

STATE OF MINNESOTA

Office of the State Auditor



Rebecca Otto
State Auditor

CITY OF FLENSBURG
FLENSBURG, MINNESOTA

YEARS ENDED DECEMBER 31, 2016 AND 2017

Description of the Office of the State Auditor

The mission of the Office of the State Auditor is to oversee local government finances for Minnesota taxpayers by helping to ensure financial integrity and accountability in local governmental financial activities.

Through financial, compliance, and special audits, the State Auditor oversees and ensures that local government funds are used for the purposes intended by law and that local governments hold themselves to the highest standards of financial accountability.

The State Auditor performs approximately 150 financial and compliance audits per year and has oversight responsibilities for over 3,300 local units of government throughout the state. The office currently maintains five divisions:

Audit Practice - conducts financial and legal compliance audits of local governments;

Government Information - collects and analyzes financial information for cities, towns, counties, and special districts;

Legal/Special Investigations - provides legal analysis and counsel to the Office and responds to outside inquiries about Minnesota local government law; as well as investigates allegations of misfeasance, malfeasance, and nonfeasance in local government;

Pension - monitors investment, financial, and actuarial reporting for approximately 650 public pension funds; and

Tax Increment Financing - promotes compliance and accountability in local governments' use of tax increment financing through financial and compliance audits.

The State Auditor serves on the State Executive Council, State Board of Investment, Land Exchange Board, Public Employees Retirement Association Board, Minnesota Housing Finance Agency, and the Rural Finance Authority Board.

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**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

Years Ended December 31, 2016 and 2017



**Audit Practice Division
Office of the State Auditor
State of Minnesota**

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**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

TABLE OF CONTENTS

	<u>Exhibit</u>	<u>Page</u>
Introductory Section		
Organization - 2016		1
Organization - 2017		2
Financial Section		
Independent Auditor's Report		3
2016 Basic Financial Statements		
Fund Financial Statements		
Governmental Funds		
Statement of Balances Arising from Cash Transactions	1	6
Statement of Cash Receipts, Disbursements, and Changes in Cash Fund Balances	2	7
Proprietary Funds		
Statement of Balances Arising from Cash Transactions	3	8
Statement of Cash Receipts, Disbursements, and Changes in Net Cash Assets	4	9
Statement of Cash Flows	5	10
2017 Basic Financial Statements		
Fund Financial Statements		
Governmental Funds		
Statement of Balances Arising from Cash Transactions	6	11
Statement of Cash Receipts, Disbursements, and Changes in Cash Fund Balances	7	12
Proprietary Funds		
Statement of Balances Arising from Cash Transactions	8	13
Statement of Cash Receipts, Disbursements, and Changes in Net Cash Assets	9	14
Statement of Cash Flows	10	15
Notes to the Financial Statements		16

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

TABLE OF CONTENTS

	<u>Exhibit</u>	<u>Page</u>
Financial Section (Continued)		
2016 Supplementary Information		
Budgetary Comparison Schedules		
General Fund - Regulatory Basis	A-1	37
Fire Special Revenue Fund - Regulatory Basis	A-2	38
Schedule of Intergovernmental Receipts	A-3	39
2017 Supplementary Information		
Budgetary Comparison Schedules		
General Fund - Regulatory Basis	A-4	40
Fire Special Revenue Fund - Regulatory Basis	A-5	41
Schedule of Intergovernmental Receipts	A-6	42
Other Information Section		
Schedule of Accounts Receivable - 2016	B-1	43
Schedule of Accounts Payable - 2016	B-2	43
Schedule of Indebtedness - 2016	B-3	44
Schedule of Accounts Receivable - 2017	B-4	45
Schedule of Accounts Payable - 2017	B-5	45
Schedule of Indebtedness - 2017	B-6	46
Management and Compliance Section		
Communication of Significant Deficiencies and/or Material Weaknesses in Internal Control Over Financial Reporting and Other Matters		47
Independent Auditor's Report on Minnesota Legal Compliance		49
Schedule of Findings and Recommendations		51

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**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

ORGANIZATION
2016

<u>Office</u>	<u>Name</u>	<u>Term Expires</u>
City Council		
Elected		
Mayor	John Gessell, Jr.	January 2017
Council Member	Kenneth Merten	January 2017
Council Member	LuAnn Morrow	January 2017
Council Member	Rebecca Piekarski	January 2019
Council Member	Michael Zupko	January 2019
Officers		
Appointed		
Clerk/Treasurer	Margurite Cofell	Indefinite

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

ORGANIZATION
2017

<u>Office</u>	<u>Name</u>	<u>Term Expires</u>
City Council		
Elected		
Mayor	John Gessell, Jr.	January 2019
Council Member	Kenneth Merten	January 2021
Council Member	LuAnn Morrow	January 2021
Council Member	Brad Pederson ¹	January 2019
Council Member	Michael Zupko	January 2019
Officers		
Appointed		
Clerk/Treasurer	Margurite Cofell	Indefinite

¹Appointed to fill the unexpired term of Rebecca Piekarski

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REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA

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INDEPENDENT AUDITOR'S REPORT

The Honorable Mayor
and Members of the City Council
City of Flensburg
Flensburg, Minnesota

Report on the Financial Statements

We have audited the accompanying cash basis financial statements of each major fund of the City of Flensburg, Minnesota, as of and for the years ended December 31, 2016 and 2017, 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 financial reporting provisions of accounting practices prescribed or permitted by the Office of the State Auditor, as described in Note 1.C., to meet the requirements of the Office of the State Auditor. Management is also responsible for 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the City's preparation and fair presentation of the financial statements in order to design

audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Basis for Adverse Opinions on U.S. Generally Accepted Accounting Principles

As discussed in Note 1.C. to the financial statements, the financial statements of the City of Flensburg are prepared by the City on the basis of financial reporting provisions of accounting practices prescribed or permitted by the Office of the State Auditor, which is a basis of accounting other than accounting principles generally accepted in the United States of America, to meet the requirements of the Office of the State Auditor. The effects on the financial statements of the variances between the basis of accounting described in Note 1.C. and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

Adverse Opinions on U.S. Generally Accepted Accounting Principles

In our opinion, because of the effects of the matter described in the "Basis for Adverse Opinions on U.S. Generally Accepted Accounting Principles" paragraph, the financial statements do not present fairly, in all material respects, the financial position of each major fund of the City of Flensburg as of December 31, 2016 and 2017, or the changes in financial position or, where applicable, cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Unmodified Opinions on Regulatory Basis of Accounting

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the cash balances of each major fund of the City of Flensburg as of December 31, 2016 and 2017, and the respective cash receipts and disbursements and, where applicable, cash flows thereof for the years then ended in accordance with financial reporting provisions of accounting practices prescribed or permitted by the Office of the State Auditor as discussed Note 1.C.

Other Matters

Supplementary and Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Flensburg's basic financial statements. The supplementary and other information as listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. 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 basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

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

/s/Rebecca Otto

REBECCA OTTO
STATE AUDITOR

October 23, 2018

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

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2016 BASIC FINANCIAL STATEMENTS

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FUND FINANCIAL STATEMENTS

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GOVERNMENTAL FUNDS

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**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT 1

**STATEMENT OF BALANCES ARISING FROM CASH TRANSACTIONS
GOVERNMENTAL FUNDS
DECEMBER 31, 2016**

	General Fund	Fire Fund	Total Governmental Funds
<u>Assets</u>			
Cash	<u>\$ 69,575</u>	<u>\$ 9,823</u>	<u>\$ 79,398</u>
 <u>Cash Fund Balances</u>			
Assigned for public safety	\$ -	\$ 9,823	\$ 9,823
Unassigned	<u>69,575</u>	<u>-</u>	<u>69,575</u>
Total Cash Fund Balances	<u>\$ 69,575</u>	<u>\$ 9,823</u>	<u>\$ 79,398</u>

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT 2

**STATEMENT OF CASH RECEIPTS, DISBURSEMENTS,
AND CHANGES IN CASH FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2016**

	<u>General Fund</u>	<u>Fire Fund</u>	<u>Total Governmental Funds</u>
Receipts			
Property taxes	\$ 31,987	\$ 7,699	\$ 39,686
Licenses, permits, and fees	74	-	74
Intergovernmental	34,196	22,194	56,390
Charges for services	1,735	-	1,735
Contributions	2,500	4,700	7,200
Miscellaneous	3,422	-	3,422
	<u>3,422</u>	<u>-</u>	<u>3,422</u>
Total Receipts	<u>\$ 73,914</u>	<u>\$ 34,593</u>	<u>\$ 108,507</u>
Disbursements			
Current			
General government			
City Clerk	\$ 11,978	\$ -	\$ 11,978
Council	1,345	-	1,345
Mayor	554	-	554
Other general government	38,143	-	38,143
	<u>38,143</u>	<u>-</u>	<u>38,143</u>
Total general government	<u>\$ 52,020</u>	<u>\$ -</u>	<u>\$ 52,020</u>
Public safety			
Fire	-	25,720	25,720
Public works			
Street maintenance and storm sewers	11,269	-	11,269
Debt service			
Principal	15,500	-	15,500
Capital outlay	<u>-</u>	<u>17,400</u>	<u>17,400</u>
Total Disbursements	<u>\$ 78,789</u>	<u>\$ 43,120</u>	<u>\$ 121,909</u>
Receipts Over (Under) Disbursements	<u>\$ (4,875)</u>	<u>\$ (8,527)</u>	<u>\$ (13,402)</u>
Other Financing Sources (Uses)			
Loans issued	<u>15,500</u>	<u>3,000</u>	<u>18,500</u>
Net Change in Cash Fund Balances	<u>\$ 10,625</u>	<u>\$ (5,527)</u>	<u>\$ 5,098</u>
Cash Fund Balances, January 1	<u>58,950</u>	<u>15,350</u>	<u>74,300</u>
Cash Fund Balances, December 31	<u><u>\$ 69,575</u></u>	<u><u>\$ 9,823</u></u>	<u><u>\$ 79,398</u></u>

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

Page 7

PROPRIETARY FUNDS

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**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT 3

**STATEMENT OF BALANCES ARISING FROM CASH TRANSACTIONS
PROPRIETARY FUNDS
DECEMBER 31, 2016**

	Enterprise Funds			
	Sewer Fund	Refuse and Recycling Fund	Liquor Fund	Total Proprietary Funds
<u>Assets</u>				
Cash	\$ 8,064	\$ -	\$ -	\$ 8,064
<u>Liabilities and Net Cash Assets</u>				
Liabilities				
Overdraft of cash	\$ -	\$ 4,810	\$ 81,491	\$ 86,301
Net Cash Assets				
Unrestricted	8,064	(4,810)	(81,491)	(78,237)
Total Liabilities and Net Cash Assets	\$ 8,064	\$ -	\$ -	\$ 8,064

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT 4

**STATEMENT OF CASH RECEIPTS, DISBURSEMENTS,
AND CHANGES IN NET CASH ASSETS
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2016**

	<u>Enterprise Funds</u>			<u>Total Proprietary Funds</u>
	<u>Sewer Fund</u>	<u>Refuse and Recycling Fund</u>	<u>Liquor Fund</u>	
Operating Receipts				
Charges for services	\$ 9,803	\$ 14,108	\$ -	\$ 23,911
Sales	-	-	329,682	329,682
Less: cost of sales	-	-	(163,419)	(163,419)
Miscellaneous	-	-	2,163	2,163
Total Operating Receipts	\$ 9,803	\$ 14,108	\$ 168,426	\$ 192,337
Operating Disbursements				
Personnel services	\$ 2,358	\$ -	\$ 116,212	\$ 118,570
Professional services	862	17,291	3,947	22,100
Utilities	1,677	-	15,657	17,334
Repairs and maintenance	-	-	1,338	1,338
Supplies	-	-	674	674
Other	600	-	20,620	21,220
Total Operating Disbursements	\$ 5,497	\$ 17,291	\$ 158,448	\$ 181,236
Operating Income (Loss)	\$ 4,306	\$ (3,183)	\$ 9,978	\$ 11,101
Nonoperating Receipts (Disbursements)				
Interest paid	-	-	(5,786)	(5,786)
Net Income (Loss) Before Other Receipts (Disbursements)	\$ 4,306	\$ (3,183)	\$ 4,192	\$ 5,315
Other Receipts (Disbursements)				
Loans issued	\$ -	\$ -	\$ 10,000	\$ 10,000
Debt principal paid	-	-	(15,211)	(15,211)
Total Other Receipts (Disbursements)	\$ -	\$ -	\$ (5,211)	\$ (5,211)
Change in Net Cash Assets	\$ 4,306	\$ (3,183)	\$ (1,019)	\$ 104
Net Cash Assets, January 1	3,758	(1,627)	(80,472)	(78,341)
Net Cash Assets, December 31	\$ 8,064	\$ (4,810)	\$ (81,491)	\$ (78,237)

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT 5

**STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2016**

	<u>Enterprise Funds</u>			<u>Total Proprietary Funds</u>
	<u>Sewer Fund</u>	<u>Refuse and Recycling Fund</u>	<u>Liquor Fund</u>	
Cash Flows from Operating Activities				
Receipts from customers	\$ 9,803	\$ 14,108	\$ 329,682	\$ 353,593
Payments to suppliers	(3,139)	(17,291)	(205,655)	(226,085)
Payments to employees	(2,358)	-	(116,212)	(118,570)
Other receipts	-	-	2,163	2,163
Net cash provided by (used in) operating activities	<u>\$ 4,306</u>	<u>\$ (3,183)</u>	<u>\$ 9,978</u>	<u>\$ 11,101</u>
Cash Flows from Noncapital Financing Activities				
Proceeds from loan	\$ -	\$ -	\$ 10,000	\$ 10,000
Principal paid on debt	-	-	(15,211)	(15,211)
Interest paid on debt	-	-	(5,786)	(5,786)
Net cash provided by (used in) noncapital financing activities	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (10,997)</u>	<u>\$ (10,997)</u>
Net Increase (Decrease) in Cash and Overdraft in Cash	<u>\$ 4,306</u>	<u>\$ (3,183)</u>	<u>\$ (1,019)</u>	<u>\$ 104</u>
Cash and Overdraft of Cash, January 1	<u>3,758</u>	<u>(1,627)</u>	<u>(80,472)</u>	<u>(78,341)</u>
Cash and Overdraft of Cash, December 31	<u>\$ 8,064</u>	<u>\$ (4,810)</u>	<u>\$ (81,491)</u>	<u>\$ (78,237)</u>

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2017 BASIC FINANCIAL STATEMENTS

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FUND FINANCIAL STATEMENTS

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GOVERNMENTAL FUNDS

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**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT 6

**STATEMENT OF BALANCES ARISING FROM CASH TRANSACTIONS
GOVERNMENTAL FUNDS
DECEMBER 31, 2017**

	General Fund	Fire Fund	Total Governmental Funds
<u>Assets</u>			
Cash	\$ 31,316	\$ 23,513	\$ 54,829
<u>Cash Fund Balances</u>			
Assigned for public safety	\$ -	\$ 23,513	\$ 23,513
Unassigned	31,316	-	31,316
Total Cash Fund Balances	\$ 31,316	\$ 23,513	\$ 54,829

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT 7

**STATEMENT OF CASH RECEIPTS, DISBURSEMENTS,
AND CHANGES IN CASH FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2017**

	<u>General Fund</u>	<u>Fire Fund</u>	<u>Total Governmental Funds</u>
Receipts			
Property taxes	\$ 51,528	\$ 12,403	\$ 63,931
Licenses, permits, and fees	1,950	-	1,950
Intergovernmental	5,113	23,312	28,425
Charges for services	2,399	-	2,399
Contributions	-	4,000	4,000
Miscellaneous	2,823	434	3,257
Total Receipts	\$ 63,813	\$ 40,149	\$ 103,962
Disbursements			
Current			
General government			
City Clerk	\$ 9,055	\$ -	\$ 9,055
Council	2,057	-	2,057
Mayor	647	-	647
Other general government	30,051	-	30,051
Total general government	\$ 41,810	\$ -	\$ 41,810
Public safety			
Fire	-	28,959	28,959
Public works			
Street maintenance and storm sewers	14,606	-	14,606
Debt service			
Principal	19,155	-	19,155
Total Disbursements	\$ 75,571	\$ 28,959	\$ 104,530
Receipts Over (Under) Disbursements	\$ (11,758)	\$ 11,190	\$ (568)
Other Financing Sources (Uses)			
Loans issued	\$ 19,155	\$ -	\$ 19,155
Proceeds from the sale of capital assets	-	2,500	2,500
Transfers out	(45,656)	-	(45,656)
Total Other Financing Sources (Uses)	\$ (26,501)	\$ 2,500	\$ (24,001)
Net Change in Cash Fund Balances	\$ (38,259)	\$ 13,690	\$ (24,569)
Cash Fund Balances, January 1	69,575	9,823	79,398
Cash Fund Balances, December 31	\$ 31,316	\$ 23,513	\$ 54,829

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

Page 12

PROPRIETARY FUNDS

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**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT 8

**STATEMENT OF BALANCES ARISING FROM CASH TRANSACTIONS
PROPRIETARY FUNDS
DECEMBER 31, 2017**

	Enterprise Funds		
	Sewer Fund	Refuse and Recycling Fund	Total Proprietary Funds
<u>Assets</u>			
Cash	\$ -	\$ -	\$ -
<u>Liabilities and Net Cash Assets</u>			
Liabilities			
Overdraft of cash	\$ 11,444	\$ 22,434	\$ 33,878
Net Cash Assets			
Unrestricted	(11,444)	(22,434)	(33,878)
Total Liabilities and Net Cash Assets	\$ -	\$ -	\$ -

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT 9

**STATEMENT OF CASH RECEIPTS, DISBURSEMENTS,
AND CHANGES IN NET CASH ASSETS
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2017**

	Enterprise Funds			Total Proprietary Funds
	Sewer Fund	Refuse and Recycling Fund	Liquor Fund	
Operating Receipts				
Charges for services	\$ 8,001	\$ 5,504	\$ -	\$ 13,505
Sales	-	-	226,841	226,841
Less: cost of sales	-	-	(111,543)	(111,543)
Miscellaneous	-	-	823	823
Total Operating Receipts	\$ 8,001	\$ 5,504	\$ 116,121	\$ 129,626
Operating Disbursements				
Personnel services	\$ 4,807	\$ -	\$ 121,306	\$ 126,113
Professional services	8,396	15,144	7,954	31,494
Utilities	1,263	-	18,934	20,197
Repairs and maintenance	11,516	-	858	12,374
Supplies	-	-	1,183	1,183
Other	380	9,584	11,187	21,151
Total Operating Disbursements	\$ 26,362	\$ 24,728	\$ 161,422	\$ 212,512
Operating Income (Loss)	\$ (18,361)	\$ (19,224)	\$ (45,301)	\$ (82,886)
Nonoperating Receipts (Disbursements)				
Intergovernmental	\$ -	\$ 1,600	\$ -	\$ 1,600
Interest paid	(1,147)	-	-	(1,147)
Total Nonoperating Receipts (Disbursements)	\$ (1,147)	\$ 1,600	\$ -	\$ 453
Net Income (Loss) Before Other Receipts (Disbursements)	\$ (19,508)	\$ (17,624)	\$ (45,301)	\$ (82,433)
Other Receipts (Disbursements)				
Transfers in	\$ -	\$ -	\$ 45,656	\$ 45,656
Special item (Note 6)	-	-	131,444	131,444
Loans issued	25,000	-	-	25,000
Debt principal paid	(25,000)	-	(50,308)	(75,308)
Total Other Receipts (Disbursements)	\$ -	\$ -	\$ 126,792	\$ 126,792
Change in Net Cash Assets	\$ (19,508)	\$ (17,624)	\$ 81,491	\$ 44,359
Net Cash Assets, January 1	8,064	(4,810)	(81,491)	(78,237)
Net Cash Assets, December 31	\$ (11,444)	\$ (22,434)	\$ -	\$ (33,878)

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

Page 14

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT 10

**STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2017**

	Enterprise Funds			Total Proprietary Funds
	Sewer Fund	Refuse and Recycling Fund	Liquor Fund	
Cash Flows from Operating Activities				
Receipts from customers	\$ 8,001	\$ 5,504	\$ 226,841	\$ 240,346
Payments to suppliers	(21,555)	(24,728)	(151,659)	(197,942)
Payments to employees	(4,807)	-	(121,306)	(126,113)
Other receipts	-	-	823	823
Net cash provided by (used in) operating activities	\$ (18,361)	\$ (19,224)	\$ (45,301)	\$ (82,886)
Cash Flows from Noncapital Financing Activities				
Proceeds from loan	\$ 25,000	\$ -	\$ -	\$ 25,000
Transfers in	-	-	45,656	45,656
Intergovernmental	-	1,600	-	1,600
Principal paid on debt	(25,000)	-	(50,308)	(75,308)
Interest paid on debt	(1,147)	-	-	(1,147)
Net cash provided by (used in) noncapital financing activities	\$ (1,147)	\$ 1,600	\$ (4,652)	\$ (4,199)
Cash Flows from Capital and Related Financing Activities				
Proceeds from sale of capital assets	\$ -	\$ -	\$ 131,444	\$ 131,444
Net Increase (Decrease) in Cash and Overdraft in Cash	\$ (19,508)	\$ (17,624)	\$ 81,491	\$ 44,359
Cash and Overdraft of Cash, January 1	8,064	(4,810)	(81,491)	(78,237)
Cash and Overdraft of Cash, December 31	\$ (11,444)	\$ (22,434)	\$ -	\$ (33,878)

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

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**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

NOTES TO THE FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2017

1. Summary of Significant Accounting Policies

A. Financial Reporting Entity

The City of Flensburg, Minnesota, (the City) is a statutory city that has a mayor-council form of government that is governed by an elected mayor and a four-member council. The City provides the following services: sewer, refuse and recycling, recreation, municipal liquor store, public improvements, public safety, and general administrative services.

The accompanying financial statements present the City and its component units. The City includes all funds, organizations, institutions, agencies, departments, and offices that are not legally separate from it. Component units are legally separate entities for which the City is financially accountable, or for which the exclusion of the component unit would render the financial statements of the City misleading.

The criteria used to determine if the City is financially accountable for a component unit includes whether or not (1) the City appoints the voting majority of the potential component unit's governing body and is able to impose its will on the potential component unit or is in a relationship of financial benefit or burden with the potential component unit; or (2) the potential component unit is fiscally dependent on and there is a potential of the potential component unit to provide specific financial benefits to, or impose specific financial burdens on, the City.

As a result of applying the criteria above, the City of Flensburg has no component units.

B. Basis of Presentation

Fund Financial Statements

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

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

1. Summary of Significant Accounting Policies

B. Basis of Presentation

Fund Financial Statements (Continued)

The City reports the following major governmental funds:

- The General Fund is the City's primary operating fund. It accounts for all financial resources of the general government, except those accounted for in another fund.
- The Fire Fund is a special revenue fund used to account for specific intergovernmental receipts from the state government, as well as assigned property tax receipts for the operation of the City's fire department.

The City reports the following major proprietary funds:

- The Sewer Fund is used to account for sewer service charges, which are used to finance the sewer system operating costs.
- The Refuse and Recycling Fund is used to account for refuse and recycling service charges, which are used to finance contracted collection of refuse and recycling.
- The Liquor Fund is used to account for receipts from sales to customers, which are used to finance the municipal liquor store operations and activities.

C. Measurement Focus and Basis of Accounting

The City of Flensburg follows the regulatory basis of accounting for all funds. The accompanying financial statements were prepared on the regulatory basis of accounting in accordance with financial reporting provisions of accounting practices prescribed or permitted as described in the Office of the State Auditor's *Reporting and Publishing Requirements for City Audited Financial Statements for Cities Under 2,500 in Population Reporting on the Cash or Regulatory Basis of Accounting*. Under this regulatory basis of accounting, in the governmental and proprietary fund statements, receipts are recognized when received rather than when measurable and available, and disbursements are recognized when paid rather than when the obligation is incurred. These statements do not give effect to receivables, payables, accrued expenses, and inventories and, accordingly, are not presented in accordance with accounting principles generally accepted in the United States of America. Other differences from accounting

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

1. Summary of Significant Accounting Policies

C. Measurement Focus and Basis of Accounting (Continued)

principles generally accepted in the United States of America result from the City omitting a management's discussion and analysis, a government-wide statement of net position, and a government-wide statement of activities, and the City not recognizing governmental fund receipts and disbursements in accordance with the modified accrual basis of accounting or proprietary fund receipts and disbursements in accordance with the full accrual basis of accounting.

D. Assets, Liabilities, Cash Fund Balance, and Net Cash Assets

1. Cash

For purposes of the Statement of Cash Flows, "cash" includes all cash on hand, demand and savings accounts, and certificates of deposit with an original maturity of three months or less from the date of acquisition. Certificates of deposit are stated at cost, which approximates fair value.

Negative cash is shown as "overdraft of cash" in the liability section of the Statement of Balances Arising from Cash Transactions. See Note 2.C. and Note 3.B. for additional information.

2. Long-Term Debt

Long-term debt is not reported as liabilities in the fund financial statements. The debt proceeds are reported as other financing sources, and payment of principal and interest are reported as disbursements in governmental funds. In proprietary funds, debt proceeds and payment of principal and interest are reported as other receipts and disbursements. Bond premiums and discounts, as well as bond issuance costs, if any, are recognized during the current period.

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, Cash Fund Balance, and Net Cash Assets (Continued)

3. Classification of Cash Fund Balance

In the governmental fund financial statements, cash fund balance is divided into four classifications--restricted, committed, assigned, and unassigned--based primarily on the extent to which the City of Flensburg is bound to observe constraints imposed upon the use of the resources reported in the governmental funds. The classifications are as follows:

- Restricted - amounts in which constraints have been placed on the use of resources either externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments, or imposed by law through constitutional provisions or enabling legislation.
- Committed - amounts that can be used only for the specific purposes imposed by formal action (resolution) of the City Council. Those committed amounts cannot be used for any other purpose unless the City Council removes or changes the specified use by taking the same type of action (resolution) it employed to previously commit those amounts.
- Assigned - amounts the City intends to use for specific purposes that do not meet the criteria to be classified as restricted or committed. In governmental funds other than the General Fund, assigned cash fund balance represents the remaining amount that is not restricted or committed. In the General Fund, assigned amounts represent intended uses established by the City Council.
- Unassigned - the residual classification for the General Fund and includes all remaining amounts not contained in the other cash fund balance classifications. In other governmental funds, the unassigned classification is used only to report a deficit balance resulting from overspending for specific purposes for which amounts had been restricted or committed.

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, Cash Fund Balance, and Net Cash Assets

3. Classification of Cash Fund Balance (Continued)

When a disbursement is incurred for which the City may use either restricted or unrestricted cash fund balance, the City uses restricted resources first unless unrestricted cash fund balances (committed, assigned, and unassigned) will have to be returned because they were not used. Similarly, within unrestricted cash fund balances, when a disbursement is incurred for purposes for which amounts in any unrestricted cash fund balance could be used, the City uses cash fund balances in the following order: committed, assigned, though the City does not have a formal policy addressing this.

The City does not have a minimum cash fund balance policy for its governmental funds.

4. Classification of Net Cash Assets

In the proprietary fund financial statements, net cash assets represent the difference between assets and liabilities. Net cash assets is classified in the following categories:

- Restricted - the amount of net cash assets for which external restrictions have been imposed by creditors, grantors, contributors, or laws or regulations of other governments and restrictions imposed by law through constitutional provisions or enabling legislation.
- Unrestricted - the amount of net cash assets that does not meet the definition of restricted.

The City does not have a formal policy addressing which category of net cash assets is to be applied first when a disbursement is incurred for which both restricted or unrestricted net cash assets is available.

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

1. Summary of Significant Accounting Policies (Continued)

E. Receipts and Disbursements

1. Property Taxes

Under state law, municipalities are limited in their ability to levy a property tax. The City levies its property tax for the subsequent year during the month of September. Morrison County is the collecting agency for the levy and remits the collections to the City. The City receives its taxes in three installments in January, June, and November of the following year. Delinquent collections are remitted to the City with each settlement. In the fund financial statements, property taxes are recorded as receipts in the period levied to the extent they are collected.

December 31 is the last day the City can certify a tax levy to the County Auditor for collection the following year. The County Auditor prepares the tax list for all taxable property in the City and applies the applicable tax rate to the tax capacity of individual properties to arrive at the actual tax for each property. The County Auditor also collects all special assessments, except for certain prepayments paid directly to the City. The County Auditor remits a list of taxes and special assessments to be collected on each parcel of property to the County Treasurer in January of each year. The County Treasurer collects all taxes and assessments, except as noted above. The County Treasurer mails copies of all real estate and personal property tax statements. Each year, property owners are required to pay one half of their real estate taxes by May 15 and the balance by October 15. Penalties and interest are assessed to property owners who do not pay their property taxes and special assessments by the due dates.

2. Intergovernmental Receipts

The property tax levies in 2016 and 2017 include certain state credits, which are distributed to the City directly by the state. These credits are classified as intergovernmental receipts.

Also included in intergovernmental receipts is local government aid which is distributed to the City directly by the state. During 2016, the City received \$28,272 in local government aid. During 2017, the City received no local government aid.

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

1. Summary of Significant Accounting Policies

E. Receipts and Disbursements (Continued)

3. Operating Receipts and Disbursements

Proprietary funds distinguish operating receipts and disbursements from nonoperating items. Operating receipts and disbursements generally result from providing services and producing and delivering goods and/or services in connection with a proprietary fund's principal ongoing operations. Operating disbursements for proprietary funds include the cost of sales and services and administrative expense. All receipts and disbursements not meeting this definition are reported as nonoperating items, which include receipts and disbursements related to capital and related financing, noncapital financing, or investing activities.

4. Disbursements

In the fund financial statements, disbursements are classified as follows:

Governmental funds by:

Character
Function
Activity

Proprietary funds by:

Operating and nonoperating

In the fund financial statements, governmental funds report disbursements of financial resources.

F. Use of Estimates

The preparation of financial statements in conformity with the regulatory basis of accounting could require management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of receipts and disbursements during the reporting period. Actual results could differ from those estimates.

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

2. Stewardship, Compliance and Accountability

A. Budgetary Information

The City Council adopts an annual budget. The amounts shown in the financial statements as “budget” represent the original budgeted amounts and all revisions made during the year. The City follows these procedures in establishing the budgetary data reflected in the financial statements:

1. Prior to October 1, the City Clerk/Treasurer submits to the City Council a proposed operating budget for the fiscal year commencing the following January 1. The operating budget includes proposed disbursements and the means of financing them.
2. Public hearings are conducted to obtain taxpayer comments.
3. The budget is legally enacted through City Council action after obtaining taxpayer comments. The action approved by the City Council sets forth the budgets at the function level for the General Fund and the Fire Fund.
4. Budgets for the General Fund and the Fire Fund are adopted on the regulatory basis of accounting in accordance with the Office of the State Auditor.
5. Disbursements may not legally exceed budgeted appropriations at the department level. No fund’s budget can be increased without City Council approval. The City Council may authorize transfer of budgeted amounts between departments within any fund. Management may amend budgets within a fund/department level, so long as the total fund/department budget is not changed.
6. An annual appropriated budget is adopted during the year for the General Fund and the Fire Fund.

Budgeted amounts are as originally adopted or as amended by the City Council. Over the course of the year, the City Council may revise estimated receipt and disbursement budgets. These budget amendments fall into three categories: new information changing original budget estimations, greater than anticipated receipts or costs, and new grant awards. Budgeted disbursement appropriations lapse at year-end.

There were no individual amendments to the original amounts budgeted for 2016 or 2017.

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

2. Stewardship, Compliance and Accountability (Continued)

B. Disbursements Exceeding Appropriations

The following funds had disbursements that exceeded appropriations for the year ended December 31, 2016:

	<u>Disbursements</u>	<u>Final Budget</u>	<u>Excess</u>
General Fund	\$ 78,789	\$ 71,400	\$ 7,389
Fire Special Revenue Fund	43,120	-	43,120

The following fund had disbursements that exceeded appropriations for the year ended December 31, 2017:

	<u>Disbursements</u>	<u>Final Budget</u>	<u>Excess</u>
Fire Special Revenue Fund	\$ 28,959	\$ -	\$ 28,959

C. Deficit Net Cash Assets

The following proprietary funds had deficit net cash assets as of December 31, 2016:

Refuse and Recycling Fund	\$ 4,810
Liquor Fund	81,491

The following proprietary funds had deficit net cash assets as of December 31, 2017:

Sewer Fund	\$ 11,444
Refuse and Recycling Fund	22,434

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

The following table presents the City's cash and deposit balances at December 31, 2016 and 2017:

	<u>2016</u>	<u>2017</u>
Checking	<u>\$ 1,161</u>	<u>\$ 20,951</u>

During the years ended December 31, 2016 and 2017, the City had no investments.

a. Deposits

The City is authorized by Minn. Stat. §§ 118A.02 and 118A.04 to designate a depository for public funds and to invest in certificates of deposit. The City is required by Minn. Stat. § 118A.03 to protect deposits with insurance, surety bond, or collateral. The market value of collateral pledged shall be at least ten percent more than the amount on deposit at the close of the financial institution's banking day that is not covered by insurance or bonds, except that where the collateral is irrevocable standby letters of credit issued by Federal Home Loan Banks, the amount shall be at least equal to the excess amount on deposit at the close of the financial institution's banking day.

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

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

3. Detailed Notes

A. Assets

1. Deposits and Investments

a. Deposits (Continued)

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a financial institution failure, the City's deposits may not be returned to it. The City does not have a formal deposit policy for custodial credit risk. As of December 31, 2016 and 2017, the City's deposits were not exposed to custodial credit risk.

b. Investments

The City may invest in the following types of investments as authorized by Minn. Stat. §§ 118A.04 and 118A.05:

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

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

3. Detailed Notes

A. Assets

1. Deposits and Investments

b. Investments (Continued)

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

Interest Rate Risk

Interest rate risk is the risk that changes in the market interest rates will adversely affect the fair value of an investment. The City does not have a formal policy to address this risk.

Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. The City does not have a formal policy to address this risk.

Custodial Credit Risk

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities in the possession of an outside party. The City does not have a formal policy to address this risk.

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

3. Detailed Notes

A. Assets

1. Deposits and Investments

b. Investments (Continued)

Concentration of Credit Risk

The concentration of credit risk is the risk of loss that may be caused by the City's investment in a single issuer. The City does not have a formal policy limiting the amounts that may be invested in any one issuer.

B. Liabilities

1. Overdraft of Cash

The following proprietary funds had an overdraft of cash at December 31, 2016:

Refuse and Recycling Enterprise Fund	\$	4,810
Liquor Enterprise Fund		81,491

The following proprietary funds had an overdraft of cash at December 31, 2017:

Sewer Enterprise Fund	\$	11,444
Refuse and Recycling Enterprise Fund		22,434

2. Transfers

In 2017, the City transferred \$45,656 from the General Fund to the Liquor Fund to eliminate the negative cash balance and to close the Liquor Fund.

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

3. Detailed Notes

B. Liabilities (Continued)

3. Short-Term Debt

In April 2016, Badger Creek Farm, LLC, loaned the City \$12,500, and the City Clerk/Treasurer loaned the City \$3,000 for cash flow purposes. The City repaid both loans in December 2016. Neither loan required interest.

In June 2017, the First State Bank of Swanville loaned the City \$25,000 for a sewer repair project. The City repaid the loan in October 2017. The interest rate was 6.99 percent. Also, in July 2017, Badger Creek Farm, LLC, loaned the City \$19,155 for cash flow purposes. The City repaid this loan in November 2017. This loan did not require interest.

4. Long-Term Debt

Proprietary Funds

Long-term debt at December 31, 2016, is comprised of the following:

	<u>Original Amount Issued</u>	<u>Interest Rate</u>	<u>Final Maturity Date</u>	<u>Balance December 31, 2016</u>
Loans Payable				
First State Bank of Swanville - 16309	\$ 85,000	6.96%	11/01/2016	\$ 48,233
First State Bank of Swanville - 17164	10,000	6.00	07/20/2016	<u>2,075</u>
Total				<u>\$ 50,308</u>

There was no long-term debt at December 31, 2017.

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

3. Detailed Notes

B. Liabilities (Continued)

5. Debt Service Requirements

Proprietary Funds

Debt service requirements at December 31, 2016, were as follows:

Year Ending December 31	Loans	
	Principal	Interest
2017	\$ 50,308	\$ -

There were no debt service requirements at December 31, 2017.

6. Changes in Long-Term Debt

Proprietary Funds

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

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Loans Payable					
First State Bank of Swanville - 16309	\$ 55,519	\$ -	\$ 7,286	\$ 48,233	\$ 48,233
First State Bank of Swanville - 17164	-	10,000	7,925	2,075	2,075
Total	\$ 55,519	\$ 10,000	\$ 15,211	\$ 50,308	\$ 50,308

Long-term liability activity for the year ended December 31, 2017, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Loans Payable					
First State Bank of Swanville - 16309	\$ 48,233	\$ -	\$ 48,233	\$ -	\$ -
First State Bank of Swanville - 17164	2,075	-	2,075	-	-
Total	\$ 50,308	\$ -	\$ 50,308	\$ -	\$ -

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

3. Detailed Notes

B. Liabilities

6. Changes in Long-Term Debt

Proprietary Funds (Continued)

In 2011, the City received a loan of \$85,000 with an interest rate of 6.96 percent to rebuild the municipal liquor store. Payments of \$950 were due monthly for five years.

In April 2016, the City received a loan of \$10,000 with an interest rate of 6.00 percent for cash flow purposes. One lump sum payment was due in July 2016.

4. Pension Plans

A. Defined Benefit Pension Plan - Statewide Public Employees Retirement Association

1. Plan Description

Certain part-time employees of the City of Flensburg are covered by a defined benefit pension plan administered by the Public Employees Retirement Association of Minnesota (PERA). PERA administers the General Employees Retirement Plan, which is a cost-sharing, multiple-employer retirement plan. The plan is established and administered in accordance with Minn. Stat. chs. 353 and 356. PERA's defined benefit pension plan is a tax qualified plan under Section 401(a) of the Internal Revenue Code.

The General Employees Retirement Plan (accounted for in the General Employees Fund) has multiple benefit structures with members belonging to the Coordinated Plan, the Basic Plan, or the Minneapolis Employees Retirement Fund. Coordinated Plan members are covered by Social Security and Basic Plan and Minneapolis Employees Retirement Fund members are not. The Basic Plan was closed to new members in 1967. The Minneapolis Employees Retirement Fund was closed to new members during 1978 and merged into the General Employees Retirement Plan in 2015. All new members must participate in the Coordinated Plan, for which benefits vest after five years of credited service.

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

4. Pension Plans

A. Defined Benefit Pension Plan - Statewide Public Employees Retirement Association
(Continued)

2. Benefits Provided

PERA provides retirement benefits as well as disability benefits to members and benefits to survivors upon death of eligible members. Benefit provisions are established by state statute and can be modified only by the state legislature. Benefit increases are provided to benefit recipients each January. Increases are related to the funding ratio of the plan. Benefit recipients receive a future annual 1.0 percent post-retirement benefit increase. If the funding ratio reaches 90 percent for two consecutive years, the benefit increase will revert to 2.5 percent. If, after reverting to a 2.5 percent benefit increase, the funding ratio declines to less than 80 percent for one year or less than 85 percent for two consecutive years, the benefit increase will decrease to 1.0 percent.

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

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 General Employees Retirement Plan Coordinated and Basic Plan members. Members hired prior to July 1, 1989, receive the higher of a step-rate benefit accrual formula (Method 1) or a level accrual formula (Method 2). Under Method 1, the annuity accrual rate for a Basic Plan member is 2.2 percent of average salary for each of the first ten years of service and 2.7 percent for each remaining year. The annuity accrual rate for a Coordinated Plan member is 1.2 percent of average salary for each of the first ten years of service and 1.7 percent for each remaining year. Under Method 2, the annuity accrual rate is 2.7 percent of average salary for Basic Plan members and 1.7 percent for Coordinated Plan members for each year of service. Only Method 2 is used for members hired after June 30, 1989. Minneapolis Employees Retirement Fund members have an annuity accrual rate of 2.0 percent of average salary for each of the first ten years of service and 2.5 percent for each remaining year.

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

4. Pension Plans

A. Defined Benefit Pension Plan - Statewide Public Employees Retirement Association

2. Benefits Provided (Continued)

For General Employees Retirement Plan 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. Disability benefits are available for vested members and are based on years of service and average high-five salary.

3. Contributions

Pension benefits are funded from member and employer contributions and income from the investment of fund assets. Rates for employer and employee contributions are set by Minn. Stat. ch. 353. These statutes are established and amended by the state legislature. General Employees Retirement Plan Basic members, Coordinated members, and Minneapolis Employees Retirement Fund members were required to contribute 9.10 percent, 6.50 percent, and 9.75 percent, respectively, of their annual covered salary in 2016 and 2017.

The City was required to contribute the following percentages of annual covered payroll in 2016 and 2017:

	2016	2017
General Employees Retirement Plan		
Basic Plan members	11.78%	11.78%
Coordinated Plan members	7.50	7.50
Minneapolis Employees Retirement Fund members	9.75	9.75

The employee and employer contribution rates did not change from 2015.

The City's contributions for the years ending December 31, 2015, 2016, and 2017, for the General Employees Retirement Plan were:

	2015	2016	2017
General Employees Retirement Plan	\$ 5,467	\$ 5,283	\$ 2,423

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

4. Pension Plans

A. Defined Benefit Pension Plan - Statewide Public Employees Retirement Association

3. Contributions (Continued)

The contributions are equal to the contractually required contributions as set by state statute.

PERA issues a publicly available financial report that includes financial statements and required supplementary information for the General Employees Retirement Plan. That report may be obtained on the internet at www.mnpera.org; by writing to PERA at 60 Empire Drive, Suite 200, St. Paul, Minnesota 55103-2088; or by calling 651-296-7460 or 1-800-652-9026.

B. Defined Benefit Pension Plan - Fire Relief Association

1. Plan Description

The Flensburg Fire Relief Retirement Plan (Plan) is a single-employer defined benefit pension plan administered by the Flensburg Fire Relief Association. The Plan provides retirement, disability, and death benefits to Plan members and beneficiaries. The Flensburg Fire Relief Association has 17 active members who are covered by the Plan. The Plan currently pays \$350 a year for each year of service provided by each firefighter. Members are eligible for a lump-sum retirement benefit at 50 years of age. Plan provisions include a pro-rated vesting schedule. The Flensburg Fire Relief Association issues a publicly available financial report that may be obtained by contacting the City.

2. Contributions

The Plan is funded in part by state aid and, if necessary, municipal contributions as specified in Minnesota statutes, and voluntary City contributions. The State of Minnesota distributed to the City, and the City passed through to the Plan, \$10,498 and \$10,316 in fire state aid for the years ending December 31, 2016 and 2017, respectively. The State of Minnesota also contributed to the City, and the City passed through to the plan, \$2,547 and \$2,496 in Police and Firefighter Retirement Supplemental State Aid for the years ending December 31, 2016 and 2017, respectively. Required employer contributions are calculated annually based on statutory provisions. The City was not required to make a municipal contribution to the Plan for the years ended December 31, 2015, 2016, and 2017.

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

4. Pension Plans

B. Defined Benefit Pension Plan - Fire Relief Association

2. Contributions (Continued)

Below is a schedule of distributions for the years ending December 31, 2015, 2016, and 2017:

	<u>2015</u>	<u>2016</u>	<u>2017</u>
State of Minnesota Fire Aid	\$ 10,518	\$ 10,498	\$ 10,316
State of Minnesota Police and Firefighter Retirement Supplemental State Aid	2,542	2,547	2,496
Statutorily required contributions	-	-	-

The annual required contributions for 2016 and 2017 were determined by forms provided and required by the Office of the State Auditor. The actuarial assumptions included a five percent investment rate of return.

5. Risk Management

The City is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; injuries to employees; and natural disasters. To manage these risks, the City purchases commercial insurance.

The City purchased various insurance coverages (property, crime, and workers compensation) through the League of Minnesota Cities Insurance Trust (LMCIT), a public entity risk pool currently operating as a common risk management and insurance program for Minnesota cities. The City pays an annual premium to the LMCIT for its insurance coverage. The LMCIT is self-sustaining through member premiums and will reinsure through commercial companies for claims in excess of reserved amounts for each insured event. The LMCIT allows the pool to make additional assessments to make the pool self-sustaining. Current state statutes provide limits of liability for certain kinds of claims.

The City purchased commercial insurance for certain risks of loss for its municipal liquor store.

The amount of settlements did not exceed insurance coverage for the past three fiscal years. There were no significant reductions in insurance from the prior year.

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

6. Special Item

At the September 13, 2017, City Council meeting, the Council voted to sell its municipal liquor store to Herbie's Bar Property, LLC. The final day of business was September 20, 2017, and the closing date of the sale was September 22, 2017. The sale price was \$215,000 (per settlement statement). Reductions for fees, commissions, the pay-off of tax liens, and establishing an escrow account for the hot water heater resulted in a special item of \$131,444. In addition, a transfer of \$45,656 from the General Fund to the Liquor Fund was needed to close the Liquor Fund. The proceeds were used to pay-off both bank loans, the loan from Badger Creek Farm, LLC, and past-due accounts to vendors.

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2016 SUPPLEMENTARY INFORMATION

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**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT A-1

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

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
Receipts				
Property taxes	\$ 44,000	\$ 44,000	\$ 31,987	\$ (12,013)
Licenses, permits, and fees	600	600	74	(526)
Intergovernmental	60,000	60,000	34,196	(25,804)
Charges for services	-	-	1,735	1,735
Contributions	-	-	2,500	2,500
Miscellaneous	3,500	3,500	3,422	(78)
Total Receipts	\$ 108,100	\$ 108,100	\$ 73,914	\$ (34,186)
Disbursements				
Current				
General government				
City Clerk			\$ 11,978	
Council			1,345	
Mayor			554	
Other general government			38,143	
Total general government	\$ 54,000	\$ 54,000	\$ 52,020	\$ 1,980
Public works				
Street maintenance and storm sewers	6,000	6,000	11,269	(5,269)
Debt service				
Principal	11,400	11,400	15,500	(4,100)
Total Disbursements	\$ 71,400	\$ 71,400	\$ 78,789	\$ (7,389)
Receipts Over (Under) Disbursements	\$ 36,700	\$ 36,700	\$ (4,875)	\$ (41,575)
Other Financing Sources (Uses)				
Loans issued	-	-	15,500	15,500
Net Change in Cash Fund Balance	\$ 36,700	\$ 36,700	\$ 10,625	\$ (26,075)
Cash Fund Balance, January 1	58,950	58,950	58,950	-
Cash Fund Balance, December 31	\$ 95,650	\$ 95,650	\$ 69,575	\$ (26,075)

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT A-2

**BUDGETARY COMPARISON SCHEDULE - FIRE SPECIAL REVENUE FUND
REGULATORY BASIS
FOR THE YEAR ENDED DECEMBER 31, 2016**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
Receipts				
Property taxes	\$ 13,000	\$ 13,000	\$ 7,699	\$ (5,301)
Intergovernmental	-	-	22,194	22,194
Contributions	-	-	4,700	4,700
Total Receipts	<u>\$ 13,000</u>	<u>\$ 13,000</u>	<u>\$ 34,593</u>	<u>\$ 21,593</u>
Disbursements				
Current				
Public safety				
Fire	\$ -	\$ -	\$ 25,720	\$ (25,720)
Capital outlay	-	-	17,400	(17,400)
Total Disbursements	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 43,120</u>	<u>\$ (43,120)</u>
Receipts Over (Under) Disbursements	<u>\$ 13,000</u>	<u>\$ 13,000</u>	<u>\$ (8,527)</u>	<u>\$ (21,527)</u>
Other Financing Sources (Uses)				
Loans issued	-	-	3,000	3,000
Net Change in Cash Fund Balance	<u>\$ 13,000</u>	<u>\$ 13,000</u>	<u>\$ (5,527)</u>	<u>\$ (18,527)</u>
Cash Fund Balance, January 1	<u>15,350</u>	<u>15,350</u>	<u>15,350</u>	<u>-</u>
Cash Fund Balance, December 31	<u><u>\$ 28,350</u></u>	<u><u>\$ 28,350</u></u>	<u><u>\$ 9,823</u></u>	<u><u>\$ (18,527)</u></u>

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT A-3

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

	<u>General Fund</u>	<u>Fire Fund</u>	<u>Total Governmental Funds</u>
Appropriations			
Market value credit	\$ 5,667	\$ -	\$ 5,667
PERA rate reimbursement	237	-	237
Local government aid	28,272	-	28,272
Fire state aid	-	10,498	10,498
Volunteer retention stipend aid	-	8,500	8,500
Police/fire supplemental state aid	-	2,547	2,547
Total appropriations	\$ 34,176	\$ 21,545	\$ 55,721
Grants			
State			
Minnesota Department of Public Safety	\$ -	\$ 649	\$ 649
Minnesota Trial Courts	20	-	20
Total grants	\$ 20	\$ 649	\$ 669
Total Intergovernmental Receipts	\$ 34,196	\$ 22,194	\$ 56,390

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2017 SUPPLEMENTARY INFORMATION

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**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT A-4

**BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
REGULATORY BASIS
FOR THE YEAR ENDED DECEMBER 31, 2017**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
Receipts				
Property taxes	\$ 64,000	\$ 64,000	\$ 51,528	\$ (12,472)
Licenses, permits, and fees	600	600	1,950	1,350
Intergovernmental	29,500	29,500	5,113	(24,387)
Charges for services	23,000	23,000	2,399	(20,601)
Miscellaneous	4,700	4,700	2,823	(1,877)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total Receipts	\$ 121,800	\$ 121,800	\$ 63,813	\$ (57,987)
Disbursements				
Current				
General government				
City Clerk			\$ 9,055	
Council			2,057	
Mayor			647	
Other general government			30,051	
			<u> </u>	
Total general government	\$ 52,500	\$ 52,500	\$ 41,810	\$ 10,690
Public works				
Street maintenance and storm sewers	15,000	15,000	14,606	394
Debt service				
Principal	11,130	11,130	19,155	(8,025)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total Disbursements	\$ 78,630	\$ 78,630	\$ 75,571	\$ 3,059
Receipts Over (Under) Disbursements	\$ 43,170	\$ 43,170	\$ (11,758)	\$ (54,928)
Other Financing Sources (Uses)				
Loans issued	\$ -	\$ -	\$ 19,155	\$ 19,155
Transfers out	-	-	(45,656)	(45,656)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total Other Financing Sources (Uses)	\$ -	\$ -	\$ (26,501)	\$ (26,501)
Net Change in Cash Fund Balance	\$ 43,170	\$ 43,170	\$ (38,259)	\$ (81,429)
Cash Fund Balance, January 1	69,575	69,575	69,575	-
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Cash Fund Balance, December 31	\$ 112,745	\$ 112,745	\$ 31,316	\$ (81,429)

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT A-5

**BUDGETARY COMPARISON SCHEDULE - FIRE SPECIAL REVENUE FUND
REGULATORY BASIS
FOR THE YEAR ENDED DECEMBER 31, 2017**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	Variance with Final Budget Positive (Negative)
	<u>Original</u>	<u>Final</u>		
Receipts				
Property taxes	\$ 13,000	\$ 13,000	\$ 12,403	\$ (597)
Intergovernmental	-	-	23,312	23,312
Contributions	-	-	4,000	4,000
Miscellaneous	-	-	434	434
Total Receipts	\$ 13,000	\$ 13,000	\$ 40,149	\$ 27,149
Disbursements				
Current				
Public safety				
Fire	-	-	28,959	(28,959)
Receipts Over (Under) Disbursements	\$ 13,000	\$ 13,000	\$ 11,190	\$ (1,810)
Other Financing Sources (Uses)				
Proceeds from the sale of capital assets	-	-	2,500	2,500
Net Change in Cash Fund Balance	\$ 13,000	\$ 13,000	\$ 13,690	\$ 690
Cash Fund Balance, January 1	9,823	9,823	9,823	-
Cash Fund Balance, December 31	\$ 22,823	\$ 22,823	\$ 23,513	\$ 690

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT A-6

**SCHEDULE OF INTERGOVERNMENTAL RECEIPTS
FOR THE YEAR ENDED DECEMBER 31, 2017**

	General Fund	Fire Fund	Total Governmental Funds
Appropriations			
Market value credit	\$ 4,876	\$ -	\$ 4,876
PERA rate reimbursement	237	-	237
Fire state aid	-	10,316	10,316
Volunteer retention stipend aid	-	9,000	9,000
Police/fire supplemental state aid	-	2,496	2,496
	\$ 5,113	\$ 21,812	\$ 26,925
Grants			
State			
Minnesota Department of Natural Resources	-	1,500	1,500
	\$ 5,113	\$ 23,312	\$ 28,425
Total Intergovernmental Receipts	\$ 5,113	\$ 23,312	\$ 28,425

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**Other Information
Section**

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**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT B-1

**SCHEDULE OF ACCOUNTS RECEIVABLE - 2016
AS OF DECEMBER 31, 2016**

<u>Fund</u>	<u>Source of Revenue and Purpose</u>	<u>Amount</u>
None		\$ -
	Total Accounts Receivable	\$ -

(Unaudited)

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT B-2

**SCHEDULE OF ACCOUNTS PAYABLE - 2016
AS OF DECEMBER 31, 2016**

<u>Fund</u>	<u>Vendor Name</u>	<u>Item and Purpose</u>	<u>Check/Wire Number</u>	<u>Amount</u>
Liquor	Minnesota Department of Revenue	December Sales Tax	12113607	\$ 2,411
Liquor	Central Payment Services	Credit Card Fees	12113611	138
Liquor	Minnesota Department of Revenue	Payroll Taxes	12113617	560
Liquor	Henry's Foods, Inc.	Food/Beverages	7837	55
Liquor	Viking Beverage	Food/Beverages	7838	1,101
Liquor	C&L Distributing, Inc.	Food/Beverages	7854	1,025
Liquor	Ameripride	Laundry/Cleaning	7857, 7947	1,005
Liquor	C&L Distributing, Inc.	Food/Beverages	7872	352
Liquor	Phillips Wine and Spirits	Food/Beverages	7875	539
Refuse and Recycling	Long Prairie Sanitation	Trash Hauling	7876	3,000
General	Loven's Auto Center	Maintenance/Repair	7891, 7944	1,397
Liquor	Federated Co-op	Heating	7905, 7946	1,296
General	Tony's Truck & Equipment Repair	Maintenance/Repair	7922	706
Refuse and Recycling	Long Prairie Sanitation	Trash Hauling	7989, 8157	3,730
Sewer	DHIA Laboratories	Testing	8009, 8196	483
General	Kulus Feeds	Fuel for Lawnmower	8059	53
General	League of Minnesota Cities	Dues	8132	396
Liquor	Old Dutch Foods, Inc.	Food/Beverages	8323	85
Liquor	Bernick's	Food/Beverages	N/A	748
Liquor	St. Cloud Refrigeration	Maintenance/Repair	N/A	355
	Total Accounts Payable			\$ 19,435

(Unaudited)

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT B-3

**SCHEDULE OF INDEBTEDNESS - 2016
FOR THE YEAR ENDED DECEMBER 31, 2016**

<u>Type</u>	<u>Issue Date</u>	<u>Interest Rate (%)</u>	<u>Maturity Date</u>	<u>Initial Authorized Issue</u>	<u>Outstanding Balance January 1, 2016</u>	<u>Issued</u>	<u>Paid</u>	<u>Outstanding Balance December 31, 2016</u>	<u>Principal Due in 2017</u>
First State Bank of Swanville - 16309	01/01/2012	6.96	12/31/2017	\$ 85,000	\$ 55,519	\$ -	\$ 7,286	\$ 48,233	\$ 48,233
First State Bank of Swanville - 17164	04/20/2016	6.00	07/20/2016	10,000	-	10,000	7,925	2,075	2,075
Totals				<u>\$ 95,000</u>	<u>\$ 55,519</u>	<u>\$ 10,000</u>	<u>\$ 15,211</u>	<u>\$ 50,308</u>	<u>\$ 50,308</u>

(Unaudited)

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT B-4

**SCHEDULE OF ACCOUNTS RECEIVABLE - 2017
AS OF DECEMBER 31, 2017**

<u>Fund</u>	<u>Source of Revenue and Purpose</u>	<u>Amount</u>
None		\$ -
	Total Accounts Receivable	\$ -

(Unaudited)

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT B-5

**SCHEDULE OF ACCOUNTS PAYABLE - 2017
AS OF DECEMBER 31, 2017**

<u>Fund</u>	<u>Vendor Name</u>	<u>Item and Purpose</u>	<u>Check/Wire Number</u>	<u>Amount</u>
Liquor	Minnesota Department of Revenue	4th Quarter Withholding	12113674	\$ 305
Liquor	Minnesota Department of Revenue	Sales Tax	12113675	100
General	Internal Revenue Service	4th Quarter Withholding	12113679	1,377
General	Minnesota Department of Revenue	4th Quarter Withholding	12113680	97
General	Loven's Auto Center	Fuel	8360	756
General	Margurite Cofell	Building Cleaning	8361	175
General	Margurite Cofell	Supplies	8361	50
Liquor	Marshik Insurance	Liquor Liability Insurance	8365	4,323
Liquor	Bob & Fran's Grocery	Food/Beverage	8366	23
Refuse and Recycling	Long Prairie Sanitation	December Services	8367	3,580
	Total Accounts Payable			\$ 10,786

(Unaudited)

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

EXHIBIT B-6

**SCHEDULE OF INDEBTEDNESS - 2017
FOR THE YEAR ENDED DECEMBER 31, 2017**

<u>Type</u>	<u>Issue Date</u>	<u>Interest Rate (%)</u>	<u>Maturity Date</u>	<u>Initial Authorized Issue</u>	<u>Outstanding Balance January 1, 2017</u>	<u>Issued</u>	<u>Paid</u>	<u>Outstanding Balance December 31, 2017</u>	<u>Principal Due in 2018</u>
First State Bank of Swanville - 16309	01/01/2012	6.96	12/31/2017	\$ 85,000	\$ 48,233	\$ -	\$ 48,233	\$ -	\$ -
First State Bank of Swanville - 17164	04/20/2016	6.00	07/20/2016	10,000	2,075	-	2,075	-	-
Totals				<u>\$ 95,000</u>	<u>\$ 50,308</u>	<u>\$ -</u>	<u>\$ 50,308</u>	<u>\$ -</u>	<u>\$ -</u>

(Unaudited)

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REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA

OFFICE OF THE STATE AUDITOR

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COMMUNICATION OF SIGNIFICANT DEFICIENCIES AND/OR MATERIAL WEAKNESSES IN INTERNAL CONTROL OVER FINANCIAL REPORTING AND OTHER MATTERS

The Honorable Mayor
and Members of the City Council
City of Flensburg
Flensburg, Minnesota

We have audited, in accordance with auditing standards generally accepted in the United States of America, the financial statements of each major fund of the City of Flensburg, Minnesota, as of and for the years ended December 31, 2016 and 2017, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated October 23, 2018. We expressed an adverse opinion on U.S. generally accepted accounting principles because the financial statements of the City of Flensburg are prepared by the City on the basis of financial reporting provisions of accounting practices prescribed or permitted by the Office of the State Auditor, which is a basis of accounting other than accounting principles generally accepted in the United States of America, to meet the requirements of the Office of the State Auditor. However, our opinion was unmodified on the financial statements prepared under this regulatory basis.

Internal Control Over Financial Reporting

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

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant

deficiencies may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the City's financial statements will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies listed in the Schedule of Findings and Recommendations as items 2015-003, 2017-001, 2017-003, and 2017-004 to be material weaknesses.

A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies in the City's internal control, identified as items 2015-001, 2015-002, 2015-004 through 2015-006, 2017-002, 2017-005, and 2017-006 in the Schedule of Findings and Recommendations, to be significant deficiencies.

Other Matters

Also included in the Schedule of Findings and Recommendations are management practices comments. We believe these recommendations to be of benefit to the City of Flensburg, and they are reported for that purpose.

The City of Flensburg's written responses to the internal control and management practices findings identified in our audit have been included in the Schedule of Findings and Recommendations. We did not audit the City's responses and, accordingly, we express no opinion on them.

This communication is intended solely for the information and use of the Mayor and members of the City Council, management, and others within the City, and is not intended to be, and should not be, used by anyone other than those specified parties.

/s/Rebecca Otto

REBECCA OTTO
STATE AUDITOR

October 23, 2018

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR



REBECCA OTTO
STATE AUDITOR

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INDEPENDENT AUDITOR'S REPORT ON MINNESOTA LEGAL COMPLIANCE

The Honorable Mayor
and Members of the City Council
City of Flensburg
Flensburg, Minnesota

We have audited, in accordance with auditing standards generally accepted in the United States of America, the accompanying financial statements of each major fund of the City of Flensburg, Minnesota, as of and for the years ended December 31, 2016 and 2017, and the related notes to the financial statements, which collectively comprise the City's basic financial statements and have issued our report thereon dated October 23, 2018.

The *Minnesota Legal Compliance Audit Guide for Cities*, promulgated by the State Auditor pursuant to Minn. Stat. § 6.65, contains seven categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, miscellaneous provisions, and tax increment financing. Our audit considered all of the listed categories, except that we did not test for compliance with the provisions for public indebtedness and tax increment financing because the City of Flensburg did not issue or have outstanding any permissible public indebtedness and does not administer any tax increment financing districts.

In connection with our audit, nothing came to our attention that caused us to believe that the City of Flensburg failed to comply with the provisions of the *Minnesota Legal Compliance Audit Guide for Cities*, except as described in the Schedule of Findings and Recommendations as items 2015-007 through 2015-009. 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.

The City of Flensburg's written responses to the legal compliance findings identified in our audit have been included in the Schedule of Findings and Recommendations. We did not audit the City's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Mayor and members of the City Council and management of the City of Flensburg and the State Auditor, and is not intended to be, and should not be, used by anyone other than those specified parties.

/s/Rebecca Otto

REBECCA OTTO
STATE AUDITOR

October 23, 2018

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

**CITY OF FLENSBURG
FLENSBURG, MINNESOTA**

SCHEDULE OF FINDINGS AND RECOMMENDATIONS
FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2017

I. INTERNAL CONTROL OVER FINANCIAL REPORTING

PREVIOUSLY REPORTED ITEMS NOT RESOLVED

Finding Number 2015-001

Vendor Invoice Retention

Criteria: Management is responsible for establishing and implementing internal controls over the accounting cycles and the system used for financial reporting. Invoices should be maintained to support the disbursements made by the City.

Minnesota Statutes § 15.17 requires all public officers in Minnesota to create and maintain all records “necessary to a full and accurate knowledge of their official activities.” Public records can only be destroyed pursuant to Minn. Stat. § 138.17, which requires permission from the Minnesota Records Disposition Panel (Panel), which would include destruction through a record retention schedule approved by the Panel. The General Record Retention Schedule for Cities approved by the Panel requires that invoices be retained for six years.

Condition: Payments to six vendors were reviewed to determine if supporting documentation had been maintained. Of the payments made to the six vendors, payments to four vendors did not have supporting invoices. Instances were noted where vendor invoices were not attached to the check voucher to support disbursements.

Context: For the four vendors, invoices from August to December 2016 and May to September 2017 for Henry’s Foods were unavailable; invoices from September to November 2017 for Bernick’s were unavailable; the one payment made in 2017 to Heggie’s Pizza did not have an invoice; and invoices for January, August, and September 2016 for D&D Beer were unavailable.

Effect: Documentation showing the disbursement is a valid claim has not been obtained or maintained. This does not allow for proper review and approval by the City Council.

Violations of Minn. Stat. §§ 15.17 and 138.17.

Cause: The City discontinued the practice of filing invoices with claim documentation. Oftentimes, the City was making payment based on vendor statements with past due balances, which would not have been supported by a current invoice.

Recommendation: We recommend invoices be attached to the claim form and properly cancelled when paid. Further, we recommend the City only destroy public records as permitted by law.

Client's Response:

The City will attach invoices to all claim forms and have them attached to the checks for review when checks are presented for signatures.

Finding Number 2015-002

Vendor Payments by Employees

Criteria: Minnesota Statutes § 471.38 requires that persons seeking payment from the City submit an itemized bill to the City for audit and approval by the City Council.

Condition: Several instances were noted where City employees paid liquor store vendors with personal checks. The employees were subsequently reimbursed by the City.

Context: Payments of \$1,615 to Henry's Foods, \$2,695 to C&L Distributing, Inc., \$586 to Viking Coca-Cola, and \$408 to Heggie's Pizza were made by City employees.

Effect: When a vendor receives a personal check from employees, the claim process set forth in statute is violated and, as a further result, claimants do not sign a declaration that the claim was true and correct and that no part of it had been paid as required by Minn. Stat. § 412.271.

Cause: The City was having cash flow issues. Oftentimes, there was a necessity to pay vendors with personal checks upon receipt of goods because the City had been delinquent on its accounts. The City did not always have funds available, so at times, payment was made directly by employees.

Recommendation: All claims must be processed as required by Minn. Stat. §§ 471.38 and 412.271. All payments to vendors must be made directly by the City.

Client's Response:

The City will use the City checking account for payment of all vendors.

Finding Number 2015-003

Bank Reconciliations

Criteria: Management is responsible for establishing and implementing internal controls over the accounting cycles and the system used for financial reporting. Performing complete and timely bank reconciliations is a control designed to detect errors and irregularities in a timely manner.

Condition: The City has one checking account. The City does not complete bank reconciliations. Errors and unrecorded transactions were noted, totaling approximately \$14,000 for 2016 and approximately \$29,000 for 2017.

Context: The City maintains its general ledger in CTAS (Small City and Town Accounting System). The 2016 beginning cash in CTAS agreed with the audited 2015 ending cash.

Effect: Failure to monitor cash activity monthly increases the risk that fraud or errors will go undetected and that financial reporting will not be accurate.

Cause: The City had communicated that there were issues reconciling its beginning cash, and the required reports from its general ledger could not be printed as of the bank statement date.

Recommendation: We recommend bank reconciliations be completed on a monthly basis (within two weeks after receipt of the bank statement is reasonable) and reviewed by a supervisor or someone independent of the preparer. Bank reconciliations should be signed by both the preparer and reviewer. The Cash Control Statement, Outstanding Checks, and Deposits in Transit reports from CTAS should support the bank reconciliation and be printed monthly and retained.

Client's Response:

The City will appoint a Council member to review the statement and sign-off on the reconciliation of the City checking account. The checking account will be balanced monthly before the regular monthly council meeting.

Finding Number 2015-004

Check Sequencing

Criteria: Management is responsible for establishing and implementing internal controls over the accounting cycles and the system used for financial reporting. Controls over check sequencing provide assurance that no unauthorized payments are made, all amounts due are paid timely, and payments are accurately recorded.

Condition: Over 50 instances were noted between the beginning of 2016 and the end of 2017 where incorrect check numbers were entered into CTAS.

Context: Duplication of check numbers was not noted during the 2016 and 2017 audit. Duplication of check numbers had been noted in prior audits.

Effect: Failure to implement controls over check sequencing increases the risk that fraud or errors will go undetected and that financial reporting will not be accurate.

Cause: Errors or issues in printing checks occurred without staff going back and correcting the check numbers in CTAS.

Recommendation: We recommend maintaining strict numerical control over all checks issued and issuing checks in sequence as much as possible.

Client's Response:

The City Clerk/Treasurer will go back and correct any errors to the check numbers that occur to make sure that all checks printed have the correct number listed.

Finding Number 2015-005

Financial Statement Preparation

Criteria: Management is responsible for the preparation and fair presentation of the financial statements, the related notes, and all accompanying information.

Condition: As is the case with many small entities, the City has relied on its independent external auditors to assist in the preparation of the financial statements, including notes to the financial statements, as part of its external financial reporting process.

Context: The City's ability to prepare financial statements is based, at least in part, on its reliance on its external auditors, who cannot by definition be considered part of the City's internal control.

Effect: The City lacks internal control over the preparation of financial statements.

Cause: It was determined by the City that it is more cost effective to have its auditors prepare its financial statements rather than to incur the time and expense of obtaining the necessary training and expertise required to prepare the financial statements internally.

Recommendation: We recommend the City obtain the training and expertise to internally prepare its annual financial statements. If the City still intends to have external audit staff assist in preparation then, at a minimum, it must have an individual identified and trained with the expertise to sufficiently review, understand, and approve the City's financial statements, including the related notes.

Client's Response:

The City Council will look into having the Clerk/Treasurer get the training needed to be in charge of preparing and understanding the financial statements. We are confident that without the Liquor Store the City's financial statements can be prepared accurately without the expense of hiring an external auditor to do them.

Finding Number 2015-006

Fund Balance

Criteria: Governments are required to report amounts in the appropriate fund balance classifications, in accordance with Governmental Accounting Standards Board (GASB) Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* (GASB Statement 54), by applying their accounting policies to determine whether restricted, committed, assigned, or unassigned resources are considered to have been spent.

Condition: The City has not developed and approved a formal fund balance policy.

Context: The City had been provided with a sample policy by its auditors.

Effect: Without a formal fund balance policy, fund balance practices may not be followed as intended by management.

Cause: The City had not determined a need to develop and adopt a formal fund balance policy.

Recommendation: We recommend the City adopt a formal fund balance policy that would address the following: minimum fund balance policy, order of resource use, stabilization arrangements, committed fund balance, and assigning fund balance. Additional guidance on GASB Statement 54 can be found on the Office of the State Auditor's website at:

https://www.auditor.state.mn.us/other/Statements/fundbalances_postGASB54_1012_statement.pdf

Client's Response:

A Fund Balance Policy will be written for the City. The City will refer to the GASB Statement 54 for guidance in writing the policy along with reviewing similar-size cities' policies for reference in developing the policy. The City will set February 2019 as a completion date for the policy.

ITEMS ARISING THIS YEAR

Finding Number 2017-001

Segregation of Duties

Criteria: Management is responsible for establishing and maintaining internal control. Adequate segregation of duties is a key internal control in preventing and detecting errors or irregularities. To protect City assets, proper segregation of the record-keeping, custody, and authorization functions should be in place; and, where management decides segregation of duties may not be cost effective, compensating controls should be in place.

Under Minn. Stat. § 412.201, the mayor should execute written instruments, such as contracts, conveyances and licenses on behalf of the City.

In addition, under Minn. Stat. § 412.121, the City Council must choose an acting mayor from the council members at the first meeting each year. The acting mayor, not the clerk/treasurer, is to perform the duties of the mayor “during the disability or absence of the mayor from the city.”

Condition: The City Clerk/Treasurer has custody of assets, prepares the bank deposits, reconciles the City checkbook, prepares checks for payment, processes payroll and maintains electronic employee data, and has sole access to the financial records. The City Clerk/Treasurer also acts as backup to the Mayor in signing legal documents on behalf of the City. In addition, the City does not perform risk assessment or monitoring procedures.

Context: Due to the limited number of staff at the City, segregation of the accounting functions necessary to ensure adequate internal accounting control is not possible. This is not unusual in operations the size of the City of Flensburg; however, the City's management should constantly be aware of this condition and realize that the concentration of duties and responsibilities in a limited number of individuals is not desirable from an accounting point of view. This concern had been brought to the City's attention in prior audits as well. The City Clerk/Treasurer does provide a monthly income and expenses report that is reviewed and accepted at City Council meetings.

Effect: Noncompliance with Minn. Stat. §§ 412.121 and 412.201. In addition, inadequate segregation of duties could adversely affect the City’s ability to detect misstatements in amounts that would be material in relation to the financial statements in a timely period by employees in the normal course of performing their assigned functions.

Cause: The City informed us that it does not have the economic resources needed to hire additional qualified accounting staff in order to segregate duties.

Recommendation: We recommend the City Council be aware of the lack of segregation of the accounting functions and, where possible, implement oversight procedures by identifying areas with control weaknesses and implementing oversight/monitoring procedures. These procedures could include performing a review over checkbook reconciliations, preparing the deposit, reviewing a list of vendors the City makes payments to for appropriateness, and reviewing pay rates in CTAS.

The Mayor should execute written instruments on behalf of the City in conformance with Minn. Stat. § 412.201.

The City Council should appoint a Council member as the “acting mayor” at its first meeting annually, pursuant to Minn. Stat. § 412.121. The acting Mayor should execute written instruments as necessary during the disability or absence of the Mayor from the City.

Client’s Response:

The City will address the problem of segregation of duties and develop a plan to address the control weaknesses addressed in the findings. The Council will appoint Council members to review the areas addressed in the findings. Effective immediately, Council members will not sign any checks made payable to them and appoint a Council member to be the backup to the Mayor in signing legal documents on behalf of the City.

Finding Number 2017-002

Formal Policies and Procedures

Criteria: Management is responsible for establishing and implementing internal controls over the accounting cycles and the system used for financial reporting. Written policies and procedures should exist to ensure the City’s practices are followed as intended by management.

Condition: The City does not have formally adopted policies and procedures documenting accounting controls.

Context: The City has adopted a Mileage Reimbursement Policy, an Out of State Travel Policy, and a Wire Transfer Payments Policy.

Effect: Without formal policies and procedures, practices may not be followed as intended by management, and there is an increased risk of fraud.

Cause: The City had not determined a need to develop and adopt formal policies and procedures.

Recommendation: We recommend the City develop formal policies and procedures documenting at a minimum accounting controls over cash, receipts, disbursements, and payroll.

Client's Response:

The City will develop formal policies and procedures in regards to accounting controls over cash, receipts, disbursements and payroll. Again, the Clerk/Treasurer will review the policies of "like cities" in developing this policy.

Finding Number 2017-003

Material Audit Adjustments

Criteria: A deficiency in internal control over financial reporting 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 of the financial statements on a timely basis. Auditing standards define a material weakness as a deficiency, or 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.

Condition: Material audit adjustments were identified that resulted in significant changes to the City's financial statements.

Context: The inability to detect material misstatements in the financial statements increases the likelihood that the financial statements would not be fairly presented. The adjustments were found in the audit; however, independent external auditors cannot be considered part of the City's internal control.

Effect: The following material audit adjustments were reviewed and approved by management and are reflected in the financial statements:

2016

General Fund:

- Increased property tax receipts and cash by \$2,301 to correct the property tax allocation between the General Fund and the Fire Fund.
- Decreased cash and miscellaneous receipts by \$4,549 to record receipts for pull tabs in the Liquor Fund.
- Decreased cash and contributions by \$3,700 to record contributions received for the purchase of the fire truck in the Fire Fund.
- Increased cash and decreased general government and debt service disbursements by \$17,900 to record loan payments for the liquor store in the Liquor Fund.

Fire Fund:

- Decreased property tax receipts and cash by \$2,301 to correct the property tax allocation between the General Fund and the Fire Fund.
- Increased cash and contributions by \$3,700 to record contributions received for the purchase of the fire truck recorded in the General Fund.
- Decreased cash and increased public safety disbursements by \$4,000 to record a reimbursement for a receipt deposited for the fire truck recorded in the Liquor Fund.

Sewer Fund:

- Increased cash and charges for services by \$2,265 to record receipts for sewer charges recorded in the General Fund and Refuse and Recycling Fund.
- Decreased cash and increased personnel services by \$1,000 to correct payroll disbursement classifications between the General Fund and Sewer Fund.

Refuse and Recycling Fund:

- Decreased cash and charges for services by \$1,100 to record receipts for sewer charges in the Sewer Fund.
- Increased cash and charges for services by \$1,771 to record receipts for sanitation charges recorded in the General Fund and Sewer Fund.
- Decreased cash and increased professional services by \$1,500 to adjust an entry made to record a returned check.

2017

General Fund:

- Decreased cash and property tax receipts by \$7,403 to correct the property tax allocation between the General Fund and the Fire Fund.
- Decreased cash and miscellaneous receipts by \$33,356 to record receipts for pull tabs in the Liquor Fund.
- Decreased cash and contributions by \$3,000 to record contributions received for the Fire Department in the Fire Fund.
- Decreased cash and miscellaneous receipts by \$2,500 to record proceeds from the sale of the fire truck in the Fire Fund.
- Decreased cash and miscellaneous receipts by \$25,000 to record the proceeds from the issuance of the loan for sewer repair costs to the Sewer Fund.
- Increased cash and decreased general government disbursements by \$12,051 to correct payroll disbursement classifications between the General Fund, Sewer Fund, and Liquor Fund.
- Increased cash and decreased debt service disbursements by \$127,541 to record loan payments for the liquor store and sewer repairs to the Liquor Fund and Sewer Fund.
- Increased cash and decreased other financing uses by \$15,000 to eliminate a transfer out recorded for the payment of sewer disbursements made by the Sewer Fund.

Fire Fund:

- Increased cash and property tax receipts by \$7,403 to correct the property tax allocation between the General Fund and the Fire Fund.
- Increased cash and contributions by \$3,000 to record contributions received for the Fire Department recorded in the General Fund.
- Increased cash and proceeds from the sale of capital assets by \$2,500 to record proceeds from the sale of the fire truck recorded in the General Fund.

Sewer Fund:

- Increased cash and loans issued by \$25,000 to record the proceeds from the issuance of the loan for sewer repair costs recorded in the General Fund.
- Decreased cash and increased personnel services disbursements by \$2,700 to correct payroll disbursement classifications between the General Fund and Sewer Fund.
- Decreased cash by \$25,712, increased debt principal paid and interest paid by \$26,147, and decreased repairs and maintenance disbursements by \$435 to record loan payments for sewer repairs recorded in the General Fund.
- Decreased cash and other receipts by \$15,000 to eliminate a transfer in from the General Fund recorded for the payment of sewer disbursements made by the Sewer Fund.

Refuse and Recycling Fund:

- Decreased cash and increased other operating disbursements by \$8,239 for the payment of sales tax for sanitation charges recorded in the Liquor Fund.

Liquor Fund:

- Increased cash and miscellaneous receipts by \$33,356 to record receipts for pull tabs recorded in the General Fund.
- Decreased cash and increased other disbursements by \$50,308 to record loan payments for the liquor store recorded in the General Fund.
- Decreased cash and increased disbursements by \$20,949 to record payments to Public Employees Retirement Association of Minnesota (PERA), the IRS, the Minnesota Department of Revenue, and for utility, phone, and cable services not recorded in the general ledger.
- Decreased cash and increased personnel services disbursements by \$9,351 to correct payroll disbursement classifications between the General Fund and Liquor Fund.

Cause: Adjustments were required due to incomplete or improper information being entered into the general ledger (CTAS).

Recommendation: We recommend the City establish internal controls necessary to ensure the City's annual financial statements are free of material misstatements.

Client's Response:

The City Clerk/Treasurer will be more diligent in assuring that the entries made to CTAS are correct by running monthly reports to the different funds for review of accuracy and providing the Council with these reports for review at monthly Council meetings.

Finding Number 2017-004

Liquor Store Receipts

Criteria: Management is responsible for establishing and implementing internal controls over the accounting cycles and the system used for financial reporting.

Condition: Two months of daily reconciliations performed by liquor store staff for both 2016 and 2017 were tested. Out of the 65 reconciliations reviewed for 2016, 11 did not reconcile to the amount deposited by \$20 or more, 7 of which did not reconcile by \$100 or more. Out of the 56 reconciliations reviewed for 2017, 10 did not reconcile to the amount deposited by \$50 or more, 4 of which did not reconcile by \$500 or more. In all but one instance out of the 21 that did not reconcile, actual cash deposited was less than the amount of sales to be deposited based on the liquor store reconciliations. In some instances, the reconciliations did not tie to the deposit due to cash payments made to vendors or for groceries for the sale of food at the liquor store. Cash paid out was not always supported with detailed receipts.

Context: The City sold its liquor store in September 2017.

Effect: Lack of controls over cash receipts puts the City at risk for loss of revenue. When payment is made directly from the cash till, the City is not recording the disbursement, and liquor store sales receipts are understated. Also, cash payments to vendors bypass the City Council's approval process over payments.

Cause: The City was not maintaining documentation of cash payments made directly from the liquor store till.

Recommendation: Even though the City's liquor store has since been sold, the City's practice should be to reconcile receipts to ensure it receives what is expected and records what is actually received. All vendor payments should be made by City check, and reimbursements for costs should be supported with detailed receipts.

Client's Response:

All receipts will be reviewed by the Council member appointed to review the monthly checking statement. A periodic review of garbage and sewer receipts will be done to match the amounts recorded in the garbage and sewer ledgers to the deposited amounts. The vendor payments have been addressed in "Finding Number 2015-001".

Finding Number 2017-005

Employee Reimbursements

Criteria: Management is responsible for establishing and implementing internal controls over the accounting cycles and the system used for financial reporting.

All claims need to be in writing and itemized per Minn. Stat. § 471.38. Without documentation to support a claim, the City cannot “audit” and approve the claim for payment. Further, Minn. Stat. § 15.17 requires that all documentation needed for a “full and accurate knowledge” of official activities be created and maintained.

Condition: All payments made to City employees were reviewed. One of these payments made in July 2016 was for \$1,355 for reimbursement for office supplies, repair and maintenance, postage, and liquor and food for the liquor store. Approximately \$850 of this claim had receipts from prior to 2016, as early as April 2014. Another payment made in June 2016 was a reimbursement for a personal check made to the City in the amount of \$4,000; however, the receipt to the City was only noted to be \$3,000. Another payment was for reimbursement of mileage paid in October 2017. The rate at which mileage was reimbursed (\$0.55) was not in accordance with the City’s Mileage Reimbursement Policy, which stated that the 2017 IRS rate was to be used (\$0.535). Out of 26 payments reviewed for 2016 and 2017, 12 did not have any support; 9 included support, however, it was not detailed. At times, the only support included was a carbon copy of a personal check written.

Context: For the July 2016 payment noted above, the disbursements in CTAS were viewed for the month of, before, and after the date of the receipts provided as support. No previous reimbursements for these payments in those months were noted.

Effect: Failure to require proper support for payment increases the risk of fraudulent activity. The City is in violation of Minn. Stat. §§ 15.17 and 471.38.

Cause: Receipts had not yet been previously submitted for reimbursement. Mileage was believed to have been paid at the correct rate. No procedures have been established on submitting employee requests for reimbursement.

Recommendation: We recommend the City establish a policy and procedures over reimbursements made to employees. The policy and procedures should include a requirement for review and approval by a supervisor, a requirement to provide detailed receipts, and for reimbursements to be requested in a timely manner.

Further, we recommend that pursuant to Minn. Stat. § 471.38 no claims be paid unless they are in writing and itemized. City records must be retained pursuant to state law.

Client's Response:

A policy for Employee Reimbursements will be written and will address the requirements for review and approval by a supervisor, a requirement to provide detailed receipts, and for reimbursements to be requested in a timely manner.

Finding Number 2017-006

Payroll

Criteria: Management is responsible for establishing and maintaining internal control over various accounting cycles, including payroll. In the payroll system, changes to the payroll master file and payroll processing should be segregated. If that is not practical, changes to the payroll master file should be monitored by someone independent of payroll processing at least monthly. In addition, employee and supervisor signatures on time sheets or time forms must be required to attest to the validity of time reported as required by Minn. Stat. § 412.271.

Condition: The processing of payroll and changes to the payroll master file for occurrences such as new hires, terminations, promotions, and pay increases are done by the same person. Timesheets are not completed by staff who were not employed at the liquor store. In addition, six payments were noted that were made at a pay rate where approval by the City Council could not be found.

Context: It is not unusual for organizations the size of the City of Flensburg to allow salaried elected officials to approve their own time.

Effect: When there is limited segregation of duties and monitoring, there is an increased risk that errors or irregularities may occur and not be detected in a timely manner.

Cause: No procedures have been established for submitting and approving time.

Recommendation: Management should be aware that segregation of duties is not adequate from an internal control point of view. Someone independent of the payroll processing function should review the payroll master file periodically to ensure any changes were properly authorized and document this review. Time sheets should be completed and signed by employees and approved and signed by supervisors per Minn. Stat. § 412.271, subd. 2.

Client's Response:

A Council member will be appointed to review the payroll processing in CTAS, including pay rates and hours. This will be addressed in the written policy for Internal Controls that will be developed and approved by the Council. Time sheets have been made and will be used for the recording of hours by hourly paid employees and signed off by a supervisor.

II. OTHER FINDINGS AND RECOMMENDATIONS

A. MINNESOTA LEGAL COMPLIANCE

PREVIOUSLY REPORTED ITEMS NOT RESOLVED

Finding Number 2015-007

Electronic Funds Transfer Policy

Criteria: The City is authorized by Minn. Stat. §§ 471.381 to make payments via electronic funds transfer. The statute requires the City to establish policies and procedures to ensure the validity of any electronic approvals. In addition, Minn. Stat. § 15.17 requires the City to make and preserve records necessary to a full and accurate knowledge of the City’s official activities. The City’s Wire Transfer Payments Policy states that a “Wire Transfer Authorization Form” must be submitted with the voucher in order to execute a wire transfer.

Condition: The City’s Wire Transfer Payments Policy states that “the authorized approver is a designated person with the City of Flensburg”; however, it does not make the delegation. No delegation was noted in the City Council meeting minutes. A single payment was noted that was made via electronic funds transfer. This payment was to the State of Minnesota, and no corresponding “Wire Transfer Authorization Form” was available. It cannot be readily determined from ACH payment information on the bank statements if more electronic funds transfers were made.

Context: The City approved its Wire Transfer Payments Policy on January 11, 2017.

Effect: Noncompliance with Minn. Stat. § 15.17. The “Wire Transfer Authorization Form” provides for signatory approval from the City of Flensburg authorized approver. The City is not following its Wire Transfer Payments Policy.

Cause: “Wire Transfer Authorization Forms” are prepared for the bank to complete the wire and are kept by the bank.

Recommendation: We recommend the City retain copies of the “Wire Transfer Authorization Forms” to document approvals over electronic funds transfers as well as to adhere to its policy.

Client’s Response:

The “Electronic Funds Transfer Policy” will be updated to comply with Minnesota Statutes.

Finding Number 2015-008

Prompt Payment of Invoices

Criteria: As stated in Minn. Stat. § 471.425, the City is required to make payment on vendor invoices according to the terms of the contract, or within 35 days of the completed delivery of the goods or services or the receipt of the invoice, whichever is later. For bills paid after the time period set by contract or standard payment period, the government entity must calculate and pay interest as required.

Condition: Numerous bills that were not paid within 35 days from the date of receipt were noted. For the month of March 2016, one invoice from Tyco Integrated Security, LLC, stated 61-90 days past due; one invoice from Bernick's stated 61 days past due; and one invoice from Central Minnesota Electric, Inc. stated 31-60 days past due. For the month of March 2017, one invoice from Federated Co-ops, Inc., stated over 90 days past due; one invoice from DHIA Laboratories stated over 120 days past due; one invoice from Tony's Truck and Equipment Repair, Inc. stated over 90 days past due; one invoice from the League of Minnesota Cities stated over 61 days past due; one invoice from Kulus Feed Store, Inc. stated 61-90 days past due; and one invoice from St. Cloud Refrigeration stated 91-120 days past due. Interest was not calculated or paid as required.

Context: The City Council holds meetings on a monthly basis.

Effect: Making payment on invoices after 35 days of the completed delivery of the goods or services or receipt of the invoice, whichever is later, is in noncompliance with Minn. Stat. § 471.425 if interest is not calculated and paid.

Cause: The City was not able to pay its bills in a timely manner due to cash flow issues.

Recommendation: We recommend the City make payments on vendor invoices in accordance with Minn. Stat. § 471.425.

Client's Response:

In the future, payments of bills will be made in a timely manner, in accordance with Minn. Stat. 471.425.

Finding Number 2015-009

Unallowed Debt

Criteria: The power of a city to incur indebtedness is governed by Minnesota Statutes.

Condition: The City entered into three commercial loans with First State Bank of Swanville, as well as loans with its employees and Badger Creek Farm, LLC. These types of obligations are not authorized indebtedness.

Context: The City paid off all of these obligations by the end of 2017.

Effect: Noncompliance with Minnesota statutes, primarily Minn. Stat. ch. 475.

Cause: The City was not aware of what debt is authorized. The City had cash flow issues and needed cash quickly.

Recommendation: We recommend any future debt financing entered into by the City only be as authorized under Minnesota Statutes.

Client's Response:

The City will follow the Minnesota statutes in regards to any future financing if it is needing to explore financing options.

B. MANAGEMENT PRACTICES

PREVIOUSLY REPORTED ITEMS NOT RESOLVED

Finding Number 2015-010

Form 941

Criteria: The City is to complete IRS Form 941 on a quarterly basis to determine its tax liability quarterly.

Condition: Not all federal 941 forms had been filed and the related taxes had not been paid on a timely basis. Although the 941 forms for 2015 had been filed, there were still significant federal liens against the City in place for taxes due from 2013, 2014, and 2015. During 2016 and 2017, all Form 941 forms had been noted as filed. Also, all of the City's current and prior tax obligations have been settled.

Context: The IRS levied the City's revenue sources in 2017 for collection of taxes owed.

Effect: The City incurred a significant amount of fees and penalties due to not filing and paying taxes timely.

Cause: The City was not able to pay its bills in a timely manner due to cash flow issues.

Recommendation: We recommend the City continue to file its taxes on a timely basis to ensure that it does not incur fees and penalties in the future.

Client's Response:

The City will continue to file all taxes on a timely basis.

Finding Number 2015-011

W-2 Forms

Criteria: The City is to provide federal W-2 forms to employees and the IRS annually to report taxable wages.

Condition: Payroll taxable wages according to the Employee's Earnings Record CTAS reports did not always reconcile to the W-2 forms. For 2016, 21 of 29 taxable wages in CTAS did not agree with the employees' W-2 forms. For 2017, 14 of 26 taxable wages in CTAS did not agree with the employees' W-2 forms.

Context: Payroll wages in CTAS reconciled to W-2 forms, excluding amounts paid out for the last payroll runs of 2015, 2016, and 2017.

Effect: Taxable wages reported on W-2 forms are not supported by the City's general ledger (CTAS).

Cause: Discrepancies between wages included in the general ledger and included on W-2 forms.

Recommendation: We recommend the City reconcile payroll wages in CTAS to W-2 forms quarterly to ensure accurate reporting.

Client's Response:

The City Clerk/Treasurer will address the issue of the W-2's not matching the payroll records to insure that they are in balance before producing them.

ITEMS ARISING THIS YEAR

Finding Number 2017-007

City Fines

Criteria: City officers are stewards of public funds.

Condition: The City paid over \$3,000 in bank fees in 2016 and over \$1,200 in bank fees in 2017. In addition, the City incurred penalties of approximately \$650 due to the City not paying contributions to PERA. Lastly, the City incurred over \$9,800 in penalties and interest from not paying federal taxes on a timely basis.

Context: City finances were stressed by the municipal liquor store operating at a loss since 2014. The City's sewer line collapsed in 2017, resulting in over \$25,000 in emergency repairs.

Effect: The City made payments that did not serve as a benefit to the taxpayers of the City.

Cause: The City was not able to pay its bills in a timely manner due to cash flow issues, resulting in overdraft and late fee charges and penalties and interest.

Recommendation: We recommend the City pay its bills in a timely manner to avoid overdraft and late fee charges and penalties and interest.

Client's Response:

The City will pay all bills in a timely manner to avoid any late fees, overdrafts and penalties and interest.

Finding Number 2017-008

City Assets/Records

Criteria: Minnesota law establishes a presumption that government data are public and are accessible by the public for both inspection and copying unless there is a federal law, a state statute, or a temporary classification of data that provides that certain data are not public.

Condition: The City does not utilize its City Community building or Fire Hall to conduct City business, and as a result, it has fallen upon the City Clerk/Treasurer to conduct City business from her home. The City Clerk/Treasurer records transactions for the City in CTAS on her personal computer. City records are also partially kept at the Clerk/Treasurer's home. Citizens contact the City Clerk/Treasurer on her personal cell phone or at her home directly for City business.

Context: The City leases its City Community building to the American Legion. City Council meetings are held at this building. The City also owns a Fire Hall.

Effect: City records held at the home of a City employee reduces oversight by the City Council, and limits the availability of records to the public. There is also a risk of City assets and records being comingled with that of the City employee, as well as not being kept secure.

Cause: The City has had financial issues not allowing it to develop a dedicated workspace for the City Clerk/Treasurer. This has also been past practice.

Recommendation: We recommend the City Council consider whether to set part-time business hours at its City Community building or Fire Hall for citizens to come to conduct City business. We also recommend the City consider establishing a dedicated space at the City Community building or Fire Hall for the Clerk/Treasurer to conduct City business, maintain City records, and keep City assets.

Client's Response:

The City will immediately look in options for establishing a dedicated space for the Clerk/Treasurer to conduct City business, maintain City records and keep City assets.