureau also experienced additional increases in salary and benefits due to increased time working with the new MNLARS (a system mandated by the State of Minnesota) which was not a smooth conversion. As a result, the license bureau is reflecting a decrease in net assets of \$11,745. However, this was an improvement over the prior year operating loss reported of \$32,698.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis are intended to serve as an introduction to the City of Deer River's basic financial statements. The statements are comprised of three components:

1. Government-wide financial statements
2. Fund financial statements
3. Notes to the basic financial statements

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Management's Discussion and Analysis
Fiscal Year Ending December 31, 2018

Government-Wide Financial Statements

These statements are designed to provide readers with a broad overview of the City of Deer River's finances in a manner similar to private sector business.

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

The *statement of activities* presents information showing how Deer River's net position changed during the year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

Both of the government-wide financial statements distinguish functions of the City that are mainly supported by taxes and intergovernmental revenues (governmental activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the City of Deer River include general government, public safety, highways and streets, interest and other expenses. The major business type activities of the city include water, sewer, and the license bureau.

The government-wide financial statements can be found on pages 15 through 18 of this report.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City of Deer River utilizes fund accounting to demonstrate compliance with finance-related legal requirements. The funds of the City of Deer River are divided into two types: governmental and proprietary (enterprise) funds. The City's funds are described in more detail in the following paragraphs.

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

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Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements.

By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between the two.

The City of Deer River maintains eight individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the General Fund, Fire Department, Community Development Revolving Fund #2, Debt Service Fund, and North/South Capital Project funds which are considered to be major funds. Data from the other three funds are combined into a single aggregated presentation. Individual fund data for each of these non-major governmental funds is provided in the form of combining statements elsewhere in this report as supplementary information.

The City of Deer River adopts a one-year budget for its governmental funds. A budgetary comparison statement has been provided for the General Fund and all major special revenue funds in the basic financial statements.

The governmental funds financial statements can be found on pages 19 through 25 of this report.

Proprietary Funds: The City of Deer River maintains three (3) enterprise funds. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. Information is presented separately in the proprietary statement of net assets and the proprietary statement of revenues, expense and changes in fund net assets for the Water, Sewer, and License Bureau funds, which are considered major funds.

The proprietary funds financial statements can be found on pages 26 through 29 of this report.

Notes to the Basic Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the basic financial statements can be found on pages 30 through 49 of this report.

CITY OF DEER RIVER, MINNESOTA
Management's Discussion and Analysis
Fiscal Year Ending December 31, 2018

GOVERNMENT-WIDE FINANCIAL ANALYSIS

The City continues to present its financial statements under the reporting model required by GASB 34. The City has provided comparative data to the prior year to assist the readers in assessing the financial position of the city.

	Net Position December 31, 2018 and 2017					
	Govern- mental Activities 2018	Govern- mental Activities 2017	Business- type Activities 2018	Business- type Activities 2017	Total 2018	Total 2017
Current assets	\$ 1,693,505	793,774	\$ 160,107	201,161	\$ 1,853,612	994,935
Capital assets and other noncurrent assets	3,559,444	2,268,524	4,878,666	3,342,516	8,438,110	5,611,040
Deferred Outflows	360,762	627,078	40,478	67,063	401,240	694,141
Total assets and deferred outflows	<u>5,613,711</u>	<u>3,689,376</u>	<u>5,079,251</u>	<u>3,610,740</u>	<u>10,692,962</u>	<u>7,300,116</u>
Current liabilities	249,318	154,869	192,793	182,618	442,111	337,487
Long-term liabilities	4,227,331	619,338	1,264,052	1,413,881	5,491,383	2,033,219
Deferred Inflows	1,156,838	1,385,358	52,016	59,096	1,208,854	1,444,454
Total liabilities and deferred inflows	<u>5,633,487</u>	<u>2,159,565</u>	<u>1,508,861</u>	<u>1,655,595</u>	<u>7,142,348</u>	<u>3,815,160</u>
Net position:						
Net investment in capital						
Assets	(1,038,571)	1,406,891	3,593,179	1,90,4218	2,554,608	3,311,109
Restricted	999,556	191,779	-	-	999,556	191,779
Unrestricted	<u>19,239</u>	<u>(68,859)</u>	<u>(22,789)</u>	<u>50,927</u>	<u>(3,550)</u>	<u>(17,932)</u>
Total net position	<u>\$ (19,776)</u>	<u>1,529,811</u>	<u>\$ 3,570,390</u>	<u>1,955,145</u>	<u>\$ 3,550,614</u>	<u>3,484,956</u>

CITY OF DEER RIVER, MINNESOTA
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Changes in Net Assets						
Years Ended December 31, 2018 and 2017						
	Govern- mental	Govern- mental	Business- type	Business- type		
	Activities 2018	Activities 2017	Activities 2018	Activities 2017	Total 2018	Total 2017
Revenues						
Program Revenues						
Charges for services	\$ 248,693	246,393	\$ 649,867	521,647	\$ 898,560	768,040
Operating grants	118,063	132,704	-	-	118,063	132,704
Capital grants	-	-	-	-	-	-
General Revenues						
Property taxes	760,006	536,617	-	128,665	760,006	665,282
Intergovernmental aids	316,454	325,866	-	-	316,454	325,866
Investment earnings	3,726	1,559	-	-	3,726	1,559
Miscellaneous/Gain (Loss)	(4,437)	13,073	-	-	(4,437)	13,073
Total Revenues	1,442,505	1,256,212	649,867	650,312	2,092,372	1,906,524
Expenses						
General government	335,251	279,467	-	-	335,251	279,467
Public Safety	648,503	820,569	-	-	648,503	820,569
Highways and streets	250,673	263,708	-	-	250,673	263,708
Culture and recreation	53,004	53,574	-	-	53,004	53,574
Interest	137,083	6,410	-	-	137,083	6,410
Other	48,139	15,348	-	-	48,139	15,348
Water	-	-	233,611	221,602	233,611	221,602
Sewer	-	-	221,765	231,666	221,765	231,666
License Bureau	-	-	98,685	104,467	98,685	104,467
Total Expenses	1,472,653	1,439,076	554,061	557,735	2,026,714	1,996,811
Change in net position before transfers	\$ (30,148)	(182,864)	\$ 95,806	92,577	\$ 65,658	(90,287)

Governmental Activities. As noted earlier, net position serves as a useful indicator of financial position. As of December 31, 2018, liabilities and deferred inflows exceeded liabilities and deferred outflows by \$19,776. As discussed in the financial highlights section, this is a result of the City issuing \$3,783,000 in new debt for a street sweeper and infrastructure improvements to the City streets, water and sewer distribution systems. The debt is being carried in the City's governmental funds.

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However, the City transferred the respective costs of the water and sewer line upgrades to the enterprise funds according. As a result, the governmental activities are reporting a deficit of \$1,038,571 in investment net investment in capital assets.

Other significant noncurrent liabilities that are reported in the governmental activities statement of net position include \$192,930 for net pension liabilities and \$78,911 for compensated absences. Both of these along with the deferred inflows of resources of \$1,156,838 impact the overall net position of the City.

Business-Type Activities. Business-type activities increased the City's net position by \$95,806 before the \$1,519,439 transfer from the governmental activities for the water and sewer portions of the upgrades done on the North/South project and Highway 2 construction projects. The City raised user rates for both the water and sewer accordingly in prior years to assist with the costs. Also as noted in the financial highlights section, the City received a one-time user assessment of \$89,250 which helped the operating income for the sewer fund.

FINANCIAL ANALYSIS OF THE CITY'S MAJOR FUNDS

The City of Deer River uses fund accounting to ensure compliance with finance related legal requirements.

Governmental Funds: The purpose of the City's governmental fund financial statements is to provide information on revenues, expenditures and balances of spendable resources. This information is useful in assessing financing requirements. Unassigned fund balance may indicate Deer River's net resources available for spending at the end of the fiscal year.

As of December 31, 2018, the city's governmental funds reported combined ending fund balances of \$1,494,986, which is an increase of \$861,628 from December 31, 2017. Of this amount \$999,556 are restricted for community development revolving loans, debt service and TIF district dollars. Total committed funds by the Council amounted to \$763,680 for fire and the municipal forest operations. No unassigned funds are available for future operations for the governmental funds as a whole as of the end of 2018. Instead the City is reporting a \$268,250 deficit.

General Fund

The general fund is the city's chief operating fund. At the end of 2018, unassigned fund balance was a deficit of \$268,250. This was an increase in the deficit of \$52,575 for the year. As discussed in the financial highlights section, the City continued to experienced unbudgeted items in 2018 which once again impacted the governmental fund balances and has caused the City to experience a significant strain on its cash flow.

CITY OF DEER RIVER, MINNESOTA
Management's Discussion and Analysis
Fiscal Year Ending December 31, 2018

Fire Department Fund

The fire department fund saw an increase of \$100,008 as the City continues to receive fire fees and aids that cover the operational costs of the fire department.

Community Development Revolving Loan #2

The program within this fund was completed back in 2016 and continues to hold the notes receivable only. The City has \$526,625 of deferred loans it is holding that will be potentially forgiven each year as occupancy requirements are met. No revenues or expenses are reported in the fund.

Debt Service Fund

The debt service fund increased by \$68,125. \$44,950 was realized in taxes and special assessments while \$43,661 was paid out in scheduled debt payments.

North/South Capital Project Fund

The City opened a new capital projects fund in 2018 to account for the proceeds and uses of the \$3,555,000 GO Bond that was issued for the improvements to a section of the City's water, sewer, and street distribution system. The City realized net proceeds of \$3,504,165 from the issuance of the bonds. \$32,314 was expended in issuance costs. Total construction costs for the street portion was \$1,146,243 while \$1,586,275 was the estimated portion relating to the water and sewer. This was reflected as a transfer to those funds respectively. \$739,333 remains within that fund and is anticipated to be utilized in the upcoming year as the project is closed and finalized.

Other Non-Major Funds

Other non-major funds (consisting of the Municipal Forest Fund, the Community Development Revolving Fund, and the TIF District 1 Capital Projects fund) increased by \$6,737 primarily due to the revenue received in the municipal forest fund that exceeded the expenditures by \$6,418.

Proprietary (Enterprise) Funds: The City's enterprise funds provide the same type of information found in the government-wide financial statements, but in more detail.

Total net position at the end of the year were as follows:

- Water \$ 1,994,331
- Sewer \$ 1,654,448
- License Bureau \$ (78,389)

Generally, the net position in the water and sewer funds are a result of the City's investment in capital assets. The unrestricted, undesignated balances available for future operational costs are:

CITY OF DEER RIVER, MINNESOTA
Management's Discussion and Analysis
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- Water \$ 8,037
- Sewer \$ 48,489
- License Bureau \$ (79,315) deficit

The City had implemented rate increases in the water and sewer funds in the prior year which directly impacted the operations of each utility. The user fees were adequate to cover depreciation costs as well as absorb the impact of the GASB 68 increase in pension costs for the water and sewer utilities. Staff in the license bureau were eligible for compensated absences during the year, there were significant additional training costs due to implementation of a new reporting system to the State, and with the additional impact of GASB 68 pension increase, the fund once again reported a loss for the year of \$11,745 and ended with an overall deficit net position of \$78,389.

GENERAL FUND BUDGETARY HIGHLIGHTS

The General Fund budgeted expenditures for 2018 were \$1,149,219. Actual expenditures were \$1,378,863 therefore reflecting a variance of \$229,644 over the approved budget expenditures primarily due to the unbudgeted purchase of the new street sweeper for 214,901. In addition, actual revenues were under budgeted revenues by \$33,859 due to less than anticipated collections on several intergovernmental aids and other anticipated miscellaneous revenues. However, because the City issued a GO Equipment Certificate of Indebtedness for the street sweeper in the amount of \$228,000, it left the City with a net change of \$55,686 under the anticipated budget for the fund as a whole.

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Summary Analysis of General Fund Budget
Fiscal Year 2018

	Original Budget	Final Budget	Actual	Variance with Final Budget
Revenues				
Taxes	\$ 665,619	\$ 665,619	\$ 678,861	\$ 13,242
Special assessments	-	-	-	-
Licenses and permits	17,000	17,000	14,600	(2,400)
Intergovernmental	370,911	370,911	353,140	(17,771)
Charges for services	7,100	7,100	10,038	2,938
Fines and forfeitures	12,500	12,500	7,525	(4,975)
Other revenues	64,200	64,200	39,307	(24,893)
Total Revenues	1,137,330	1,137,330	1,103,471	(33,859)
Expenditures				
General government	322,983	322,983	315,593	7,390
Public safety	508,453	508,453	471,849	36,604
Highways and streets	242,604	242,604	210,114	32,490
Culture and recreation	50,029	50,029	44,393	5,636
Capital Outlay	25,150	25,150	336,914	(311,764)
Total Expenditures	1,149,219	1,149,219	1,378,863	(229,644)
Expenditures Over Revenues	(11,889)	(11,889)	(275,392)	(263,503)
Other Financing Sources	15,000	15,000	222,817	207,817
Excess of Revenues and Other Financing Sources Over Expenditures	\$ 3,111	\$ 3,111	\$ (52,575)	\$ (55,686)

The City did not modify the original budgets during the year.

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 Management's Discussion and Analysis
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CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets: The City's investments in capital assets for its governmental and business-type activities at December 31, 2018 amounts to \$7,909,094 (net of accumulated depreciation). This investment in capital assets includes land, buildings, improvements, distribution lines, automobiles, equipment, roads and infrastructure.

Capital Assets (Net of depreciation)
 December 31, 2018 and 2017

	Govern- mental Activities 2018	Govern- mental Activities 2017	Business- type Activities 2018	Business- type Activities 2017	Total 2018	Total 2017
Buildings	\$ 292,945	308,118	\$ 3,476	4,252	\$ 296,421	312,370
Land	437,393	437,393	21,000	21,000	458,393	458,393
Improvements	259,122	131,377	2,525,287	1,849,164	2,784,409	1,980,541
Machinery/Equipment	695,798	557,042	124,792	144,671	820,590	701,713
Infrastructure/ Distribution Systems	198,926	231,346	565,177	610,320	764,103	841,666
Work in process	<u>1,146,244</u>	-	<u>1,638,934</u>	<u>713,109</u>	<u>2,785,178</u>	<u>713,109</u>
	<u>\$ 3,030,428</u>	<u>1,665,276</u>	<u>\$ 4,878,666</u>	<u>3,342,516</u>	<u>\$ 7,909,094</u>	<u>5,007,792</u>

Major capital asset additions during 2018 included the following:

- Infrastructure costs in the water and sewer for the Hwy 2 project
- Infrastructure costs for the North/South project resulting in additions to the governmental funds for the street portion of \$1,146,243, water of \$927,436 and sewer of \$765,820
- Sidewalks/infrastructure under the Safe Route to Schools program of \$109,301
- A new street sweeper for \$214,901
- A lift crane for \$7,300
- Upgrades to the parking area at the fire hall for \$8,650
- Miscellaneous fire equipment including signs and a saw

Additional information on the City's capital assets can be found in Note 4 of the basic financial statements.

Long Term Debt: As of December 31, 2017, the city had total debt of \$1,673,780. The City had two new debt issues for \$3,783,000 and made principal payments of \$195,000. Therefore, debt payable at December 31, 2018 was \$5,261,780.

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Outstanding Debt
December 31, 2018 and 2017

	Governmental Activities 2018	Governmental Activities 2017	Business- type Activities 2018	Business- type Activities 2017	Total 2018	Total 2017
General Obligation	\$ 3,991,365	255,720	\$ 1,270,415	1,418,060	\$ 5,261,780	1,673,780

The governmental debt revenues are obtained through residential assessments and property tax. The business-type activity debt repayment funds are obtained through fees for service and property taxes. Additional long-term debt includes compensated absences and net pension liability accruals reflected of \$116,783 and \$427,170 respectively. Additional information on the City's debt can be found in Note 5 of the basic financial statements.

ECONOMIC FACTORS AND BUDGETS

The City of Deer River prepares its budgets on an annual basis. The departments are encouraged to bring future expenditure needs and requirements to the budget table. The City considers the following situations in the development of its budget:

- The City attempts to provide the same services it has to its citizens while being cognizant of keeping property taxes in line despite decreases of its state aid.
- The City continues to review the rate structures for the utilities to try to balance the costs (including depreciation) with the burden on the customers.
- The City also is continuing to work on capital project planning and has been working with the Minnesota Legislature to find possible funding sources for these planned projects. Without additional capital funding the City cannot actively seek developers because of the need for a fourth wastewater pond. The City does not have the funds to build the additional pond without a significant and detrimental impact to the taxpayers.

CONTACTING THE CITY'S FINANCE DEPARTMENT

This management's discussion and analysis is designed to provide citizens, taxpayers, customers, and investors and creditors with a general overview of the City's finances and to demonstrate the City's accountability for the money it receives. If you have questions or need additional financial information, please contact the City of Deer River's clerk at 218-246-8195.

CITY OF DEER RIVER, MINNESOTA

STATEMENT OF NET POSITION - GOVERNMENT-WIDE

December 31, 2018

	Primary Government		
	Governmental Activities	Business-type Activities	Total
Assets			
Current Assets			
Cash	\$ 1,613,449	\$ 106,403	\$ 1,719,852
Receivables			
Accounts	801	36,547	37,348
Unbilled revenues	-	17,157	17,157
Taxes	13,581	-	13,581
Special assessments	2,441	-	2,441
Unremitted taxes	16,320	-	16,320
Notes	442	-	442
Due from other governments	225	-	225
Allowance for uncollectible	(7,000)	-	(7,000)
Prepaid expenses	53,246	-	53,246
Total Current Assets	1,693,505	160,107	1,853,612
Noncurrent Assets			
Special assessments	1,467	-	1,467
Notes receivable	527,549	-	527,549
Capital assets (net of accumulated depreciation)	3,030,428	4,878,666	7,909,094
	3,559,444	4,878,666	8,438,110
Total Assets	5,252,949	5,038,773	10,291,722
Deferred Outflows of Resources			
Related to net pension liability	360,762	40,478	401,240
Total Assets and Deferred Outflows of Resources	\$ 5,613,711	\$ 5,079,251	\$ 10,692,962

(Continued)

CITY OF DEER RIVER, MINNESOTA

STATEMENT OF NET POSITION - GOVERNMENT-WIDE

December 31, 2018

	Primary Government		
	Governmental Activities	Business-type Activities	Total
Liabilities and Net Assets			
Current liabilities			
Current portion of long-term debt	\$ 35,875	\$ 141,905	\$ 177,780
Accounts payable	120,568	28,342	148,910
Accrued interest	77,634	15,072	92,706
Accrued payroll	2,611	654	3,265
Accrued compensated absences	12,630	6,820	19,450
Total Current Liabilities	249,318	192,793	442,111
Noncurrent liabilities			
Compensated absences	78,911	18,422	97,333
Net pension liability	192,930	117,120	310,050
Bonds and notes	3,955,490	1,128,510	5,084,000
Total Noncurrent Liabilities	4,227,331	1,264,052	5,491,383
Total Liabilities	4,476,649	1,456,845	5,933,494
Deferred Inflows of Resources			
Related to net pension liability	630,213	52,016	682,229
Notes receivable	526,625	-	526,625
Total Deferred Inflows of Resources	1,156,838	52,016	1,208,854
Net Position			
Net investment in capital assets	(1,038,571)	3,593,179	2,554,608
Restricted for			
Revolving Loan Fund	1,346	-	1,346
Debt Service Fund	244,292	-	244,292
TIF District Fund	14,585	-	14,585
North/South Project Fund	739,333	-	739,333
Unrestricted	19,239	(22,789)	(3,550)
Total Net Position	(19,776)	3,570,390	3,550,614
Total Liabilities, Deferred Inflows of Resources and Net Position	\$ 5,613,711	\$ 5,079,251	\$ 10,692,962

See accompanying notes and auditor's report.

CITY OF DEER RIVER, MINNESOTA

STATEMENT OF ACTIVITIES - GOVERNMENT-WIDE
For the Year Ended December 31, 2018

	Net (Expense) Revenue and Changes in Net Assets						
	Program Revenues				Primary Government		
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-type Activities	Total
Functions/Programs							
Primary Government							
Governmental activities							
General government	\$ 335,251	\$ 10,749	\$ 7,345	\$ -	\$ (317,157)	\$ -	\$ (317,157)
Public safety	648,503	224,678	109,318	-	(314,507)	-	(314,507)
Highways and streets	250,673	677	-	-	(249,996)	-	(249,996)
Culture and recreation	53,004	-	1,400	-	(51,604)	-	(51,604)
Debt service - interest	137,083	-	-	-	(137,083)	-	(137,083)
Other	48,139	12,589	-	-	(35,550)	-	(35,550)
Total governmental activities	1,472,653	248,693	118,063	-	(1,105,897)	-	(1,105,897)
Business-type activities							
Water	233,611	216,607	-	-	-	(17,004)	(17,004)
Sewer	221,765	346,320	-	-	-	124,555	124,555
License Bureau	98,685	86,940	-	-	-	(11,745)	(11,745)
Total business-type activities	554,061	649,867	-	-	-	95,806	95,806
Total Primary Government	\$ 2,026,714	\$ 898,560	\$ 118,063	\$ -	(1,105,897)	95,806	(1,010,091)

See accompanying notes and auditor's report.

(Continued)

CITY OF DEER RIVER, MINNESOTA

STATEMENT OF ACTIVITIES - GOVERNMENT-WIDE
For the Year Ended December 31, 2018

	Net (Expense) Revenue and Changes in Net Assets		
	Primary Government		
	Governmental Activities	Business-type Activities	Total
Continued from page 17	\$ (1,105,897)	\$ 95,806	\$ (1,010,091)
General Revenues			
Property taxes	760,006	-	760,006
Intergovernmental aids	316,454	-	316,454
Unrestricted interest earnings	3,726	-	3,726
Total general revenues	1,080,186	-	1,080,186
Other item - loss on disposal of capital items	(4,437)	-	(4,437)
Internal transfers	(1,519,439)	1,519,439	-
Change in Net Position	(1,549,587)	1,615,245	65,658
Net Position - Beginning of the Year	1,529,811	1,955,145	3,484,956
Net Position - End of the Year	\$ (19,776)	\$ 3,570,390	\$ 3,550,614

See accompanying notes and auditor's report.

CITY OF DEER RIVER, MINNESOTA

BALANCE SHEET - GOVERNMENTAL FUNDS

December 31, 2018

Major Funds

	General Fund	Fire Department Fund	Community Development Revolving Fund #2	Debt Service Fund	Capital Projects North/South Project	Total Other Non-Major Funds	Total Governmental Funds
Assets							
Cash	\$ -	\$ 536,550	\$ -	\$ 243,786	\$ 807,697	\$ 25,416	\$ 1,613,449
Receivables							
Accounts	768	33	-	-	-	-	801
Taxes	13,581	-	-	-	-	-	13,581
Special assessment	-	-	-	3,908	-	-	3,908
Unremitted taxes	14,702	677	-	941	-	-	16,320
Notes	-	-	526,625	-	-	1,366	527,991
Due from other governments	-	225	-	-	-	-	225
Due from other funds	-	-	-	-	-	219,516	219,516
Total Assets	\$ 29,051	\$ 537,485	\$ 526,625	\$ 248,635	\$ 807,697	\$ 246,298	\$ 2,395,791
Liabilities, Deferred Inflows of Resources, and Fund Balances							
Liabilities							
Accounts payable	\$ 48,963	\$ 2,806	\$ -	\$ 435	\$ 68,364	\$ -	\$ 120,568
Accrued payroll	2,611	-	-	-	-	-	2,611
Due to other funds	219,516	-	-	-	-	-	219,516
Compensated absences	12,630	-	-	-	-	-	12,630
Total Liabilities	283,720	2,806	-	435	68,364	-	355,325
Deferred Inflows of Resources							
Property taxes	13,581	-	-	-	-	-	13,581
Special assessments	-	-	-	3,908	-	-	3,908
Notes receivable	-	-	526,625	-	-	1,366	527,991
Total Deferred Inflows of Resources	13,581	-	526,625	3,908	-	1,366	545,480
Fund Balances							
Restricted - Debt Service	-	-	-	244,292	-	-	244,292
Restricted - Special Revenue (Housing)	-	-	-	-	739,333	1,346	1,346
Restricted - Capital Projects	-	-	-	-	-	14,585	14,585
Committed - Special Revenue (Fire)	-	534,679	-	-	-	-	534,679
Committed - Special Revenue (Municipal Forest)	-	-	-	-	-	229,001	229,001
Unassigned	(268,250)	-	-	-	-	-	(268,250)
Total Fund Balances	(268,250)	534,679	-	244,292	739,333	244,932	1,494,986
Total Liabilities, Deferred Inflows of Resources, and Fund Balances	\$ 29,051	\$ 537,485	\$ 526,625	\$ 248,635	\$ 807,697	\$ 246,298	\$ 2,395,791

See accompanying notes and auditor's report.

CITY OF DEER RIVER, MINNESOTA

**RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO
THE STATEMENT OF NET POSITION**

December 31, 2018

Total fund balances - Governmental funds	\$ 1,494,986
Amounts reported for governmental activities in the statement of net assets are different because:	
Governmental funds do not generally record prepaid assets, but record the expenditure in the period in which it is due and payable.	53,246
Net delinquent property taxes receivable will be collected this year, but are not available soon enough to pay for the current period's expenditures, and therefore are deferred in the funds.	(7,000)
Capital assets (net of accumulated depreciation) used in governmental activities are not current financial resources and therefore are not reported in the governmental funds balance sheet.	3,030,428
The recognition of net pension liability is effected by timing and treatment of certain items that are not recognized in the governmental funds.	
Deferred outflows of resources as related to net pension liability	360,762
Deferred inflows of resources as related to net pension liability	(630,213)
Other long term assets are not available to pay for current period expenditures and, therefore, are deferred in the funds.	
Property taxes	13,581
Special assessments	3,908
Notes receivable	1,366
Interest payable on long-term debt does not require current financial resources. Therefore interest payable is not reported as a liability in governmental funds balance sheet.	(77,634)
Long term liabilities are not due and payable in the current period and, therefore they are not reported in the governmental funds balance sheet.	
Related to long term bonds and notes	(3,991,365)
Related to long term compensated absences	(78,911)
Related to net pension liability	(192,930)
Net position of governmental activities - Government-wide	<u>\$ (19,776)</u>

See accompanying notes and auditor's report.

CITY OF DEER RIVER, MINNESOTA

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES -
GOVERNMENTAL FUNDS**

For the Year Ended December 31, 2018

	Major Funds							Total Governmental Funds
	General Fund	Fire Department Fund	Community Development Revolving Fund #2	Debt Service Fund	Capital Projects North/South Project	Total Other Non-Major Funds	Total Governmental Funds	
Revenues								
Taxes	\$ 678,861	\$ 30,573	\$ -	\$ 41,832	\$ -	\$ 8,465	\$ 759,731	
Special assessments	-	-	-	3,118	-	-	3,118	
Licenses and permits	14,600	-	-	-	-	-	14,600	
Intergovernmental	353,140	37,609	-	-	-	-	390,749	
Charges for services	10,038	203,264	-	-	-	-	225,891	
Fines and forfeitures	7,525	-	-	-	-	12,589	20,114	
Interest earnings	-	2,458	-	-	-	-	2,458	
Other revenues	39,307	150	-	-	-	1,268	41,725	
Total Revenues	1,103,471	274,054	-	44,950	-	22,562	1,445,037	
Expenditures								
Current								
General government	315,593	-	-	-	-	-	315,593	
Public safety	471,849	150,331	-	-	-	-	622,180	
Highways and streets	210,114	-	-	-	-	-	210,114	
Culture and recreation	44,393	-	-	-	-	-	44,393	
Debt service	-	9,790	-	43,661	-	-	53,451	
Other	-	-	-	-	32,314	-	32,314	
Capital	-	-	-	-	-	-	-	
Public safety	1,891	13,925	-	-	-	-	15,816	
Highways and streets	335,023	-	-	-	1,146,243	-	1,481,266	
Total Expenditures	1,378,863	174,046	-	43,661	1,178,557	15,825	2,790,952	
Excess of Revenues Over (Under) Expenditures	(275,392)	100,008	-	1,289	(1,178,557)	6,737	(1,345,915)	
Other Financing Sources (Uses)								
Proceeds from the issuance of bonds	222,817	-	-	-	3,504,165	-	3,726,982	
Transfer from (to) other funds	-	-	-	66,836	(1,586,275)	-	(1,519,439)	
Total Other Financing Sources (Uses)	222,817	-	-	66,836	1,917,890	-	2,207,543	
Excess of Revenues and Other Financing Sources Over (Under) Expenditures and Other Financing Uses	(52,575)	100,008	-	68,125	739,333	6,737	861,628	
Fund Balance - Beginning of Year	(215,675)	434,671	-	176,167	-	238,195	633,358	
Fund Balance - End of Year	\$ (268,250)	\$ 534,679	\$ -	\$ 244,292	\$ 739,333	\$ 244,932	\$ 1,494,986	

See accompanying notes and auditor's report.

CITY OF DEER RIVER, MINNESOTA

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND
CHANGES IN FUND BALANCE OF GOVERNMENTAL FUNDS TO THE
STATEMENT OF ACTIVITIES**

For the Year Ended December 31, 2018

Net change in fund balances - Government funds	\$ 861,628
Amounts reported for governmental activities in the statement of activities are different because:	
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense and gains/losses are recognized in the period of disposal.	
Capital outlay additions	1,497,082
Loss on disposal of assets	(4,437)
Depreciation	(127,493)
Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets.	47,355
Proceeds from the issuance of bonds is an other financing source in the governmental funds, but the issuance increases long-term liabilities in the statement of net assets.	(3,783,000)
In the statement of activities, net pension liability (NPL) is measured considering the change in deferred inflows and outflows under GASB 68. In the governmental funds, pension contribution is measured based on employer contributions. This is the difference between the recognition methods.	22,935
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds until due and payable. This is the amount of change in compensated absences	
Compensated absences	6,844
Accrued interest	(74,969)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the governmental funds including taxes and special assessments.	(2,368)
Certain expenses recorded in the governmental funds relate to future economic periods and are not reported as expenses in the statement of activities. This is the amount of the change in prepaids for the year.	6,836
Change in net position of governmental activities - Government-wide	<u>\$ (1,549,587)</u>

See accompanying notes and auditor's report.

CITY OF DEER RIVER, MINNESOTA

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL - GENERAL FUND

For the Year Ended December 31, 2018

General Fund

	Original Budget	Final Budget	Actual	Variance with Final Budget
Revenues				
Taxes	\$ 665,619	\$ 665,619	\$ 678,861	\$ 13,242
Licenses and permits	17,000	17,000	14,600	(2,400)
Intergovernmental	370,911	370,911	353,140	(17,771)
Charges for services	7,100	7,100	10,038	2,938
Fines and forfeitures	12,500	12,500	7,525	(4,975)
Other revenues	64,200	64,200	39,307	(24,893)
Total Revenues	1,137,330	1,137,330	1,103,471	(33,859)
Expenditures				
General government	322,983	322,983	315,593	7,390
Public safety	508,453	508,453	471,849	36,604
Highways and streets	242,604	242,604	210,114	32,490
Culture and recreation	50,029	50,029	44,393	5,636
Capital outlay	25,150	25,150	336,914	(311,764)
Total Expenditures	1,149,219	1,149,219	1,378,863	(229,644)
Excess of Expenditures Over Revenues	(11,889)	(11,889)	(275,392)	(263,503)
Other Financing Sources				
Proceeds from the issuance of long term debt	-	-	222,817	222,817
Proceeds from the sale of assets	15,000	15,000	-	(15,000)
Excess of Revenues and Other Financing Sources Over (Under) Expenditures	15,000	15,000	222,817	207,817
Fund Balance - Beginning of Year	\$ 3,111	\$ 3,111	(52,575)	\$ (55,686)
Fund Balance - End of Year			(215,675)	\$ (268,250)

See accompanying notes and auditor's report.

CITY OF DEER RIVER, MINNESOTA

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL - FIRE DEPARTMENT FUND

For the Year Ended December 31, 2018

Fire Department Fund

	Original Budget	Final Budget	Actual	Variance with Final Budget
Revenues				
Taxes	\$ 31,000	\$ 31,000	\$ 30,573	\$ (427)
Intergovernmental	40,200	40,200	37,609	(2,591)
Charges for services	174,000	174,000	203,264	29,264
Interest earnings	500	500	2,458	1,958
Other revenues	2,000	2,000	150	(1,850)
Total Revenues	247,700	247,700	274,054	26,354
Expenditures				
Public safety	198,672	198,672	150,331	48,341
Capital outlay	38,917	38,917	13,925	24,992
Debt Service	10,111	10,111	9,790	321
Total Expenditures	247,700	247,700	174,046	73,654
Excess of Revenues Over Expenditures	\$ -	\$ -	100,008	\$ 100,008
Fund Balance - Beginning of Year			434,671	
Fund Balance - End of Year			\$ 534,679	

CITY OF DEER RIVER, MINNESOTA

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES - BUDGET AND ACTUAL - COMMUNITY DEVELOPMENT REVOLVING FUND #2

For the Year Ended December 31, 2018

	Community Development Revolving Fund #2			
	Original Budget	Final Budget	Actual	Variance with Final Budget
Revenues				
Intergovernmental	\$ -	\$ -	\$ -	\$ -
Expenditures				
Other	-	-	-	-
Excess of Revenues Over Expenditures				
Fund Balance - Beginning of Year	\$ -	\$ -	\$ -	\$ -
Fund Balance - End of Year				
			\$ -	

CITY OF DEER RIVER, MINNESOTA

STATEMENT OF NET POSITION - PROPRIETARY FUNDS

December 31, 2018

	Major (All) Funds			
	Water	Sewer	License Bureau	Total
<i>Assets and Deferred Outflows of Resources</i>				
Current Assets				
Cash	\$ 53,467	\$ 52,936	\$ -	\$ 106,403
Accounts receivable (No allowance deemed necessary)	13,698	22,179	670	36,547
Unbilled revenues	7,727	9,430	-	17,157
Due from other funds	-	15,240	-	15,240
Total Current Assets	74,892	99,785	670	175,347
Noncurrent Assets				
Capital assets (Net of accumulated depreciation)	2,525,223	2,352,517	926	4,878,666
Total Assets	2,600,115	2,452,302	1,596	5,054,013
Deferred Outflows of Resources				
Related to pensions	12,025	9,019	19,434	40,478
Total Assets and Deferred Outflows of Resources	\$ 2,612,140	\$ 2,461,321	\$ 21,030	\$ 5,094,491
<i>Liabilities, Deferred Inflows of Resources, and Net Position</i>				
Liabilities				
Current Liabilities				
Current maturities of long-term debt	\$ 53,750	\$ 88,155	\$ -	\$ 141,905
Accounts payable	16,549	10,523	1,270	28,342
Accrued payroll	177	199	278	654
Accrued compensated absences	3,023	3,023	774	6,820
Accrued interest	6,179	8,893	-	15,072
Due to other funds	-	-	15,240	15,240
Total Current Liabilities	79,678	110,793	17,562	208,033
Long-term Liabilities				
Accrued compensated absences	8,884	8,884	654	18,422
Bonds payable	479,000	649,510	-	1,128,510
Net pension liability	34,794	26,096	56,230	117,120
Total Long-term Liabilities	522,678	684,490	56,884	1,264,052
Total Liabilities	602,356	795,283	74,446	1,472,085
Deferred Inflows of Resources				
Related to pensions	15,453	11,590	24,973	52,016
Net Position				
Net investment in capital asset	1,986,294	1,605,959	926	3,593,179
Unrestricted	8,037	48,489	(79,315)	(22,789)
Total Net Position	1,994,331	1,654,448	(78,389)	3,570,390
Total Liabilities, Deferred Inflows of Resources, and Net Position	\$ 2,612,140	\$ 2,461,321	\$ 21,030	\$ 5,094,491

See accompanying notes and auditor's report.

CITY OF DEER RIVER, MINNESOTA

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION - PROPRIETARY FUNDS

For the Year Ended December 31, 2018

	Major (All) Funds			
	Water	Sewer	License Bureau	Total
Operating Revenues				
Charges for services	\$ 216,607	\$ 346,320	\$ 86,940	\$ 649,867
Expenditures				
Salaries and benefits	78,107	59,664	88,026	225,797
Depreciation	67,986	88,698	442	157,126
Materials and supplies	35,052	11,626	5,005	51,683
Other	14,334	21,087	4,248	39,669
Utilities and repairs	22,060	19,035	964	42,059
Total Expenditures	217,539	200,110	98,685	516,334
Operating Income (Loss)	(932)	146,210	(11,745)	133,533
Nonoperating Income (Expense)				
Interest	(16,072)	(21,655)	-	(37,727)
Net Income (Loss) Before Transfers	(17,004)	124,555	(11,745)	95,806
Transfer From Other Funds	906,332	613,107	-	1,519,439
Net Income (Loss)	889,328	737,662	(11,745)	1,615,245
Net Position - Beginning of Year	1,105,003	916,786	(66,644)	1,955,145
Net Position - End of Year	\$ 1,994,331	\$ 1,654,448	\$ (78,389)	\$ 3,570,390

CITY OF DEER RIVER, MINNESOTA

STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS

For the Year Ended December 31, 2018

	Major (All) Funds			
	Water	Sewer	License Bureau	Total
Cash Flows From Operating Activities				
Cash received from customers and others	\$ 229,854	\$ 357,443	\$ 87,071	\$ 674,368
Cash payments to suppliers for goods and services	(57,063)	(43,070)	(8,993)	(109,126)
Cash payments to employees and for benefits	(73,259)	(58,032)	(86,129)	(217,420)
Net Cash Provided By (Used In) Operating Activities	99,532	256,341	(8,051)	347,822
Cash Flows From Noncapital Financing Activities				
Interfund borrowing	-	(8,051)	8,051	-
Payments received from property taxes	643	2,499	-	3,142
Net Cash Provided By (Used In) Financing Activities	643	(5,552)	8,051	3,142
Cash Flows From Capital and Related Financing Activities				
Purchases of capital assets	(927,447)	(765,829)	-	(1,693,276)
Payments on bonds	(44,090)	(103,555)	-	(147,645)
Interest and bond issue costs paid	(18,106)	(24,787)	-	(42,893)
Transfer from other funds	906,332	613,107	-	1,519,439
Net Cash Used In Capital and Related Financing Activities	(83,311)	(281,064)	-	(364,375)
Cash Flows From Investing Activities	-	-	-	-
Net Increase (Decrease) in Cash	16,864	(30,275)	-	(13,411)
Cash - Beginning of Year	36,603	83,211	-	119,814
Cash - End of Year	\$ 53,467	\$ 52,936	\$ -	\$ 106,403

CITY OF DEER RIVER, MINNESOTA

STATEMENT OF CASH FLOWS - PROPRIETARY FUNDS

For the Year Ended December 31, 2018

	Major (All) Funds			
	Water	Sewer	License Bureau	Total
Cash Flows From Operating Activities				
Operating income (loss)	\$ (932)	\$ 146,210	\$ (11,745)	\$ 133,533
Adjustments to reconcile operating income to cash provided by operating activities				
Depreciation	67,986	88,698	442	157,126
Decrease in deferred outflows - related to pensions	6,265	5,787	14,533	26,585
Decrease in accounts receivable	14,364	12,533	131	27,028
Increase in unbilled revenue	(1,117)	(1,410)	-	(2,527)
Increase in accounts payable	14,383	8,678	1,224	24,285
Decrease in accrued payroll	(1,103)	(862)	(1,847)	(3,812)
Increase (decrease) in compensated absences payable	(258)	(258)	1,428	912
Increase (decrease) in net pension liabilities	608	(1,578)	(7,258)	(8,228)
Decrease in deferred inflows - related to pensions	(664)	(1,457)	(4,959)	(7,080)
Net Cash Provided By (Used In) Operating Activities	\$ 99,532	\$ 256,341	\$ (8,051)	\$ 347,822

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following is a summary of the significant accounting policies of the various funds of the City.

Reporting Entity

The City's combined financial statements include the accounts of all City operations. The criteria for including organizations as component units within the City's reporting entity, as set forth in Government Accounting Standards Board Statement No. 61, *The Financial Reporting Entity*, amends GASB Statement No. 14, *The Financial Reporting Entity*, and GASB Statement No. 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments* by clarifying requirements for the reporting of component units. Consideration for inclusion as a component unit include whether the organization is legally separate, the City hold the corporate powers of the organization, the City appoints a voting majority of the board, the City is able to impose its will, whether the organization has the potential to impose a financial burden/benefit on the City and the level of fiscal dependency. GASB 61 expanded the definitions found within Statement 14 as well as clarified many of the criteria used to determine the financial benefit and burden relationships.

Based upon the application of these criteria, there are no component units required to be included in the government's reporting entity.

Basis of Presentation

Government-Wide Financial Statements

The government-wide financial statements (the statement of net position and the statement of activities) report information on all of the activities of the City. The effect of interfund activity, within the governmental and business-type activities columns, has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The statement of activities demonstrates the degree to which the direct expenses of a given program are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific program. Program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given program and 2) operating or capital grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Taxes and other items not properly included among program revenues are reported instead as general revenues.

Fund Financial Statements

The City segregates transactions relating to certain functions or activities in separate funds in order to aid financial management and to demonstrate legal compliance. Separate statements are presented for governmental and proprietary activities. These statements present each major fund as a separate column on the fund financial statements; all non-major funds are aggregated and presented in a single column.

Governmental funds are those funds through which most governmental functions typically are financed. The measurement focus of governmental funds is on the sources, uses and balance of current financial resources. The City has presented the following major governmental funds:

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

General Fund

The General Fund is the main operating fund of the City. This fund is used to account for all financial resources not accounted for in other funds. All general tax revenues and other receipts that are not restricted by law or contractual agreement to some other fund are accounted for in this fund. General operating expenditures, fixed charges and capital improvement costs that are not paid through other funds are paid from the General Fund.

Fire Department

The Fire Department Fund is used to account for the activities of the City's fire department.

Community Development Revolving Fund #2

The Community Development Revolving Fund #2 is used to account for the activities of the housing development grant. Currently the fund holds notes which will potentially be forgiven as time restrictions are met.

Debt Service Fund

Debt Service Fund is used to account for the accumulation of resources for, and the payment of, general long-term debt principal, interest and related costs.

North/South Capital Projects Fund

The North/South Capital Projects Fund is used to account for the activities of the capital construction project that included water, sewer, and street infrastructure upgrades.

Total Other Non-Major Funds

Total Other Non-Major Funds is a summarization of all of the nonmajor governmental funds which include the City's community development revolving fund #1, Municipal Forest fund and TIF district 1 fund.

Proprietary funds are accounted for using the economic resources measurement focus and the accrual basis of accounting. The accounting objectives are determinations of net income, financial position and cash flow. All assets and liabilities are included on the Statement of Net Position. The City has presented the following major proprietary funds: Water, Sewer, and License Bureau.

All the enterprise funds account for the operation of the City's water and sewer utilities and license bureau. Activities of the funds include administration, operation and maintenance of the license bureau and the water and sewer system and billing and collection activities. The funds also account for the accumulation of resources for, and the payment of, long-term debt principal and interest for revenue bonds throughout the year. All costs are financed through established fees with the State of Minnesota and the Department of Natural Resources for the License Bureau. Most costs in the water and sewer funds are financed with charges made to customers with rates reviewed periodically and adjusted if necessary to ensure the integrity of the funds.

Proprietary funds distinguish operating revenues and expenses from non-operating 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. Operating expenses for the proprietary funds include the cost of personal and contractual services, supplies and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

GASB 34 eliminates the presentation of Account Groups, but provides for these records to be maintained and incorporates the information into the Governmental Activities column in the government-wide Statement of Net Assets.

CITY OF DEER RIVER, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Measurement Focus/Basis of Accounting

Measurement focus refers to what is being measured; basis of accounting refers to when revenues and expenditures are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurement made, regardless of the measurement focus applied.

The government-wide statements and fund financial statements for the proprietary funds are reported using the economic resources measurement focus and the accrual basis of accounting. The economic resources measurement focus means all assets and liabilities (whether current or non-current) are included in the statement of net position and the operating statements present increases (revenues) and decreases (expenses) in net total assets. Under the accrual basis of accounting, revenues are recognized when earned, including unbilled utility services which are accrued. Expenses are recognized at the time the liability is incurred.

Governmental fund financial statements are reported using the current financial resources measurement focus and are accounted for using the modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues are recognized when susceptible to accrual; i.e., when they become both measurable and available. "Measurable" means the amount of the transaction can be determined and "available" means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. The City considers property taxes as available if they are collected within 60 days after year end. A one-year availability period is used for recognition of all other Governmental Fund revenues. Expenditures are recorded when the related fund liability is incurred. However, debt service expenditures, except for interest payable, are accrued at the debt issuance date for which cash is received with the debt proceeds, as well as expenditures related to compensated absences which are recorded only when payment has matured and will be payable shortly after year-end.

The revenues susceptible to accrual are property taxes, franchise fees, licenses, charges for service, interest income and intergovernmental revenues.

Cash and Cash Equivalents

Cash and cash equivalents consist of checking and savings accounts held in a local institution and funds held in a money market fund.

Investments

State statutes authorize the City to invest in obligations of the U.S. Treasury, commercial paper, corporate bonds or repurchase agreements. All investments are recorded at fair value based on quoted market prices. Fair value is the amount of which a financial instrument could be exchanged in a current transaction between willing parties. As of December 31, 2018, the City did not hold any investments.

Prepaid Expenses

Prepaid balances are for payments made by the City in the current year for goods or services benefiting subsequent fiscal years.

Deferred Inflows and Outflows of Resources

Deferred inflows of resources represent an acquisition of net position that applies to a future period, and is therefore deferred until that time. The City recognizes deferred inflows of resources related to pensions.

Governmental funds report revenue that are unavailable as deferred inflows of resources as well as unavailable revenue from property taxes, special assessments, and certain loans with forgiveness provisions. These amounts are deferred and recognized as revenue in the period that the amounts become available.

Deferred outflows of resources represent a consumption of net position that applies to a future period, and is therefore deferred until that time. The City also recognized deferred outflows of resources related to pensions.

CITY OF DEER RIVER, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Capital Assets

Capital assets, which include property, plant, equipment, and infrastructure assets, are reported in the applicable governmental or business-type activities columns in the government-wide financial statements and in the fund financial statements for the proprietary funds. All capital assets are valued at historical cost or estimated historical cost if actual historical cost was not available. Donated assets are valued at acquisition value on the date donated. Repairs and maintenance are recorded as expenses. Renewals and betterments are capitalized. Interest has not been capitalized during the construction period on the capital assets.

Assets capitalized, not including infrastructure assets, have an original cost of \$1,000 or more and over one year of useful life. Infrastructure assets capitalized have varying original costs depending upon the nature of the project. The City has elected to prospectively record infrastructure as of December 31, 2003, the initial date of implementation of GASB 34.

Depreciation has been calculated on each class of depreciable property using the straight-line method. Estimated useful lives are as follows:

Buildings	50 years
Machinery and equipment	5 - 15 years
Improvements	10 - 50 years
Water and sewer lines	40 - 50 years
Infrastructure	50 years

The City reviewed the provisions of GASB Statement No. 51 *Accounting and Financial Reporting for Intangible Assets* and determined no material provision in the current reporting year would apply. The City is required to implement the standard prospectively only.

Compensated Absences

Vacation and sick leave are payable upon termination from the City of Deer River and are based upon contracts. Accumulated vacation and sick leave that is expected to be liquidated with expendable available financial resources is reported as an expenditure and a fund liability of the fund that will pay it.

Property Taxes

Property taxes are recognized as revenue to the extent they are collected in the current period. Property taxes collected by Itasca County, but not paid to the City by December 31, are classified as unremitted taxes. The City maintains an allowance equal to the full amount of delinquent accounts at December 31 for the governmental fund statements.

The City annually adopts a tax levy and certifies it to Itasca County for collection. The County is responsible for collecting all property taxes for the City. Property taxes attach as an enforceable lien on January 1 of each year and are payable on May 15 and October 15 each year.

Portions paid by the State of Minnesota in the form of tax credits or other aids are included in intergovernmental revenues.

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Budget

An annual appropriated budget is adopted on a basis consistent with generally accepted accounting principles. All annual appropriations lapse at year end.

A budget of revenues and expenditures, for the following year, is prepared by the City Clerk by December 31 of the current year. Budget amounts are primarily based on requests of department heads. Once prepared, the budget is presented to the City Council for approval. All subsequent budget amendments, if any, are presented to the Council for approval.

Transactions Between Funds

Legally authorized transfers are treated as interfund transfers and are included in the results of operations of both governmental and proprietary funds.

Fund Balance Classifications

In the fund financial statements, governmental funds report fund balance in classifications that disclose constraints for which amounts in those funds can be spent. These classifications are as follows:

Nonspendable - consists of amounts that are not in spendable form, such as inventories, prepaids, and long term receivables.

Restricted - consists of amounts related to externally imposed constraints established by creditors, grantors, or contributors; or enabling legislation. Currently the City has restricted funds for debt service under a bond agreement, for a housing grant set by enabling legislation, and for a capital projects funds based on tax increment financing agreements and a major infrastructure upgrades financed through bonds.

Committed - consists of internally imposed constraints. These constraints are established by formal resolution of the city council which is the city's highest level of decision making authority. Committed funds cannot be used for any other purpose unless the City modifies or rescinds the commitment by resolution.

Assigned - consists of internally imposed constraints. These constraints reflect the specific purpose of which is the City's intended use. The constraints are established by the City and/or management but the council has authorized the city clerk or finance department to establish the assigned amounts.

Unassigned - is the residual classification for the general fund and also reflects negative residual amounts in other funds.

When both restricted and unrestricted resources are available for use, it is the City's policy to first use restricted resources, and then use unrestricted resources as they are needed.

When committed, assigned, or unassigned resources are available for use, it is the City's policy to use resources in the following order: 1) committed 2) assigned and 3) unassigned.

Minimum Unassigned Fund Balance Policy

The City has approved a general fund balance policy that strives for an unassigned general fund balance of not less than five percent of the budgeted operating expenditures.

Net Position

Net position represent the difference between assets/deferred outflows and liabilities/deferred inflows. Investment in net assets consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowing used for the acquisition, construction or improvements of those assets, and adding back unspent proceeds. Net position is reported as restricted when there are limitations or restrictions imposed by creditors, grantors or laws or regulations of other governments.

Nature and Purpose of Reservations of Fund Equity

The City maintains reservations in its general and special revenue fund that represents accumulated earnings set aside for debt service, housing development and a tax increment district.

CITY OF DEER RIVER, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of certain assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures/expenses during the reporting period. As such, actual results could differ from those estimates.

Pensions

The City reports pension costs on the pay-as-you-go basis based on when payroll is paid and pension disbursements are made to the Public Employees Retirement Association. (PERA)

As a participant in PERA, the City is, however, allocated its proportionate share of PERA's net pension liability. (See Note 8) For purposes of measuring that net pension liability, deferred outflows/inflows of resources and pension expense, information about the fiduciary net position of PERA and additions to/deductions from PERA's fiduciary net position have been determined on the same basis as they are reported by PERA except that PERA's fiscal year end is June 30. For this purpose, plan contributions are recognized as of employer payroll paid dates and benefit payments and refunds are recognized when due and payable in accordance with benefit terms. Investments are reported at fair value.

For the City pension costs related to the Deer River Firefighters Relief Association are recorded based on a statutorily calculated annual minimum municipal contribution amount. This amount is certified to the City by August 1 of each year and is payable in the following year.

NOTE 2 CASH AND INVESTMENTS

Deposits

Minnesota Statutes require that all City deposits be protected by insurance, surety bond, or collateral. The market value for pledged collateral must equal 110% of the deposits not covered by insurance or bonds.

Custodial credit risk is the risk that, in the event of a bank failure, the City's deposits might not be recovered. The City does not have a formal deposit policy for custodial credit risk. As of December 31, 2018, all deposits were adequately covered by deposit insurance or collateral held in safekeeping in the City's name.

NOTE 3 NOTES RECEIVABLE/DEFERRED REVENUE

The City maintains a special revenue fund to account for the grants and deferred loans authorized under the Community Development Revolving Loan program. Housing assistance is provided to qualified applicants to help fund home improvement projects. The original proceeds were received under a grant provided to the City of Deer River from the Minnesota Department of Trade and Economic Development. The City worked with a separate management agency to determine eligibility and to oversee the program. As of December 31, 2018, the City has notes receivable of \$1,366 and a corresponding deferred inflow reported in a special revenue fund in the accompanying governmental fund financial statements.

CITY OF DEER RIVER, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 3 NOTES RECEIVABLE/DEFERRED REVENUE (Continued)

The City also received funding under a separate housing grant that it records in a special revenue fund. The Community Development Revolving Fund #2 is used by the City to record newly awarded grants which do not have a repayment feature assuming certain restrictions are met. As of December 31, 2018, the City had completed the grant and recorded \$526,625 in notes receivable and corresponding deferred inflows still outstanding. The City does not anticipate receiving cash flow from these notes as they anticipate the loans will be forgiven as the occupancy requirements are met. The loan agreements call for 10% to be forgiven each year through 2025.

NOTE 4 CAPITAL ASSETS

The following is a summary of changes in capital assets for the year ended December 31, 2018:

	Balance January 1	Additions	Retirements	Balance December 31
Governmental activities:				
Land	\$ 437,393	\$ -	\$ -	\$ 437,393
Buildings and structures	667,738	-	-	667,738
Improvements	200,869	135,311	-	336,180
Machinery and equipment	1,683,644	241,538	(26,625)	1,898,557
Infrastructure	301,569	1,120,233	-	1,421,802
	<u>3,291,213</u>	<u>1,497,082</u>	<u>(26,625)</u>	<u>4,761,670</u>
Less: accumulated depreciation				
Buildings and structures	359,620	15,173	-	374,793
Improvements	69,492	7,566	-	77,058
Machinery and equipment	1,126,602	98,345	(22,188)	1,202,759
Infrastructure	70,223	6,409	-	76,632
	<u>1,625,937</u>	<u>127,493</u>	<u>(22,188)</u>	<u>1,731,242</u>
Total Capital Assets, net	<u>\$ 1,665,276</u>	<u>\$ 1,369,589</u>	<u>\$ (4,437)</u>	<u>\$ 3,030,428</u>

The City of Deer River has elected to prospectively record infrastructure assets effective January 1, 2005.

	Balance January 1	Additions	Retirements	Balance December 31
Business-type activities:				
Buildings	\$ 19,085	\$ -	\$ -	\$ 19,085
Land	21,000	-	-	21,000
Improvements	3,248,973	763,781	-	4,012,754
Distribution system	1,808,868	-	-	1,808,868
Machinery and equipment	348,415	3,650	-	352,065
Work in process	713,109	925,825	-	1,638,934
	<u>6,159,450</u>	<u>1,693,256</u>	<u>-</u>	<u>7,852,706</u>
Less: accumulated depreciation				
	<u>(2,816,914)</u>	<u>(157,126)</u>	<u>-</u>	<u>(2,974,040)</u>
Total Capital Assets, net	<u>\$ 3,342,536</u>	<u>\$ 1,536,130</u>	<u>\$ -</u>	<u>\$ 4,878,666</u>

CITY OF DEER RIVER, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 4 CAPITAL ASSETS (Continued)

The following is a summary of enterprise fund type fixed assets at December 31, 2018:

	Water Fund	Sewer Fund	License Bureau Fund	Total
Buildings	\$ 9,052	\$ 8,554	\$ 1,479	\$ 19,085
Land	13,600	7,400	-	21,000
Improvements	2,127,574	1,885,180	-	4,012,754
Distribution system	476,300	1,332,568	-	1,808,868
Machinery and equipment	172,587	176,570	2,908	352,065
Work in process	912,812	726,122	-	1,638,934
	<u>3,711,925</u>	<u>4,136,394</u>	<u>4,387</u>	<u>7,852,706</u>
Accumulated depreciation	(1,186,702)	(1,783,877)	(3,461)	(2,974,040)
	<u>\$ 2,525,223</u>	<u>\$ 2,352,517</u>	<u>\$ 926</u>	<u>\$ 4,878,666</u>

Depreciation expense was charged as direct expense to programs of the primary government as follows:

Governmental activities

General government	\$ 5,851
Public safety	72,472
Highways and streets	40,559
Culture and recreation	8,611
	<u>\$ 127,493</u>

Business-type activities

Water	\$ 67,986
Sewer	88,698
License Bureau	442
	<u>\$ 157,126</u>

CITY OF DEER RIVER, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 5 LONG-TERM DEBT

General long-term debt at December 31, 2018, is as follows:

	Governmental	Business-type
2009 PFA Loan dated August 2009 in the amount of \$50,193, due in annual installments of \$2,695 to \$3,030 through August 2029; interest rate of 1%.	\$ -	\$ 32,000
\$164,000 1992 GO Water & Sewer Revenue Bonds, due in annual installments of \$1,458 to \$11,910 through January 1, 2019; interest rate of 5.5%.	-	780
\$322,131 2002 State Drinking Water Loan, due in annual installments of \$15,299 to \$19,310, maturing August 20, 2022; interest rate of 1.63%.	-	69,000
\$1,050,000 GO Bonds, Series 2015A, due in annual installments of \$41,300 to \$186,356 through January 1, 2031; interest rate of 1% to 3.25%.	208,365	516,635
\$654,000 GO Utility Revenue Note Series 2017A, due in annual installments of \$33,000 to \$54,000 through February 1, 2033; interest rate of 3.35%.	-	652,000
\$228,000 GO Equipment Certificate of Indebtedness, Series 2018A, due in annual installments of \$22,000 to \$28,000 through February 1, 2028; interest rate of 2.95%.	228,000	-
\$3,555,000 GO Bond, Series 2018B, due in annual installments of \$80,000 to \$145,000 through February 1, 2048; interest rate of 3% to 4%.	3,555,000	-
	3,991,365	1,270,415
Less: Current maturities	(35,875)	(141,905)
	<u>\$ 3,955,490</u>	<u>\$ 1,128,510</u>

Annual requirements to amortize long-term debt at December 31, 2018 are as follows:

	Governmental Activities		Business-type Activities		Total
	Principal	Interest	Principal	Interest	
2019	\$ 35,875	\$ 158,119	\$ 141,905	\$ 35,085	\$ 370,984
2020	123,525	135,320	107,475	32,420	398,740
2021	115,915	131,912	89,085	30,068	366,980
2022	116,915	128,801	91,085	27,863	364,664
2023	124,350	125,771	77,650	25,438	353,209
2024 - 2028	649,315	576,345	405,685	90,942	1,722,287
2029 - 2033	570,470	482,149	357,530	26,489	1,436,638
2034 - 2038	620,000	383,003	-	-	1,003,003
2039 - 2043	735,000	256,100	-	-	991,100
2044 - 2048	900,000	93,200	-	-	993,200
	<u>\$ 3,991,365</u>	<u>\$ 2,470,720</u>	<u>\$ 1,270,415</u>	<u>\$ 268,305</u>	<u>\$ 8,000,805</u>

CITY OF DEER RIVER, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 5 LONG-TERM DEBT (Continued)

Changes in long-term debt occurred during the year as follows:

	Balance January 1	Additions	Reductions	Balance December 31
Governmental Activities				
Compensated absences	\$ 73,125	\$ 43,357	\$ 37,571	\$ 78,911
Bonds and notes payable	255,720	3,783,000	47,355	3,991,365
	<u>\$ 328,845</u>	<u>\$ 3,826,357</u>	<u>\$ 84,926</u>	<u>\$ 4,070,276</u>
Business-type Activities				
Compensated absences	\$ 11,298	\$ 13,927	\$ 6,803	\$ 18,422
Bonds and notes payable	1,418,060	-	147,645	1,270,415
	<u>\$ 1,429,358</u>	<u>\$ 13,927</u>	<u>\$ 154,448</u>	<u>\$ 1,288,837</u>

The City typically finances the debt payments through the debt service fund through tax levies and special assessments and through user fees in the water and sewer funds.

As part of the \$3,555,000 GO Bond, Series 2018B issuance, the principal and interest on the bonds must be paid with respect to the improvement project, from special assessments levied upon the property specifically benefitted by the improvement project in addition to user fees and ad valorem taxes levied.

NOTE 6 CONDUIT DEBT

The City of Deer River was the issuer of several conduit debt obligations issued on behalf of the Deer River Health Care Center, an independent nonprofit corporation. The City has no responsibility for the payment of the debt except for the payments received on the underlying loan agreement. The total amount of all conduit debt outstanding as of December 31, 2018 was \$4,443,381.

CITY OF DEER RIVER, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 7 SEGMENT INFORMATION - ENTERPRISE FUNDS

The City maintains three enterprise funds which are to be self-supporting through user fees charged for services to the public. Financial segment information as of and for the year ended December 31, 2018, is presented below.

	Water Fund	Sewer Fund	License Bureau Fund	Totals
Assets				
Current	\$ 74,892	\$ 99,785	\$ 670	\$ 175,347
Noncurrent	2,525,223	2,352,517	926	4,878,666
Deferred Outflows	12,025	9,019	19,434	40,478
Liabilities				
Current	79,678	110,793	17,562	208,033
Long-term	522,678	684,490	56,884	1,264,052
Deferred Inflows	15,453	11,590	24,973	52,016
Net Position				
Net investment in capital assets	1,986,294	1,605,959	926	3,593,179
Restricted	-	-	-	-
Unrestricted	8,037	48,489	(79,315)	(22,789)
Operating revenues	216,607	346,320	86,940	649,867
Operating expenses (excl. depreciation)	149,553	111,412	98,243	359,208
Depreciation	67,986	88,698	442	157,126
Operating income (loss)	(932)	146,210	(11,745)	133,533
Capital grants	-	-	-	-
Other non-operating revenues (expenses)	(16,072)	(21,655)	-	(37,727)
Transfers in (out)	906,332	613,107	-	1,519,439
Change in net position	889,328	737,662	(11,745)	1,615,245
Beginning net position	1,105,003	916,786	(66,644)	1,955,145
Ending net position	1,994,331	1,654,448	(78,389)	3,570,390
Net cash provided by:				
Operating activities	99,532	256,341	(8,051)	347,822
Noncapital financing	643	(5,552)	8,051	3,142
Capital and related financing activities	(83,311)	(281,064)	-	(364,375)
Investing activities	-	-	-	-
Beginning cash	36,603	83,211	-	119,814
Ending cash	53,467	52,936	-	106,403

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 8 DEFINED BENEFIT PENSION PLANS

Plan Description

The City participates in the following cost-sharing multiple-employer defined benefit pension plans administered by the Public Employees Retirement Association of Minnesota (PERA) as well as the employer maintained defined benefit pension plan for its volunteer firefighters. PERA's defined benefit pension plans are established and administered in accordance with Minnesota Statutes, Chapters 353 and 356. PERA's defined benefit pension plans are tax qualified plans under Section 401 (a) of the Internal Revenue Code.

General Employees Retirement Plan - Multiple Employer Cost Sharing Plan

All full-time and certain part-time employees of the City are covered by the General Employees Plan. General Employees Plan members belong to the Coordinated Plan. Coordinated Plan members are covered by Social Security.

Public Employees Police and Fire Plan - Multiple Employer Cost Sharing Plan

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

Deer River Firefighters Relief Association - Single Employer Plan

Volunteer firefighters of the City of Deer River, Minnesota, are covered by a defined benefit pension plan administered by the Deer River Firefighters Relief Association. The plan has 18 active and 5 deferred members as of December 31, 2018.

Benefits Provided

PERA provides retirement, disability, and death benefits. Benefits provisions are established by state statutes and can only be modified by the state legislature. Vested, terminated employees who are entitled to benefits, but are not receiving them yet, are bound by the provision in effect at the time they last terminated their public service.

General Employees Plan Benefits

Benefits are based on a member's highest average salary for any five successive years of allowable service, age, and years of credit at termination of service. Two methods are used to compute benefits for PERA's Coordinated Plan members. Membered hired prior to July 1, 1989, receive the higher of Method 1 or Method 2 formulas. Only Method 2 is used for members hired after June 30, 1989. Under Method 1, the accrual rate for Coordinated members is 1.2 percent of average salary for each of the first 10 years of service and 1.7 percent of average salary for each additional year. Under Method 2, the accrual rate for Coordinated members is 1.7 percent of average salary for all years of service. For members hired prior to July 1, 1989, a full annuity is available when age plus years of service equal 90 and normal retirement age is 65. For members hired on or after July 1, 1989, normal retirement age is the age for unreduced Social Security benefits capped at 66.

Benefit increases are provided to benefit recipients each January. Increases are related to the funding ratio of the plan. If the General Employees Plan is at least 90 percent funded for two consecutive years, benefit recipients are given a 2.5 percent increase. If the plan has not exceeded 90 percent funded, or have fallen below 80 percent, benefit recipients are given a one percent increase. A benefit recipient who has been receiving a benefit for at least 12 full months as of June 30, will receive a full increase. Members receiving benefits for at least one month but less than 12 full months as of June 30, will receive a pro rata increase.

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 8 DEFINED BENEFIT PENSION PLANS (Continued)

Police and Fire Plan Benefits

Benefits for these plan members first hired after June 30, 2010, but before July 1, 2014, vest on a prorated basis from 50% after five years up to 100% after ten years of credited service. Benefits for plan members first hired after June 30, 2014, vest on a prorated basis from 50% after ten years up to 100% after twenty years of credited service. The annuity accrual rate is 3% of average salary for each year of service. A full, unreduced pension is earned when members are age 55 and vested, or for members who were first hired prior to July 1, 1989, when age plus years of service equal at least 90.

Benefit increases are provided to benefit recipients each January. Recipients receive a future annual 1 percent increase. An annual adjustment will equal 2.5 percent any time the plan exceeds a 90 percent funded ratio for two consecutive years. If the adjustment is increased to 2.5 percent and the funded ratio falls below 80 percent for one year or 85 percent for two consecutive years, the post-retirement benefit increase will be lowered to one percent. A benefit recipient who has been receiving a benefit for at least 12 full months as of June 30 will receive a full increase. Members receiving benefits for at least one month but less than 12 full months as of June 30 will receive a pro rata increase. For retirements after May 31, 2014 the first increase will be delayed two years.

Deer River Firefighters Relief Association Benefits

The Association provides retirement benefits as well as disability benefits to members. The defined retirement benefits are based on a member's years of service and become fully vested after 20 years. Members are entitled to lump sum benefits upon retirement equal to \$2,800 per year for each year of service.

Contributions

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

General Employees Fund Contributions

Coordinated Plan members were required to contribute 6.5 percent of their annual covered salary in fiscal year 2018 and the City was required to contribute 7.5 percent for Coordinated members. The City's contributions to the General Employees Fund for the year ended December 31, 2018 were \$31,274. The City's contributions were equal to the required contributions as set by state statute.

Police and Fire Fund Contributions

Plan members were required to contribute 10.8% of their annual covered salary and the City was required to contribute 16.20% of pay for members in fiscal year 2018. The City's contributions to the Police and Fire Fund for the year ending December 31, 2018 were \$38,739. The City's contributions were equal to the required contributions as set by state statute.

Deer River Firefighters Relief Association Contributions

The City is required to remit the state fire aid along with a statutorily computed minimum municipal aid. For 2018, the City remitted total state fire aid of \$35,339 to the relief association. No minimum municipal contribution was required for 2018.

Pension Costs

General Employees Fund Pension Costs

At December 31, 2018, the City reported a liability of \$310,665 for its proportionate share of the General Employees Fund's net pension liability. The City's net pension liability reflected a reduction due to the State of Minnesota's contribution of \$16 million to the fund in 2018. The State is considered a non-employer contributing entity and the state's contribution meets the definition of a special funding situation. The State of Minnesota's proportionate share of the net pension liability associated with the City was \$10,219.

CITY OF DEER RIVER, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 8 DEFINED BENEFIT PENSION PLANS (Continued)

The net pension liability was measured as of June 30, 2018 and the total liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The City's proportion of the net pension liability was based on the City's contributions received by PERA during the measurement period for employer payroll paid dates from July 1, 2017 through June 30, 2018 relative to the total employer contributions received from all of PERA's participating employers. At June 30, 2018, the City's proportional share was .0056% which was an increase of .0005% from its proportion measured as of June 30, 2017.

The City's proportional share of the net pension liability	\$ 310,665
State of Minnesota's proportionate share of the net pension liability associated with the City	10,219
	<u>\$ 320,884</u>

For the year ended December 31, 2018, the City recognized pension expense of \$38,761 for its proportionate share of the General Employees Plan's pension expense. The City recognized an additional \$2,383 as pension expense (and grant revenue) for its proportionate share of the State of Minnesota's contribution of \$16 million to the General Employees Fund.

At December 31, 2018, the City's proportionate share of the Plan's deferred outflows of resources and deferred inflows of resources related to pensions are as follows from the various sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between expected and actual economic experience	\$ 7,521	\$ 9,384
Changes in Actuarial Assumptions	30,736	32,773
Difference between projected and actual investment earnings	39,908	67,397
Changes in proportion	12,956	28,418
Contributions paid to PERA subsequent to the measurement date	16,249	-
Total	<u>\$ 107,370</u>	<u>\$ 137,972</u>

\$16,249 reported as deferred outflows of resources related to pensions resulting from the City's contributions subsequent to the measurement date will be recognized as a reduction of net pension liability in the year ended December 31, 2019. Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended December 31:	Pension Expense Amount
2019	11,842
2020	(28,353)
2021	(23,855)
2022	(6,485)

CITY OF DEER RIVER, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 8 DEFINED BENEFIT PENSION PLANS (Continued)

Police and Fire Fund Pension Costs

At December 31, 2018, the City has a liability of \$223,838 for its proportionate share of the Fund's net pension liability. The net pension liability was measured as of June 30, 2018, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The City's proportion of the net pension liability was based on the City's contributions received by PERA during the measurement period for employer payroll paid dates from July 1, 2017, through June 30, 2018, relative to the total employer contributions received from all of PERA's participating employers. At June 30, 2018, the City's proportion was .021% which was an decrease of .001% from its proportion measured as of June 30, 2017. The City also recognized \$1,890 for the year ended December 31, 2018 as revenue and an offsetting reduction of net pension liability for its proportionate share of the State of Minnesota's on-behalf contributions to the Police and Fire fund. Legislation passed in 2013 required the State of Minnesota to begin contributing \$9 million to the Police and Fire Fund each year, starting in fiscal year 2014.

For the year ended December 31, 2018, the City recognized pension expense of \$(24,312) for its proportionate share of the Police and Fire Plan's pension expense.

At December 31, 2018, the City's proportionate share of the PEPFF's deferred outflows of resources and deferred inflows of resources related to pensions are as follows from the various sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between expected and actual economic experience	\$ 8,359	\$ 25,038
Changes in Actuarial Assumptions	176,690	288,626
Difference between projected and actual investment earnings	66,564	109,206
Changes in proportion	11,364	55,841
Contributions paid to PERA subsequent to the measurement date	20,023	-
Total	<u>\$ 283,000</u>	<u>\$ 478,711</u>

\$20,023 reported as deferred outflows of resources related to pensions resulting from the City's contributions subsequent to the measurement date will be recognized as a reduction of net pension liability in the year ended December 31, 2019. Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended December 31:	Pension Expense Amount
2019	2,985
2020	(170,919)
2021	(38,173)
2022	(9,627)

CITY OF DEER RIVER, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 8 DEFINED BENEFIT PENSION PLANS (Continued)

Deer River Firefighters Relief Association Pension Costs

The Deer River Firefighters Relief Association's net pension liability was measured as of December 31, 2017 under the allowable lookback method with a December 31, 2018 reporting date for the City as follows:

Service Cost	\$ 25,554
Interest	21,727
Differences between expected and actual experience	-
Changes in assumptions	(6,783)
Changes in benefit terms	-
Benefit payments	(90,000)
	<hr/>
Net change in total pension liability	(49,502)
Total Pension Liability - Beginning of the Year	414,474
	<hr/>
Total Pension Liability - End of the Year	364,972
	<hr/>
Fiduciary Net Position	589,425
	<hr/>
Net Pension Asset at end of the year	\$ 224,453
	<hr/> <hr/>

At December 31, 2018, the City's share of the Association's deferred outflows of resources and deferred inflows of resources related to pensions are as follows from the various sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
	<hr/>	<hr/>
Difference between expected and actual liability	\$ -	\$ 28,605
Change of assumptions	10,870	18,738
Net difference between projected and actual investment earnings	-	18,203
	<hr/>	<hr/>
Total	\$ 10,870	\$ 65,546
	<hr/> <hr/>	<hr/> <hr/>

Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended December 31:	Pension Expense Amount
2019	(5,670)
2020	(5,689)
2021	(14,541)
2022	(10,423)
2023	(4,530)
Thereafter	(13,823)

Total Pension Expense

The total pension expense for all plans recognized by the City for the year ended December 31, 2018, was as follows:

General	\$ 38,761
Police and Fire	(24,312)
Fire Relief	15,305
	<hr/>
	\$ 29,754
	<hr/> <hr/>

CITY OF DEER RIVER, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 8 DEFINED BENEFIT PENSION PLANS (Continued)

Actuarial Assumptions

The total pension liability in the June 30, 2018 actuarial valuation was determined using the following actuarial assumptions:

Inflation	<i>GERF and PEPFF</i>	<i>Relief Association</i>
Active Member Payroll Growth	2.50% per year	2.75% per year
Investment Rate of Return	3.25% per year	-
	7.5%	5.50%

General Employees Plan and Police and Fire Plan

Salary increases were based on service-related tables. Mortality rates for active members, retirees, survivors, and disabilitants were based on RP 2014 tables for all plans for males and females, as appropriate, with slight adjustments to fit PERA's experience. Cost of living benefit increases for retirees are assumed to be 1.25 percent per year for the General plan and 1.0 percent per year for the Police and Fire Plan.

Actuarial assumptions used in the June 30, 2018, valuation were based on the results of actuarial studies. The most recent six year experience study in the General Employees Plan was completed in 2015. The most recent four year experience study for the Police and Fire plan was completed in 2016.

The following changes in actuarial assumptions occurred in 2018:

General Employees Fund

- The mortality projection scale was changed from MP-2015 to MP-2017.
- The assumed post-retirement benefit increase changed from 1.0 percent per year through 2044 and 2.5 percent per year thereafter to 1.25 percent per year.

Police and Fire Fund

- The mortality projection scale was changed from MP-2016 to MP-2017.
- As set by statute, the assumed post-retirement benefit increase was changed from 1.0 percent per year through 2064 and 2.5 percent per year, thereafter, to 1.0 percent for all years, with no trigger.

Deer River Firefighters Relief Association

- The discount rate was changed from 5.50% to 6.00% and the expected long-term rate of return on assets was increased to 6.00%.

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

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Domestic Stocks	36%	5.10%
International Stocks	17%	5.30%
Bonds	20%	0.75%
Alternative Assets	25%	5.90%
Cash	2%	0.00%

CITY OF DEER RIVER, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 8 DEFINED BENEFIT PENSION PLANS (Continued)

Deer River Firefighters Relief Association

The long-term expected rate of return on pension plan investments is 5.5%. The Association uses an investment advisor to manage its portfolio. Best estimates of geometric real and nominal rates of return for each major asset class included in the pension plan's asset allocation as of the measurement date are summarized in the following table:

Asset Class	Allocation at Measurement Date	Long-Term Expected Real Rate of Return
Domestic equity	33.18%	5.39%
International equity	25.38%	5.20%
Fixed income	32.77%	1.98%
Real estate	0.42%	4.25%
Cash and equivalent	8.25%	0.79%

Discount Rate

General and Police/Fire Plans

The discount rate used to measure the total pension liability in 2018 was 7.50%. The projection of cash flows used to determine the discount rate assumed that contributions from members and employers will be made at the rates set in Minnesota statutes. Based on these assumptions, the fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Deer River Firefighters Relief Association

The discount rate used to measure the total pension liability (asset) was 6.00%.

Pension Liability Sensitivity

The following presents the City's proportionate share of the net pension liability for all plans it participates in, calculated using the discount rate disclosed in the preceding paragraph, as well as what the City's proportionate share of the net pension liability would be if it were calculated using a discount rate 1 percentage point lower or 1 percentage point higher than the current discount rate:

	1% Decrease in Discount Rate	Discount Rate	1% Increase in Discount Rate
City's proportion share of the General Employees Fund	504,870	310,665	150,354
City's proportion share of the Police and Fire Fund	479,924	223,838	12,067
City's proportion share of the Relief Association's net pension liability (asset)	(210,746)	(224,453)	(237,575)

CITY OF DEER RIVER, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 8 DEFINED BENEFIT PENSION PLANS (Continued)

Pension Plan Fiduciary Net Position

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

The City reports the following information regarding its pension plans in the government wide financial reports as follows:

	General	Police/Fire	Fire Relief Association	Total
Net pension liability (asset)	\$ 310,665	\$ 223,838	\$ (224,453)	\$ 310,050
Deferred inflows	137,972	478,711	65,546	682,229
Deferred outflows	107,370	283,000	10,870	401,240

NOTE 9 DEFINED CONTRIBUTION PLAN

Council members of the City are covered by the Public Employees Defined Contribution Plan (PEDCP) a multiple-employer deferred compensation plan administered by PERA. The Plan is a tax qualified plan under Section 401(a) of the Internal Revenue Code and all contributions by or on behalf of employees are tax deferred until time of withdrawal.

Plan benefits depend solely on amounts contributed to the plan plus investment earnings, less administrative expenses. Minnesota Statutes, Chapter 353D.03, specified plan provision, including the employee and employer contribution rates for those qualified personnel who elect to participate. An eligible elected official who decides to participate contributions 5% of salary which is matched by the elected official's employer. Employees who are paid for their services may elect to make member contributions in an amount not to exceed the employer share. Employer and employee contributions are combined and used to purchase shares in one or more of the seven of the Minnesota Supplemental Investment Fund. For administering the plan, PERA received 2% of employer contributions and twenty-five hundredths of 1% (.0025) of the assets in each member's account annually.

Total contributions made by the City during the fiscal year 2018 were:

Contributions - Employee	\$ 1,138
Contributions - Employer	\$ 1,138
Percentage of Covered Payroll - Employee	5%
Percentage of Covered Payroll - Employer	5%
Require Rate	5%

CITY OF DEER RIVER, MINNESOTA

NOTES TO FINANCIAL STATEMENTS

December 31, 2018

NOTE 10 OTHER POST EMPLOYMENT BENEFITS

Plan Description

Under current contract terms, the City allows retirees to continue to obtain medical insurance through the City's plans with the cost being fully paid by the retiree. As a result, the City has reviewed its other postemployment benefit accruals using the implicit rate subsidy formula.

The City has determined that based on the estimated usage of the retirement benefit and the projected employee retirement rates, that there would be no material impact under the other post employment standards that would impact the financial statements as of December 31, 2018. Accordingly, no provision has been reported in the accompanying financial statements.

NOTE 11 EXPENDITURES IN EXCESS OF BUDGET

The general fund exceeded its budget by \$229,644.

NOTE 12 DEFICIT FUND BALANCES

The following funds had deficit fund balances as of December 31, 2018.

General	\$	268,250
License Bureau		78,389

NOTE 13 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 and natural disasters for which the City carries commercial insurance. There have been no significant reductions in coverage from prior years and settlements have not exceeded coverage in the past three years.

NOTE 14 INTERFUND RECEIVABLES AND PAYABLES

Interfund receivables and payables at December 31, 2018 are as follows:

Major Funds	Due from other funds	Due to other funds
General Fund	\$ -	\$ 219,516
Municipal Forest - Special Revenue Fund	219,516	-
License Bureau - Proprietary Fund	-	15,240
Sewer Fund - Proprietary Fund	15,240	-
	<u>\$ 234,756</u>	<u>\$ 234,756</u>

The Municipal Forest Fund and the Sewer Fund temporarily loaned the general and license bureau money for cash flow purposes. The interfund loans are anticipated to be paid off as cash flow becomes available.

CITY OF DEER RIVER, MINNESOTA

**REQUIRED SUPPLEMENTARY INFORMATION - SCHEDULE OF EMPLOYER'S SHARE OF NET PENSION LIABILITY
AND SCHEDULE OF EMPLOYER CONTRIBUTIONS AND NOTES - PUBLIC EMPLOYEES RETIREMENT ASSOCIATION (PERA) (UNAUDITED)
GENERAL EMPLOYEES RETIREMENT FUND**

December 31, 2018

SCHEDULE OF EMPLOYER'S SHARE OF NET PENSION LIABILITY

Fiscal Year Ending June 30,	City's Proportionate Share of the Net Pension Liability	City's Proportionate Share of the Net Pension Liability	State's Proportionate Share of the Net Pension Liability		City's Covered Payroll	City's Proportionate Share of the NPL (asset) as a Percentage of its Covered Payroll	Plan Fiduciary Net Position as a Percentage of the Total Pension Liability
			Associated with the City	Total			
2018	0.0056%	\$ 310,665	\$ 10,219	\$ 320,884	\$ 377,229	82.35%	79.53%
2017	0.0051%	\$ 325,581	\$ 2,633	\$ 328,214	\$ 344,707	94.45%	75.90%
2016	0.0058%	\$ 470,931	\$ 1,841	\$ 472,772	\$ 346,245	136.01%	68.91%
2015	0.0048%	\$ 248,761	-	\$ 248,761	\$ 279,030	89.15%	78.75%

SCHEDULE OF EMPLOYER'S CONTRIBUTIONS

Year Ending December 31,	Statutorily Required Contribution	Contributions in Relation to the Statutorily Required Contribution	Contribution Deficiency (Excess)	Contributions as a Percentage of Covered Payroll	
				City's Covered Payroll	Contributions as a Percentage of Covered Payroll
2018	\$31,274	\$31,274	-	\$416,980	7.50%
2017	\$26,740	\$26,740	-	\$356,536	7.50%
2016	\$25,763	\$25,763	-	\$343,509	7.50%
2015	\$23,686	\$23,686	-	\$315,814	7.50%

CITY OF DEER RIVER, MINNESOTA

REQUIRED SUPPLEMENTARY INFORMATION - SCHEDULE OF EMPLOYER'S SHARE OF NET PENSION LIABILITY AND SCHEDULE OF EMPLOYER CONTRIBUTIONS AND NOTES - PUBLIC EMPLOYEES RETIREMENT ASSOCIATION (PERA) (UNAUDITED) GENERAL EMPLOYEES RETIREMENT FUND

December 31, 2018

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NOTES TO REQUIRED SUPPLEMENTARY INFORMATION FOR THE FISCAL YEAR ENDING DECEMBER 31, 2018

2018 The mortality projection scale was changed from MP-2015 to MP-2017. The assumed benefit increase was changed from 1% per year through 2044 and 2.5% per year thereafter to 1.25% per year.

2017 The State's special funding contribution increased from \$6 million to \$16 million. The Combined Service Annuity (CSA) loads were changed from 0.8% for active members and 60% for vested and non-vested deferred members. The revised CSA loads are now 0% for active member liability, 15% for vested deferred member liability and 3% for non-vested deferred member. The assumed post-retirement benefit increase rate was changed from 1% per year for all years to 1% per year through 2044 and 2.5% per year thereafter.

2016 The assumed post-retirement benefit increase rate was changed from 1% per year through 2035 and 2.5% per year thereafter to 1% per year for all years. The assumed investment return rate was changed from 7.9% to 7.5%. The single discount rate was changed from 7.9% to 7.5%. Other assumptions were changed pursuant to the experience study dated June 30, 2015. The assumed future salary increases, payroll growth, and inflation were decreased by 0.25% to 3.25% for payroll growth and 2.5% for inflation.

2015 On January 1, 2015, the Minneapolis Employees Retirement Fund was merged into the General Employees Fund, which increased the total pension liability by \$1.1 billion and increased the fiduciary plan net position by \$892 million. Upon consolidation, state and employer contributions were revised; the State's contribution of \$6 million, which meets the special funding situation was due September 2015. The assumed post-retirement benefit increase rate was changed from 1% per year through 2030 and 2.5% per year thereafter to 1% per year through 2035 and 2.5% per year thereafter.

CITY OF DEER RIVER, MINNESOTA

**REQUIRED SUPPLEMENTARY INFORMATION - SCHEDULE OF EMPLOYER'S SHARE OF NET PENSION LIABILITY
AND SCHEDULE OF EMPLOYER CONTRIBUTIONS AND NOTES - PUBLIC EMPLOYEES RETIREMENT ASSOCIATION (PERA) (UNAUDITED)
PUBLIC EMPLOYEES POLICE AND FIRE FUND**

December 31, 2018

SCHEDULE OF EMPLOYER'S SHARE OF NET PENSION LIABILITY

Fiscal Year Ending June 30,	City's Proportionate Share of the Net Pension Liability	City's Proportionate Share of the Net Pension Liability	State's Proportionate Share of the Net Pension Liability Associated with the City	Total	City's Covered Payroll	City's Proportionate Share of the NPL (asset) as a Percentage of its Covered Payroll	Plan Fiduciary Net Position as a Percentage of the Total Pension Liability
2018	0.0210%	\$ 223,838	\$ (1,890)	\$ 221,948	\$ 220,913	101.32%	88.84%
2017	0.0220%	\$ 297,026	\$ (1,980)	\$ 295,046	\$ 236,860	125.40%	75.90%
2016	0.0240%	\$ 963,162	\$ (2,160)	\$ 961,002	\$ 218,790	440.22%	63.88%
2015	0.0220%	\$ 249,971	\$ (1,980)	\$ 247,991	\$ 200,024	124.97%	86.61%

SCHEDULE OF EMPLOYER'S CONTRIBUTIONS

Year Ending December 31,	Statutorily Required Contribution	Contributions in Relation to the Statutorily Required Contribution	Contribution Deficiency (Excess)	City's Covered Payroll	Contributions as a Percentage of Covered Payroll
2018	\$38,739	\$38,739	-	\$239,302	16.20%
2017	\$37,514	\$37,514	-	\$231,570	16.20%
2016	\$35,665	\$35,665	-	\$220,157	16.20%
2015	\$33,976	\$33,976	-	\$209,728	16.20%

CITY OF DEER RIVER, MINNESOTA

REQUIRED SUPPLEMENTARY INFORMATION - SCHEDULE OF EMPLOYER'S SHARE OF NET PENSION LIABILITY AND SCHEDULE OF EMPLOYER CONTRIBUTIONS AND NOTES - PUBLIC EMPLOYEES RETIREMENT ASSOCIATION (PERA) (UNAUDITED) PUBLIC EMPLOYEES POLICE AND FIRE FUND

December 31, 2018

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NOTES TO REQUIRED SUPPLEMENTARY INFORMATION FOR THE FISCAL YEAR ENDING DECEMBER 31, 2018

2018 Actuarial Assumptions: The mortality projection scale was changed from MP-2016 to MP-2017.

2017 Changes in Actuarial Assumptions: The assumed salary increases were changed as recommended in the June 30, 2016 experience study. The net effect is proposed rates that average 0.34 percent lower than the previous rates. Assumed rates of retirement were changed, resulting in fewer retirements. The Combined Service Annuity (CSA) load was 30 percent for vested and non-vested deferred members. The CSA has been changed to 33 percent for vested members and 2 percent for non-vested members. The base mortality table for health annuitants was changed (with a base year of 2006), with male rates adjusted by a factor of 0.96. The mortality improvement scale was changed from Scale AA to Scale MP-2016. The base mortality table for disabled annuitants was changed from the RP-2000 disabled table to the mortality tables assumed for health retirees. Assumed termination rates were decreased to 3.0% for the first three years of service. Rates beyond the select period of three years were adjusted, resulting in more expected terminations overall. Assumed percentage of married female members was decreased from 65 percent to 60 percent. Assumed age difference was changed from separate assumptions for male members (wives assumed to be three years younger) and female members (husbands assumed to be four years older) to the assumption that males are two years older than females. The assumed percentage of female members electing Joint and Survivor annuities was increased. The assumed post-retirement benefit increase rate was changed from 1% for all years to 1% per year through 2064 and 2.5% thereafter.

2016 Changes in Actuarial Assumptions: The assumed post-retirement benefit increase rate was changed from 1% per year through 2037 and 2.5% thereafter to 1% for all future years. The assumed investment return was changed from 7.9% to 7.5%. The single discount rate changed from 7.9% to 5.6%. The assumed future salary increases, payroll growth, and inflation were decreased by .25% to 3.25% for payroll growth and 2.5% for inflation.

2015 Changes in Plan Provisions: The post-retirement benefit increase to be paid after attainment of the 90% funding threshold was changed, from inflation up to 2.5%, to a fixed rate of 2.5%.
Changes in Actuarial Assumptions: The assumed post-retirement benefit increase rate was changed from 1% per year through 2030 and 2.5% thereafter to 1% per year through 2037 and 2.5% thereafter.

CITY OF DEER RIVER, MINNESOTA

**REQUIRED SUPPLEMENTARY INFORMATION - SCHEDULE OF CHANGES IN NET PENSION ASSET AND RELATED RATIO
FIREFIGHTERS RELIEF ASSOCIATION (UNAUDITED)**

December 31, 2018

SCHEDULE OF CHANGES IN NET PENSION ASSET AND RELATED RATIO

	2015	2016	2017	2018
Total Pension Liability				
Service Cost	\$ 22,211	\$ 22,822	\$ 20,033	\$ 25,554
Interest	20,575	21,683	27,031	21,727
Differences between expected and actual experience	-	-	(35,227)	-
Changes in assumptions	-	(18,004)	13,386	(6,783)
Changes in benefit terms	-	-	26,331	-
Benefit payments	(46,500)	-	(35,000)	(90,000)
Net Change in total pension liability	(3,714)	26,501	16,554	(49,502)
Total Pension Liability - Beginning of the year	375,133	371,419	397,920	414,474
Total Pension Liability - End of the year	\$ 371,419	\$ 397,920	\$ 414,474	\$ 364,972
Plan Fiduciary Net Position				
Contributions - municipal and state	\$ 42,189	\$ 37,372	\$ 38,604	\$ 37,142
Contributions - members/donations	-	130	130	-
Net investment returns	25,402	(15,958)	54,818	57,069
Benefit payments	(46,500)	-	(35,000)	(90,000)
Administrative expenses	(1,775)	(2,050)	(1,000)	(1,300)
Net Change in plan fiduciary net position	19,316	19,494	57,552	2,911
Plan Fiduciary Net Position - Beginning of the year	490,152	509,468	528,962	586,514
Net Pension Liability (Asset) - End of the year	\$ 509,468	\$ 528,962	\$ 586,514	\$ 589,425
Net Pension Liability (Asset) - End of the year	(138,049)	(131,042)	(172,040)	(224,453)
Plan Fiduciary Net Position as a % of Total Pension Liability	137.2%	132.9%	141.5%	161.5%
Covered Payroll	na	na	na	na
Net Pension Liability as a % of Covered Payroll	na	na	na	na

Note: This schedule is built prospectively until it contains ten years of data.

CITY OF DEER RIVER, MINNESOTA

**REQUIRED SUPPLEMENTARY INFORMATION - SCHEDULE OF CITY CONTRIBUTIONS AND INVESTMENT RETURNS
FIREFIGHTERS RELIEF ASSOCIATION (UNAUDITED)**

December 31, 2018

SCHEDULE OF CITY'S CONTRIBUTIONS

	Actuarially determined contribution (ADC)	Contributions in Relation to the ADC	Contribution Deficiency (Excess)	Covered Payroll	Contributions as a Percentage of Employee Payroll
2018	na	na	na	na	na
2017	na	na	na	na	na
2016	na	na	na	na	na
2015	na	na	na	na	na

The City does not have a formal funding policy and does not calculate an ADC.

SCHEDULE OF INVESTMENT RETURNS

2018	11.40%
2017	10.80%
2016	(3.1%)
2015	5.50%

Note: This schedule is built prospectively until it contains ten years of data. The above relates to the annual money-weighted rate of return, net investment expense.

NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION

Significant Plan Provision and Actuarial Methods and Assumption Changes - The entry age normal level percent of payroll cost method was used. Under this method, the service cost for an individual participant is the level percentage of pay required to accumulate the funds needed to pay the participant's projected benefits by their assumed retirement age, beginning on the date of entry and ending at the last age before 100% retirement age. The actuarial accrued liability is the accumulated value of those annual services costs on a given date. A straight line amortization method for investment gains and losses was used over a closed 5-year period. Market value of assets were reported as of the measurement date. Liabilities were calculated as of the valuation date and rolled forward to the measurement date using standard actuarial roll-forward techniques per GASB 67 and 68. The liability discount rate was developed using the alternative method described in paragraph 43 of GASB 67. The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimates of expected future real rates of return are developed for each major asset class. These asset class estimates are combined to produce the portfolio long-term expected rate of return by weighting the expected future real rates of return by the current asset allocation percentage and by adding expected inflation.

The following are actuarial assumptions used:

Discount rate	6.00%
Expected long-term rate of return on assets	6.00%
Index rate	3.31%
Inflation rate	2.75%

CITY OF DEER RIVER, MINNESOTA

COMBINING BALANCE SHEET - NON-MAJOR GOVERNMENTAL FUNDS

December 31, 2018

	Special Revenue Fund	Special Revenue Fund	Capital Projects Fund	Total Non-Major Governmental Funds
	Municipal Forest Fund	Community Development Revolving Fund #1	TIF District 1	
Assets				
Cash	\$ 9,485	\$ 1,346	\$ 14,585	\$ 25,416
Notes receivable	-	1,366	-	1,366
Due from other funds	219,516	-	-	219,516
Total Assets	\$ 229,001	\$ 2,712	\$ 14,585	\$ 246,298
Liabilities, Deferred Inflows of Resources, and Fund Balances				
Liabilities				
Accounts Payable	\$ -	\$ -	\$ -	\$ -
Deferred Inflows of Resources				
Notes receivable	-	1,366	-	1,366
Fund balances				
Restricted	-	1,346	14,585	15,931
Committed	229,001	-	-	229,001
Total Fund Balances	229,001	1,346	14,585	244,932
Total Liabilities, Deferred Inflows of Resources, and Fund Balances	\$ 229,001	\$ 2,712	\$ 14,585	\$ 246,298

CITY OF DEER RIVER, MINNESOTA

COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
NON-MAJOR GOVERNMENTAL FUNDS

For the Year Ended December 31, 2018

	Special Revenue Fund	Special Revenue Fund	Capital Projects Fund	Total Non- Major Governmental Funds
	Municipal Forest Fund	Community Development Revolving Fund #1	TIF District 1	
Revenues				
Taxes	-	-	8,465	8,465
Charges for services	12,589	-	-	12,589
Interest earnings	1,189	-	79	1,268
Other revenues	-	240	-	240
Total Revenues	13,778	240	8,544	22,562
Expenditures				
Other	7,360	-	8,465	15,825
Excess of Revenues Over Expenditures	6,418	240	79	6,737
Fund Balance - Beginning of Year	222,583	1,106	14,506	238,195
Fund Balance - End of Year	\$ 229,001	\$ 1,346	\$ 14,585	\$ 244,932

CITY OF DEER RIVER, MINNESOTA**SCHEDULE OF REVENUES - BUDGET AND ACTUAL - GENERAL FUND**

For the Year Ended December 31, 2018

	Budget	Actual	Variance
Property Taxes	\$ 665,619	\$ 678,861	\$ 13,242
Licenses and Permits	17,000	14,600	(2,400)
Intergovernmental			
Local government aid	305,500	305,005	(495)
Other grants and aids	65,411	48,135	(17,276)
Total Intergovernmental	370,911	353,140	(17,771)
Charges for Services	7,100	10,038	2,938
Fines and Forfeitures	12,500	7,525	(4,975)
Other Revenues			
Contributions and donations	4,000	4,970	970
Refunds and reimbursements	54,700	32,013	(22,687)
Other revenues	5,500	2,324	(3,176)
Total Other	64,200	39,307	(24,893)
Total Revenues	\$ 1,137,330	\$ 1,103,471	\$ (33,859)

CITY OF DEER RIVER, MINNESOTA

SCHEDULE OF EXPENDITURES - BUDGET AND ACTUAL - GENERAL FUND

For the Year Ended December 31, 2018

	Budget	Actual	Variance
General Government			
Mayor and council	\$ 58,490	\$ 46,605	\$ 11,885
Administration and finance	222,993	235,820	(12,827)
Elections	2,200	2,456	(256)
Legal	21,000	17,361	3,639
Public buildings	18,300	13,351	4,949
Capital outlay	7,500	-	7,500
Total General Government	330,483	315,593	14,890
Public Safety			
Police protection	497,753	464,181	33,572
Building inspection	9,000	7,404	1,596
Civil defense	700	-	700
Animal control	1,000	264	736
Capital outlay	1,000	1,891	(891)
Total Public Safety	509,453	473,740	35,713
Highways and Streets			
Streets and alleys	221,654	187,781	33,873
Street lighting	20,950	22,333	(1,383)
Capital outlay	11,650	335,023	(323,373)
Total Highways and Streets	254,254	545,137	(290,883)
Culture and Recreation			
Recreation activities and facilities	50,029	44,393	5,636
Capital outlay	5,000	-	5,000
	55,029	44,393	10,636
Total Expenditures	\$ 1,149,219	\$ 1,378,863	\$ (229,644)

CITY OF DEER RIVER, MINNESOTA

COMBINING BALANCE SHEET - SPECIAL REVENUE FUNDS

December 31, 2018

	Fire Department	Municipal Forest	Community Development Revolving Fund #1	Community Development Revolving Fund #2	Total
<i>Assets</i>					
Cash	\$ 536,550	\$ 9,485	\$ 1,346	\$ -	\$ 547,381
Accounts receivable	33	-	-	-	33
Unremitted taxes	677	-	-	-	677
Due from other governments	225	-	-	-	225
Due from other funds	-	219,516	-	-	219,516
Notes receivable	-	-	1,366	526,625	527,991
Total Assets	\$ 537,485	\$ 229,001	\$ 2,712	\$ 526,625	\$ 1,295,823

Liabilities, Deferred Inflows of Resources, and Fund Balance

Liabilities	\$ 2,806	\$ -	\$ -	\$ -	\$ 2,806
Accounts payable					
Deferred Inflows of Resources					
Notes receivable	-	-	1,366	526,625	527,991
Fund Balance					
Restricted	-	-	1,346	-	1,346
Committed	534,679	229,001	-	-	763,680
Total Fund Balance	534,679	229,001	1,346	-	765,026
Total Liabilities, Deferred Inflows of Resources, and Fund Balances	\$ 537,485	\$ 229,001	\$ 2,712	\$ 526,625	\$ 1,295,823

See accompanying notes and auditor's report.

CITY OF DEER RIVER, MINNESOTA

COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN
FUND BALANCES - SPECIAL REVENUE FUNDS

For the Year Ended December 31, 2018

	Fire Department	Municipal Forest	Community Development Revolving Fund #1	Community Development Revolving Fund #2	Total
Revenues					
Property taxes	\$ 30,573	\$ -	\$ -	\$ -	\$ 30,573
Intergovernmental	37,609	-	-	-	37,609
Charges for services	203,264	12,589	-	-	215,853
Interest earnings	2,458	1,189	-	-	3,647
Other revenues	150	-	240	-	390
Total Revenues	274,054	13,778	240	-	288,072
Expenditures					
Salaries and benefits	61,363	-	-	-	61,363
Communications	3,646	-	-	-	3,646
Insurance	10,963	-	-	-	10,963
Other	2,544	7,360	-	-	9,904
Professional services	800	-	-	-	800
Relief Association	38,339	-	-	-	38,339
Repairs and maintenance	3,696	-	-	-	3,696
Supplies	14,122	-	-	-	14,122
Travel and training	7,922	-	-	-	7,922
Utilities	6,936	-	-	-	6,936
Debt service - principal	8,745	-	-	-	8,745
Debt service - interest	1,045	-	-	-	1,045
Capital outlay	13,925	-	-	-	13,925
Total Expenditures	174,046	7,360	-	-	181,406
Excess of Revenues Over Expenditures	100,008	6,418	240	-	106,666
Fund Balance - Beginning of Year	434,671	222,583	1,106	-	658,360
Fund Balance - End of Year	\$ 534,679	\$ 229,001	\$ 1,346	\$ -	\$ 765,026

See accompanying notes and auditor's report.



**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**

To the Honorable Mayor and the Members
Of the City Council
City of Deer River, Minnesota

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, each major fund, the aggregate remaining fund information, and the budgetary analysis of the City of Deer River, Minnesota as of and for the year ended December 31, 2018, and the related notes to the financial statements, which collectively comprise the City of Deer River, Minnesota's basic financial statements and have issued our report thereon dated June 18, 2019.

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.

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 entity's financial statements will not be prevented or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify certain deficiencies in internal control, described in the following paragraphs that we consider to be significant deficiencies. (2018-001 and 2018-002)

Finding 2018-001 Lack of segregation of duties

One staff person is primarily responsible for receipting, disbursements, reconciling, and reporting financial information. This same individual has the ability to make entries into the financial records. The individual has access to all general ledger functions. In addition, several staff have access to receipting, depositing and reconciling functions.

Condition: The City does not have an adequate segregation of duties due to a limited number of staff.

Criteria: Internal controls should be in place to provide adequate segregation of duties.

Effect: The lack of segregation of duties is identified as a deficiency in the design or operation of the internal control over financial reporting that could adversely affect the City's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

Prevalence: The situation is common among governments of similar size.

Recommendation: The Council needs to be cognizant of this situation and determine appropriate oversight responsibility as it deems appropriate.

City's response: The City is aware of the situation and the Council members perform reasonable and periodic inquiries over financial operations as they deem appropriate. Selected financial information is presented for review at Council meetings.

Finding 2018-002 The City requested assistance with preparation of the financial statements and related notes

Condition: The City does not have in place a system to prepare the financial reports in accordance with generally accepted accounting principles under GASB 34 presentation.

Criteria: The City should have a system in place to report all financial data reliably in accordance with generally accepted accounting principles using the presentation model required under GASB 34. Currently there is more than a remote likelihood that a misstatement in the financial statement reporting including footnote disclosures that are more than inconsequential will not be presented accordingly.

Effect: The City requests assistance with the preparation of the draft financial statements and footnotes.

Prevalence: The situation is common in governments of similar size.

Recommendation: The staff continue to take advantage of training opportunities in GAAP and GASB presentation methods and models.

City's response: The City is aware of the situation and due to budget constraints deems it more cost beneficial to contract for such services.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City of Deer River, Minnesota'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 that are required to be reported under *Government Auditing Standards*.

City of Deer River's Responses to Findings

The City's responses to the findings identified in our audit are described previously. The City of Deer River, Minnesota'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.

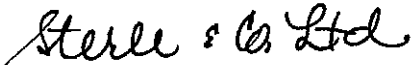
Minnesota Legal Compliance

The *Minnesota Legal Compliance Audit Guide for Cities*, promulgated by the State Auditor pursuant to Minn. Stat. Section 6.65, contains seven categories of compliance to be tested: Contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, TIF reporting and miscellaneous provisions. Our study included all of the listed categories.

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

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.



June 18, 2019