

**CITY OF HERMANTOWN, MINNESOTA**

**ANNUAL FINANCIAL REPORT**  
**FOR THE YEAR ENDED DECEMBER 31, 2015**  
**TOGETHER WITH INDEPENDENT AUDITOR'S REPORT**

CITY OF HERMANTOWN, MINNESOTA  
 TABLE OF CONTENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015

	<u>Page</u>
<u>Introductory Section</u>	
Elected and Appointed Officials .....	1
Independent Auditor's Report .....	2 - 3
<u>Required Supplementary Information</u>	
Management's Discussion and Analysis .....	4 - 9
<u>Basic Financial Statements</u>	
Government-wide Financial Statements	
Statement of Net Position .....	10
Statement of Activities .....	11
Fund Financial Statements - Governmental Funds	
Balance Sheet .....	12
Reconciliation of the Balance Sheet to the Statement of Net Position .....	13
Statement of Revenues, Expenditures, and Changes in Fund Balances .....	14
Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances to the Statement of Activities .....	15
Statement of Revenues, Expenditures, and Changes in Fund Balance - Budget and Actual	
General Fund .....	16
Sales Tax Fund .....	17
Proprietary Funds	
Statement of Net Position .....	18
Statement of Revenues, Expenses, and Changes in Net Position .....	19
Statement of Cash Flows .....	20 - 21
Notes to Financial Statements .....	22 - 56
<u>Required Supplementary Information</u>	
Information about the City's Other Postemployment Health Care Plan .....	57
Information about the District's Net Pension Liability .....	58 - 59
<u>Supplementary Information</u>	
Combining Balance Sheet .....	60 - 62
Combining Statement of Revenues, Expenditures, and Changes in Fund Balances .....	63 - 65

CITY OF HERMANTOWN, MINNESOTA  
TABLE OF CONTENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)

Page

Other Reports

Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters .....	66 - 67
Independent Auditor's Report on Legal Compliance for the State of Minnesota .....	68
Schedule of Findings and Responses .....	69
Schedule of Prior Year Findings and Responses .....	70

## **INTRODUCTORY SECTION**

CITY OF HERMANTOWN, MINNESOTA  
ELECTED AND APPOINTED OFFICIALS  
2015

Term Expires

Mayor – Wayne Boucher

December 31, 2016

Councilors

John Geissler

December 31, 2016

Darlene Koski

December 31, 2016

Gloria Nelson

December 31, 2018

Natalie Peterson

December 31, 2018

Appointed

John Mulder, City Administrator

Kevin Orme, Finance Director

James M. Crace, Police Chief

Dean Sharpe, City Superintendent

Debbie Lund, City Clerk



## Independent Auditor's Report

To the Honorable City Council  
City of Hermantown  
Hermantown, Minnesota

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component unit (Hermantown Airport Commission), each major fund, and the aggregate remaining fund information of the City of Hermantown, Minnesota ("City") as of and for the year ended December 31, 2015, which collectively comprise the City of Hermantown, Minnesota's basic financial statements as listed in the table of contents.

### ***Management's Responsibility for the Financial Statements***

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

### ***Auditor's Responsibility***

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

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

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

### ***Opinions***

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hermantown, as of December 31, 2015, and the respective changes in financial position and, where applicable, cash flows thereof, and the respective budgetary comparison for the General Fund and City Sales Tax Fund for the year then ended, in conformity with accounting principles generally accepted in the United States.

***Emphasis of Matter***

As discussed in Note 1 to the financial statements, the City adopted new accounting guidance, GASB Statement No. 68, *Accounting and Financial Reporting for Pensions* and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date* during 2015. Our opinions are not modified with respect to this matter.

***Other Matters******Required Supplementary Information***

Accounting principles generally accepted in the United States require that the management's discussion and analysis on pages 4 through 9, information about the City's other postemployment health care plan, page 57, and information about the City's net pension liability, pages 58 and 59, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

***Supplementary Information***

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Hermantown's financial statements as a whole. The combining balance sheet and individual fund financial statements and schedules, pages 60 through 65, are presented for purposes of additional analysis and are not a required part of the financial statements. The combining balance sheet and individual fund financial statements and schedules are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

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

In accordance with *Government Auditing Standards*, we have also issued our report dated April 14, 2016 on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's internal control over financial reporting and compliance.



Wipfli LLP

Duluth, Minnesota  
April 14, 2016

**REQUIRED SUPPLEMENTARY INFORMATION**

CITY OF HERMANTOWN, MINNESOTA  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEAR ENDED DECEMBER 31, 2015

Our discussion and analysis of the City of Hermantown's financial performance provides an overview of the City's financial activities for the fiscal year ended December 31, 2015. Please read it in conjunction with the City's financial statements, which begin on page 9.

### **Financial Highlights**

- The City's net position increased \$1,982,940 or 3.75 percent as a result of this year's operations. The net position of the governmental activities increased \$1,690,300, or 14.31 percent. The net position of the business-type activities increased \$292,640, or 0.71 percent.
- The General Fund unassigned fund balance was \$3,280,115 or 74.22 percent of the total General Fund expenditures for 2015.

### **Overview of the Financial Statements**

This discussion and analysis serves as an introduction to the City of Hermantown's basic financial statements, which consists of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. The report also contains other supplementary information in addition to the basic financial statements.

- The first two statements are government-wide financial statements that provide information about the City's overall financial status.
- The remaining statements are fund financial statements that focus on individual parts of the City, reporting the City's operations in more detail than the government-wide statements. The governmental funds statements explain how general government services were financed, as well as, how grant proceeds were utilized for the short-term and what remains for future spending.
- The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of required and other supplementary information that further explains and supports the information in the financial statements.

### **Government-wide Financial Statements**

The government-wide financial statements are designed to give users a broad overview of the City's finances, in a manner similar to that of a private-sector business. The statement of position presents information on all of the City's assets and deferred outflows of resources, and liabilities and deferred inflows of resources, with the difference between the two reported as net position. Increases and decreases in net position over time may serve as a useful indicator of whether the City's financial position is improving or deteriorating. The statement of activities shows how the City's net position changed during the fiscal year. All changes in net position are reported as soon as the underlying event that caused the change occurs, regardless of the timing of the related cash flows. There are revenues and expenses reported in this statement for some items that will only result in cash flows in future fiscal years; examples include uncollected grants and vacation days that are earned, but not used.

CITY OF HERMANTOWN, MINNESOTA  
 MANAGEMENT'S DISCUSSION AND ANALYSIS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

Both government-wide financial statements distinguish between functions that are governmental and business-type activities. The City's governmental activities include public safety, streets and highways, community and economic development, culture and recreation, and general administration. Property taxes and state and federal grants and aids finance most of these activities.

The City charges fees to customers to help cover all or most of the cost of certain services it provided. The City's business-type activities include the Water Utility, Sewage Disposal, and Street Lighting funds.

The two government-wide financial statements are presented immediately after this discussion and analysis.

### **Fund Financial Statements**

A fund is a set of related accounts that is used to control resources that have been segregated to carry on specific activities or to attain certain objectives in accordance with special regulations, restrictions, or limitations. The City of Hermantown, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All City funds are either governmental funds, proprietary, or fiduciary funds.

- Governmental funds - Because the focus of governmental fund financial statements is narrower than government-wide financial statements, it is useful to compare information presented for governmental funds with similar information presented for governmental activities in order to gain a better understanding of the long-term impact of the City's near-term financing decisions. The Governmental Fund Balance Sheet and the Governmental Fund Statement of Revenues, Expenditures and Changes in Fund Balances provide reconciliation to aid in the comparison of governmental funds with governmental activities.

The City maintains a number of individual governmental funds. Information is presented separately in the governmental fund financial statements for the General, City Sales Tax, G.O. Improvement & Utility Revenue Bonds Series 2007B, G.O. Improvement Bonds Series 2009A, G.O. Improvement Bonds Series 2010A and G.O. Improvement Bonds Series 2012B funds, which are considered to be major funds. Data from the remaining governmental funds is combined into a single, aggregated presentation. Individual fund data for each of these nonmajor governmental funds included in the combining fund statements in the supplementary information section of this report.

- Proprietary funds - The City maintains three enterprise funds which are included in these financial statements. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The City uses enterprise funds to account for operation of the Water Utility, Sewage Disposal, and Street Lighting funds, all of which are considered to be major funds.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail.

### **Notes to Financial Statements**

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

### **Other Information**

In addition to the basic financial statements and accompanying notes, this report also contains the combining statements referred to earlier in connection with nonmajor governmental funds. These statements follow the notes to the financial statements.

## CITY OF HERMANTOWN, MINNESOTA

MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)

**Government-wide Financial Analysis**

As noted earlier, over time net position may serve as a useful indicator of the City's financial position. A portion of the City's net position is invested in capital assets. The City uses these assets to provide services to its constituents; therefore, these assets are not available for future spending. The remaining balance of net position is unrestricted and may be used to meet the City's ongoing obligations to its constituents and creditors.

The following table presents a summary of the City's net position at December 31:

	2015			2014 Restated		
	Governmental Activities	Business- type Activities	Total	Governmental Activities	Business- type Activities	Total
<b>Assets</b>						
Current and other assets	\$ 19,880,091	\$ 7,440,521	\$ 27,320,612	\$ 19,709,281	\$ 6,624,946	\$ 26,334,227
Capital assets	19,873,399	34,210,526	54,083,925	20,686,919	34,850,536	55,537,455
Total assets	<u>39,753,490</u>	<u>41,651,047</u>	<u>81,404,537</u>	<u>40,396,200</u>	<u>41,475,482</u>	<u>81,871,682</u>
Deferred outflows of resources	<u>544,669</u>	<u>27,126</u>	<u>571,795</u>	<u>237,635</u>	<u>16,511</u>	<u>254,146</u>
<b>Liabilities</b>						
Long-term liabilities	24,110,257	259,831	24,370,088	28,075,813	252,123	28,327,936
Other liabilities	<u>2,409,615</u>	<u>115,301</u>	<u>2,524,916</u>	<u>743,326</u>	<u>242,359</u>	<u>985,685</u>
Total liabilities	<u>26,519,872</u>	<u>375,132</u>	<u>26,895,004</u>	<u>28,819,139</u>	<u>494,482</u>	<u>29,313,621</u>
Deferred inflows of resources	<u>273,291</u>	<u>12,891</u>	<u>286,182</u>			
<b>Net position</b>						
Invested in capital assets	12,839,838	34,210,526	47,050,364	13,160,927	34,850,536	48,011,463
Restricted	13,728,493	1,848,342	15,576,835	9,769,710	1,630,789	11,400,499
Unrestricted	<u>(13,063,335)</u>	<u>5,231,282</u>	<u>(7,832,053)</u>	<u>(11,115,941)</u>	<u>4,516,186</u>	<u>(6,599,755)</u>
Total net position	<u>\$ 13,504,996</u>	<u>\$ 41,290,150</u>	<u>\$ 54,795,146</u>	<u>\$ 11,814,696</u>	<u>\$ 40,997,511</u>	<u>\$ 52,812,207</u>

## CITY OF HERMANTOWN, MINNESOTA

MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)

To give users a better understanding of the sources and uses of the City's net position, the table that follows presents a summary of revenues, expenses, and changes in net position for the years ended December 31:

	2015			2014 Restated		
	Governmental Activities	Business- type Activities	Total	Governmental Activities	Business- type Activities	Total
<b>Revenues</b>						
Program revenues						
Charges for service	\$ 686,639	\$ 2,718,687	\$ 3,405,326	\$ 504,836	\$ 2,532,134	\$ 3,036,970
Operating grants and contributions	598,274		598,274	384,033		384,033
Capital grants and contributions	166,464		166,464	891,617		891,617
General revenues						
Property taxes	3,807,853		3,807,853	3,622,981		3,622,981
Sales tax	2,720,350		2,720,350	2,511,209		2,511,209
State aids	260,292		260,292	355,866		355,866
Interest	63,434	41,240	104,674	128,468	129,353	257,821
Other	372,081	270,763	642,844	428,621	416,736	845,357
Transfers	109,559	(109,559)		79,165	(79,165)	
Total revenues	<u>8,784,946</u>	<u>2,921,131</u>	<u>11,706,077</u>	<u>8,906,796</u>	<u>2,999,058</u>	<u>11,905,854</u>
<b>Expenses</b>						
General government	984,143		984,143	1,232,889		1,232,889
Public safety	3,146,397		3,146,397	2,923,221		2,923,221
Streets and highways	1,475,508		1,475,508	1,319,616		1,319,616
Community and economic development	477,479		477,479	68,782		68,782
Culture and recreation	243,876		243,876	198,345		198,345
Interest and fiscal charges	767,243		767,243	811,743		811,743
Water utility		1,269,668	1,269,668		1,335,674	1,335,674
Sewage disposal		1,302,629	1,302,629		1,271,428	1,271,428
Street lighting		56,195	56,195		37,212	37,212
Total expenses	<u>7,094,646</u>	<u>2,628,492</u>	<u>9,723,138</u>	<u>6,554,596</u>	<u>2,644,314</u>	<u>9,198,910</u>
Change in net position	1,690,300	292,639	1,982,939	2,352,200	354,744	2,706,944
Net position, beginning of year	<u>11,814,696</u>	<u>40,997,511</u>	<u>52,812,207</u>	<u>11,117,337</u>	<u>40,807,766</u>	<u>51,925,103</u>
Net position, end of year				13,469,537	41,162,510	54,632,047
Adjustment for valuation of net pension liability at December 31, 2014				(1,654,841)	(164,999)	(1,819,840)
Net position, end of year, restated				<u>\$ 11,814,696</u>	<u>\$ 40,997,511</u>	<u>\$ 52,812,207</u>
End of year net position	<u>\$ 13,504,996</u>	<u>\$ 41,290,150</u>	<u>\$ 54,795,146</u>			

The 2014 revenue and expense activity was restated for the correction of errors, not for the net pension liability, because the actuarial valuation used December 31, 2014 as the measurement date. Information relating to the pension liability prior to that date is not available. See Note 1 for information about restatement of activity and net position.

## CITY OF HERMANTOWN, MINNESOTA

MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)**Governmental Funds**

The focus of the City's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. This information is helpful in assessing the City's financing requirements; unrestricted fund balance may be an especially useful measure of the net resources available for spending at the end of the fiscal year. As of December 31, 2015, the City's governmental funds reported a combined fund balance of \$12,538,771, an increase of \$666,015 from the 2014 balance of \$11,872,756. Of the total fund balance amount, \$1,987,067 or 15.8 percent, which is reported as unassigned fund balance, is available for spending at the City's discretion.

The General Fund is the main operating fund of the City of Hermantown. At December 31, 2015, fund balance of the General Fund was \$3,477,148 with 94 percent reported as unassigned. As a measure of the General Fund's liquidity, it may be useful to compare total fund balance to total fund expenditures. Unassigned fund balance represents 74.2 percent of total General Fund expenditures. During 2015, the fund balance of the General Fund increased by \$53,515.

**Proprietary Funds**

The City's proprietary fund financial statements provide the same type of information found in the government-wide financial statements, only in more detail. The proprietary funds net position increased \$292,639 in 2015. Net operating income for 2015 was \$90,195.

**General Fund Budgetary Highlights**

The City adopted an original General Fund revenue budget of \$4,300,583 which was not revised during the year. The City adopted an original General Fund expenditure budget of \$4,327,766 which was revised to \$4,426,565.

The City's final budget for the General Fund anticipated that expenditures and other financing uses would exceed revenues and other financing sources by \$97,982, the actual results for the year showed revenues and other financing sources exceeding expenditures by \$53,515. Actual revenues and other financing sources were \$515,838 more than anticipated mostly due to:

- Additional tax revenue of \$134,500
- Additional state aids and grants of \$101,000
- Additional police services of \$36,000

Actual expenditures and other financing uses were \$364,341 more than anticipated due to a transfer to the General Capital Projects fund of \$370,000.

**Capital Assets**

The City of Hermantown's investment in capital assets as of December 31, 2015 was \$54,083,925, net of accumulated depreciation. This investment includes land, permanent easements, buildings, infrastructure, equipment and construction in progress. Additional information related to the City's capital assets can be found in Note 4 of the notes to the financial statements.

**Debt**

The City had \$23,083,860 in long-term obligations outstanding at the end of 2015.

The City continues to stay below the debt limits established by the State.

Other liabilities for obligations such as vacation, sick leave, net pension liability, and severance are discussed further in the note 5 to the financial statements.

## CITY OF HERMANTOWN, MINNESOTA

MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)**Economic Factors and Next Year's Budget**

The following key indicators provide highlights on the City's economic outlook and future budget impact:

- Development and Redevelopment Permits issued in 2015 were as follows: 4 commercial/industrial developments, 6 special use, 1 rezoning, 1 planned unit developments, 1 subdivision, and 3 zoning code amendments.
- Water purchase expense will increase 6% effective May 2016 due to the City of Duluth raising their rates. Hermantown's rates to its citizens will increase as well in June 2016.
- Holiday Inn Express and Mills Fleet Farm developments are scheduled to be completed in 2016.
- The City increased the total tax levy by 7.79% from \$3,828,912 to \$4,127,255 for the tax year 2016. At the December 2015 Truth and Taxation meeting, the City Council approved a local tax rate decrease from 36.54% in 2015 to 35.63% in 2016.
- Local Government Aid (LGA) for 2016 - Hermantown LGA was \$355,570 in 2014. In 2015 it decreased to \$259,511 and will further decrease to \$163,261 in 2016.

**Requests for Information**

This financial report is meant to provide a general overview of the City of Hermantown's finances for all those with an interest in the City's finances. Questions concerning information provided in the report, or requests for additional financial information, should be addressed to the City of Hermantown, 5105 Maple Grove Road, Hermantown, Minnesota 55811, or visit the City's website at [www.hermantownmn.com](http://www.hermantownmn.com)

## **BASIC FINANCIAL STATEMENTS**

## CITY OF HERMANTOWN, MINNESOTA

STATEMENT OF NET POSITION  
DECEMBER 31, 2015

	Governmental Activities	Business-type Activities	Total
<b>Assets</b>			
Cash and cash equivalents	\$ 12,500,666	\$ 6,174,918	\$ 18,675,584
Interest receivable		6,447	6,447
Accounts receivable, net of allowance	770,625	402,513	1,173,138
Interest receivable	7,572		7,572
Delinquent taxes receivable	182,834		182,834
Special assessments receivable	6,877,765	187,152	7,064,917
Contracts receivable		42,706	42,706
Internal balances	(550,000)	550,000	
Inventories		65,318	65,318
Prepaid items	90,629	11,467	102,096
Capital assets, net of depreciation			
Assets not being depreciated	2,170,516	607,514	2,778,030
Assets being depreciated, net	17,702,883	33,603,012	51,305,895
Total assets	<u>39,753,490</u>	<u>41,651,047</u>	<u>81,404,537</u>
Deferred outflows of resources	<u>544,669</u>	<u>27,126</u>	<u>571,795</u>
Total assets and deferred outflows of resources	<u>\$ 40,298,159</u>	<u>\$ 41,678,173</u>	<u>\$ 81,976,332</u>
<b>Liabilities</b>			
Accounts payable	\$ 102,726	\$ 82,318	\$ 185,044
Accrued wages and related liabilities	106,142	17,783	123,925
Customer deposits	50,735	15,200	65,935
Unearned revenue	75,961		75,961
Accrued interest	306,322		306,322
Long-term liabilities, net of current portion			
Amount due within one year	1,767,729		1,767,729
Amounts due in more than one year	24,110,257	259,831	24,370,088
Total liabilities	<u>26,519,872</u>	<u>375,132</u>	<u>26,895,004</u>
Deferred inflows of resources	<u>273,291</u>	<u>12,891</u>	<u>286,182</u>
<b>Net position</b>			
Net investment in capital assets	12,839,838	34,210,526	47,050,364
Restricted	13,728,493	1,848,342	15,576,835
Unrestricted	(13,063,335)	5,231,282	(7,832,053)
Total net position	<u>13,504,996</u>	<u>41,290,150</u>	<u>54,795,146</u>
Total liabilities, deferred inflows of resources and net position	<u>\$ 40,298,159</u>	<u>\$ 41,678,173</u>	<u>\$ 81,976,332</u>

See accompanying notes to financial statements.

CITY OF HERMANTOWN, MINNESOTA  
 STATEMENT OF ACTIVITIES  
 FOR THE YEAR ENDED DECEMBER 31, 2015

Functions/Programs	Program Revenues			Net (Expense) Revenue and Changes in Net Position		
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business- type Activities
<b>Governmental activities</b>						
General government	\$ 984,143	\$ 112,597	\$ 209,654	\$ 118,767	\$ (543,125)	\$ (543,125)
Public safety	3,146,397	397,856	238,825		(2,509,716)	(2,509,716)
Streets and highways	1,475,508		149,795	47,697	(1,278,016)	(1,278,016)
Community and economic development	477,479	3,770			(473,709)	(473,709)
Culture and recreation	243,876	172,416			(71,460)	(71,460)
Interest and fiscal charges	767,243				(767,243)	(767,243)
Total governmental activities	<u>\$ 7,094,646</u>	<u>\$ 686,639</u>	<u>\$ 598,274</u>	<u>\$ 166,464</u>	<u>(5,643,269)</u>	<u>(5,643,269)</u>
<b>Business-type activities</b>						
Water utility	\$ 1,269,668	\$ 1,267,225				(2,443)
Sewage disposal	1,302,629	1,317,311				14,682
Street lighting	56,195	134,151				77,956
Total business-type activities	<u>\$ 2,628,492</u>	<u>\$ 2,718,687</u>	<u>\$</u>	<u>\$</u>		<u>90,195</u>
<b>General revenues</b>						
Property taxes					3,807,853	3,807,853
Sales tax					2,720,350	2,720,350
State aids					260,292	260,292
Investment income					63,434	41,240
Other					372,081	270,763
Transfers					109,559	(109,559)
Total general revenues and transfers					<u>7,333,569</u>	<u>202,444</u>
Change in net position					1,690,300	292,639
Net position, beginning of the year, restated					<u>11,814,686</u>	<u>40,997,511</u>
Net position, end of the year					<u>\$ 13,504,996</u>	<u>\$ 41,290,150</u>

See accompanying notes to financial statements.

## CITY OF HERMANTOWN, MINNESOTA

BALANCE SHEET  
GOVERNMENTAL FUNDS  
DECEMBER 31, 2015

	General	City Sales Tax Fund	G.O. Improvement & Utility Revenue Bonds Series 2007B Fund	G.O. Improvement Bonds Series 2009A Fund	G.O. Improvement Bonds Series 2010A Fund	G.O. Improvement Bonds Series 2012B Fund	Other Governmental Funds	Total Governmental Funds
<b>Assets</b>								
Cash and cash equivalents	\$ 2,734,456	\$ 3,642,646	\$ 80,273	\$ 252,251	\$ 319,422	\$ 1,148,726	\$ 4,322,892	\$ 12,500,666
Accounts receivable	41,644	415,422					313,559	770,625
Interest receivable	4,161	2,893					518	7,572
Delinquent taxes receivable	155,304			5,607	11,138	4,429	6,356	182,834
Special assessments receivable			1,207,645	1,225,285	1,032,256	1,983,607	1,428,972	6,877,765
Prepaid items	90,447	108					74	90,629
Due from other funds	706,419							706,419
Advance to other funds	117,107						150,000	267,107
Total assets	<u>3,849,538</u>	<u>4,061,069</u>	<u>1,287,918</u>	<u>1,483,143</u>	<u>1,362,816</u>	<u>3,136,762</u>	<u>6,222,371</u>	<u>21,403,617</u>
<b>Deferred outflows of resources</b>								
Total assets and deferred outflows of resources	<u>\$ 3,849,538</u>	<u>\$ 4,061,069</u>	<u>\$ 1,287,918</u>	<u>\$ 1,483,143</u>	<u>\$ 1,362,816</u>	<u>\$ 3,136,762</u>	<u>\$ 6,222,371</u>	<u>\$ 21,403,617</u>
<b>Liabilities</b>								
Accounts payable	\$ 96,078	\$ 1,093	\$	\$	\$	\$	\$ 6,648	\$ 102,726
Accrued wages payable	104,846						203	106,142
Due to other funds							706,419	706,419
Deposits payable	45,735						5,000	50,735
Advance from other funds							817,107	817,107
Unearned revenue							75,961	75,961
Total liabilities	<u>246,659</u>	<u>1,093</u>					<u>1,611,338</u>	<u>1,859,090</u>
<b>Deferred inflows of resources</b>								
Delinquent property taxes	125,731			1,543			2,865	130,139
Deferred special assessments			1,207,645	1,225,285	1,032,256	1,983,607	1,426,824	6,875,617
Total deferred inflows of resources	<u>125,731</u>		<u>1,207,645</u>	<u>1,226,828</u>	<u>1,032,256</u>	<u>1,983,607</u>	<u>1,429,689</u>	<u>7,005,756</u>
<b>Fund balances</b>								
Nonspendable	90,447	108					74	90,629
Restricted		4,059,868	80,273	256,315	330,560	1,153,155	2,531,917	8,412,088
Committed	106,586						1,170,206	1,276,792
Assigned							772,195	772,195
Unassigned	3,280,115						(1,293,048)	1,987,067
Total fund balances	<u>3,477,148</u>	<u>4,059,976</u>	<u>80,273</u>	<u>256,315</u>	<u>330,560</u>	<u>1,153,155</u>	<u>3,181,344</u>	<u>12,538,771</u>
Total liabilities, deferred inflows of resources, and fund balances	<u>\$ 3,849,538</u>	<u>\$ 4,061,069</u>	<u>\$ 1,287,918</u>	<u>\$ 1,483,143</u>	<u>\$ 1,362,816</u>	<u>\$ 3,136,762</u>	<u>\$ 6,222,371</u>	<u>\$ 21,403,617</u>

See accompanying notes to financial statements.

## CITY OF HERMANTOWN, MINNESOTA

RECONCILIATION OF THE BALANCE SHEET TO THE STATEMENT OF NET POSITION  
GOVERNMENTAL FUNDS  
DECEMBER 31, 2015

Total fund balances - governmental funds	\$ 12,538,771
Amounts reported for governmental activities in the statement of activities are different because:	
Capital assets used in governmental activities are not financial resources and therefore are not reported as assets in governmental funds.	
Cost of capital assets	48,831,821
Less accumulated depreciation	(28,958,422)
Long-term liabilities are not due and payable in the current period and therefore are not reported as liabilities in the funds.	
	(23,750,731)
The net pension liability and the deferred outflows of resources and inflow of resources related to pensions are only reported in the statement of net position.	
Net pension liability	(2,127,255)
Deferred outflows of resources	544,669
Deferred inflows of resources	(273,291)
Long-term assets are not available to pay for current period expenditures and therefore are deferred in the funds.	
	7,005,756
Governmental funds do not report a liability for accrued interest until due and payable	
	<u>(306,322)</u>
Total net position - governmental activities	<u>\$ 13,504,996</u>

See accompanying notes to financial statements.

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

	General	City Sales Tax Fund	G.O. Improvement & Utility Revenue Bonds Series 2007B Fund	G.O. Improvement Bonds Series 2009A Fund	G.O. Improvement Bonds Series 2010A Fund	G.O. Improvement Bonds Series 2012B Fund	Other Governmental Funds	Total Governmental Funds
<b>Revenues</b>								
Taxes	\$ 3,623,092	\$ 2,720,350	\$	\$ 156,483	\$	\$	\$ 81,594	\$ 6,581,519
Special assessments			69,927	181,146	167,825	228,277	152,388	799,563
Licenses and permits	271,133						62,625	333,758
Intergovernmental	616,195						288,569	904,764
Charges for services	72,673						64,576	137,249
Fines and forfeitures	55,932						13,094	69,026
Investment income	30,041	16,955					16,438	63,434
Miscellaneous	109,484						78,491	187,975
Total revenues	<u>4,778,550</u>	<u>2,737,305</u>	<u>69,927</u>	<u>337,629</u>	<u>167,825</u>	<u>228,277</u>	<u>757,775</u>	<u>9,077,288</u>
<b>Expenditures</b>								
Current								
General government	837,697							837,697
Public safety	2,754,339						85,485	2,839,824
Streets and highways	528,471							528,471
Community and economic development	56,493	210,682					369,960	637,135
Culture and recreation	106,904						19,424	126,328
Capital outlay	125,595						188,551	314,146
Debt service								
Principal	8,735		95,000	290,000	300,000	135,000	1,631,020	2,459,755
Interest and fiscal charges	1,172		67,859	157,450	88,006	68,488	399,372	782,347
Total expenditures	<u>4,419,406</u>	<u>210,682</u>	<u>162,859</u>	<u>447,450</u>	<u>388,006</u>	<u>203,488</u>	<u>2,693,812</u>	<u>8,525,703</u>
Excess (deficiency) of revenues over expenditures	<u>359,144</u>	<u>2,526,623</u>	<u>(92,932)</u>	<u>(109,821)</u>	<u>(220,181)</u>	<u>24,789</u>	<u>(1,936,037)</u>	<u>551,585</u>
Other financing sources (uses)								
Transfer in	76,000		95,874	146,691	289,030	59,665	1,416,923	2,084,183
Transfer out	(386,500)	(1,354,861)					(233,263)	(1,974,624)
Sales of capital assets	4,871							4,871
Net other financing sources (uses)	<u>(305,629)</u>	<u>(1,354,861)</u>	<u>95,874</u>	<u>146,691</u>	<u>289,030</u>	<u>59,665</u>	<u>1,183,660</u>	<u>114,430</u>
Net change in fund balance	53,515	1,171,762	2,942	36,870	68,849	84,454	(752,377)	666,015
Fund balance, beginning, restated	<u>3,423,633</u>	<u>2,888,214</u>	<u>77,331</u>	<u>219,445</u>	<u>261,711</u>	<u>1,068,701</u>	<u>3,933,721</u>	<u>11,872,756</u>
Fund balance, ending	<u>\$ 3,477,148</u>	<u>\$ 4,059,976</u>	<u>\$ 80,273</u>	<u>\$ 256,315</u>	<u>\$ 330,560</u>	<u>\$ 1,153,155</u>	<u>\$ 3,181,344</u>	<u>\$ 12,538,771</u>

See accompanying notes to financial statements.

## CITY OF HERMANTOWN, MINNESOTA

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

Total net changes in fund balances - governmental funds	\$ 666,015
Amounts reported for governmental activities in the statement of activities are different because:	
Capital outlays are reported in governmental funds as expenditures. However in the statement of activities, the costs of those assets is allocated over the estimated useful lives as depreciated expense.	
Capital outlays	477,673
Depreciation expense	(1,291,189)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.	(402,572)
The issuance of long-term debt provides current financial resources to governmental funds, but increases long-term liabilities in the statement of net position. Also, governmental funds report the effect of premiums, discounts, and similar items when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities. This amount is the net effect of these differences.	
	6,301
Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net position.	2,459,755
Interest on long-term debt in the statement of activities differs from the amount reported in the governmental funds because interest is recognized as an expenditure in the funds when it is due. However, in the statement of activities, interest expense is recognized as it accrues, regardless of when due.	8,803
Vested employee benefits are reported in the governmental funds when amounts are paid. The statement of activities reports the value of the benefits earned during the year.	
Change in net OPEB obligation	(64,770)
Change in deferred outflows of resources related to pensions	307,034
Change in deferred inflows of resources related to pensions	(273,291)
Change in pension liability	(234,779)
Compensated absences are an expense in the governmental funds, but increase long-term liabilities in the statement of net position.	31,320
Change in net position - governmental activities	\$ 1,690,300

See accompanying notes to financial statements.

## CITY OF HERMANTOWN, MINNESOTA

## GENERAL FUND

STATEMENT OF REVENUES, EXPENDITURES, AND  
CHANGES IN FUND BALANCE - BUDGET AND ACTUAL  
FOR THE YEAR ENDED DECEMBER 31, 2015

	Budget		Actual	Variance Over (Under)
	Original	Final		
<b>Revenues</b>				
Taxes	\$ 3,467,000	\$ 3,467,000	\$ 3,623,092	\$ 156,092
Licenses and permits	240,590	240,590	271,133	30,543
Intergovernmental	453,011	453,011	616,195	163,184
Charges for services	29,674	29,674	72,673	42,999
Fines and forfeitures	58,300	58,300	55,932	(2,368)
Investment income	22,050	22,050	30,041	7,991
Miscellaneous	29,958	29,958	109,484	79,526
Total revenues	<u>4,300,583</u>	<u>4,300,583</u>	<u>4,778,550</u>	<u>477,967</u>
<b>Expenditures</b>				
Current				
General government	859,797	856,996	837,697	(19,299)
Public safety	2,636,162	2,707,162	2,754,339	47,177
Streets and highways	603,781	616,481	528,471	(88,010)
Community and economic development			56,493	56,493
Culture and recreation	118,669	136,569	106,904	(29,665)
Capital outlay	99,450	99,450	125,595	26,145
Debt service				
Principal	8,710	8,710	8,735	25
Interest and fiscal charges	1,197	1,197	1,172	(25)
Total expenditures	<u>4,327,766</u>	<u>4,426,565</u>	<u>4,419,406</u>	<u>(7,159)</u>
Excess (deficiency) of revenues over expenditures	<u>(27,183)</u>	<u>(125,982)</u>	<u>359,144</u>	<u>485,126</u>
<b>Other financing sources (uses)</b>				
Transfer in	40,000	40,000	76,000	36,000
Transfer out	(15,000)	(15,000)	(386,500)	(371,500)
Sales of capital assets	3,000	3,000	4,871	1,871
Net other financing sources (uses)	<u>28,000</u>	<u>28,000</u>	<u>(305,629)</u>	<u>(333,629)</u>
Net change in fund balance	<u>\$ 817</u>	<u>\$ (97,982)</u>	<u>53,515</u>	<u>\$ 151,497</u>
Fund balance, beginning			<u>3,423,633</u>	
Fund balance, ending			<u>\$ 3,477,148</u>	

See accompanying notes to financial statements.

## CITY OF HERMANTOWN, MINNESOTA

## CITY SALES TAX FUND

STATEMENT OF REVENUES, EXPENDITURES, AND  
CHANGES IN FUND BALANCE - BUDGET AND ACTUAL  
FOR THE YEAR ENDED DECEMBER 31, 2015

	Budget		Actual	Variance Over (Under)
	Original	Final		
Revenues				
Taxes				
Sales Taxes	\$ 2,410,000	\$ 2,410,000	\$ 2,720,350	\$ 310,350
Investment Income	25,500	25,500	16,955	(8,545)
Total revenues	<u>2,435,500</u>	<u>2,435,500</u>	<u>2,737,305</u>	<u>301,805</u>
Expenditures				
Current				
Economic development	38,603	38,603	210,682	172,079
Total expenditures	<u>38,603</u>	<u>38,603</u>	<u>210,682</u>	<u>172,079</u>
Excess revenues over expenditures	2,396,897	2,396,897	2,526,623	129,726
Other financing uses				
Transfer out	<u>(1,354,859)</u>	<u>(1,354,859)</u>	<u>(1,354,861)</u>	<u>(2)</u>
Net change in fund balance	<u>\$ 1,042,038</u>	<u>\$ 1,042,038</u>	1,171,762	<u>\$ 129,724</u>
Fund balance, beginning			<u>2,888,214</u>	
Fund balance, ending			<u>\$ 4,059,976</u>	

See accompanying notes to financial statements.

## CITY OF HERMANTOWN, MINNESOTA

STATEMENT OF NET POSITION  
PROPRIETARY FUNDS  
DECEMBER 31, 2015

	Business-type Activities Enterprise Fund			Total Enterprise Funds
	Water Utility Funds	Sewage Disposal Fund	Street Lighting Fund	
<b>Assets</b>				
Current assets				
Cash and cash equivalents	\$ 3,160,219	\$ 2,888,254	\$ 126,445	\$ 6,174,918
Interest receivable	4,027	1,425	995	6,447
Accounts receivable, net of allowance	162,027	215,205	25,281	402,513
Contracts receivable	3,997	36,288		40,285
Advance from other funds			550,000	550,000
Inventories	52,349	12,969		65,318
Prepaid items	5,986	5,481		11,467
Total current assets	<u>3,388,605</u>	<u>3,159,622</u>	<u>702,721</u>	<u>7,250,948</u>
Noncurrent assets				
Capital assets, net of depreciation				
Assets not being depreciated	221,869	385,645		607,514
Assets being depreciated, net	7,489,296	26,106,236	7,480	33,603,012
Total capital assets, net of depreciation	<u>7,711,165</u>	<u>26,491,881</u>	<u>7,480</u>	<u>34,210,526</u>
Long-term portion of contracts receivable	1,052	1,369		2,421
Special assessments receivable	4,996	182,156		187,152
Total noncurrent assets	<u>7,717,213</u>	<u>26,675,406</u>	<u>7,480</u>	<u>34,400,099</u>
Deferred outflows of resources	<u>15,500</u>	<u>11,626</u>		<u>27,126</u>
Total assets and deferred outflows of resources	<u>\$ 11,121,318</u>	<u>\$ 29,846,654</u>	<u>\$ 710,201</u>	<u>\$ 41,678,173</u>
<b>Liabilities</b>				
Current liabilities				
Accounts payable	\$ 47,966	\$ 25,179	\$ 9,173	\$ 82,318
Accrued wages and related liabilities	10,268	7,515		17,783
Deposits	15,200			15,200
Total current liabilities	<u>73,434</u>	<u>32,694</u>	<u>9,173</u>	<u>115,301</u>
Noncurrent liabilities				
Compensated absences	37,707	25,138		62,845
Net pension liability	112,564	84,422		196,986
Total noncurrent liabilities	<u>150,271</u>	<u>109,560</u>		<u>259,831</u>
Total liabilities	<u>223,705</u>	<u>142,254</u>	<u>9,173</u>	<u>375,132</u>
Deferred inflows of resources	<u>7,366</u>	<u>5,525</u>		<u>12,891</u>
<b>Net position</b>				
Net investment in capital assets	7,711,165	26,491,881	7,480	34,210,526
Restricted for replacement, depreciation, & development	706,670	1,141,672		1,848,342
Unrestricted	2,472,412	2,065,322	693,548	5,231,282
Total net position	<u>10,890,247</u>	<u>29,698,875</u>	<u>701,028</u>	<u>41,290,150</u>
Total liabilities, deferred inflows of resources, and net position	<u>\$ 11,121,318</u>	<u>\$ 29,846,654</u>	<u>\$ 710,201</u>	<u>\$ 41,678,173</u>

See accompanying notes to financial statements.

## CITY OF HERMANTOWN, MINNESOTA

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

	Business-type Activities Enterprise Fund			Total Enterprise Funds
	Water Utility Funds	Sewage Disposal Fund	Street Lighting Fund	
Operating revenues				
User fees	\$ 1,187,945	\$ 1,249,302	\$ 134,151	\$ 2,571,398
Service charges	79,280	68,009		147,289
Total operating revenues	<u>1,267,225</u>	<u>1,317,311</u>	<u>134,151</u>	<u>2,718,687</u>
Operating expenses				
Personal services	310,180	222,595		532,775
Water purchases	665,752			665,752
WLSSD charges		477,306		477,306
Maintenance and supplies	105,949	91,645	11,291	208,885
Utilities	6,688	8,175	27,488	42,351
Professional services	7,051	6,987	14,200	28,238
Insurance	5,685	8,004		13,689
Depreciation expense	168,363	487,917	3,216	659,496
Total operating expenses	<u>1,269,668</u>	<u>1,302,629</u>	<u>56,195</u>	<u>2,628,492</u>
Net operating income (loss)	(2,443)	14,682	77,956	90,195
Nonoperating revenues				
Hookups and miscellaneous income	156,324	114,439		270,763
Investment income	21,334	1,433	18,473	41,240
Total nonoperating revenues	<u>177,658</u>	<u>115,872</u>	<u>18,473</u>	<u>312,003</u>
Income before transfers	175,215	130,554	96,429	402,198
Transfer in	1,500			1,500
Transfer out	<u>(48,903)</u>	<u>(59,656)</u>	<u>(2,500)</u>	<u>(111,059)</u>
Change in net position	127,812	70,898	93,929	292,639
Net position, beginning, restated	<u>10,762,435</u>	<u>29,627,977</u>	<u>607,099</u>	<u>40,997,511</u>
Net position, ending	<u>\$ 10,890,247</u>	<u>\$ 29,698,875</u>	<u>\$ 701,028</u>	<u>\$ 41,290,150</u>

See accompanying notes to financial statements.

## CITY OF HERMANTOWN, MINNESOTA

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

	Business-type Activities Enterprise Fund			Total Enterprise Funds
	Water Utility Funds	Sewage Disposal Fund	Street Lighting Fund	
Cash flows from operating activities				
Receipts from users	\$ 1,273,779	\$ 1,288,991	\$ 145,137	\$ 2,707,907
Payments to employees	(301,055)	(215,270)		(516,325)
Payments to suppliers	(849,850)	(641,981)	(50,034)	(1,541,865)
Interfund receipts/payments		143,388	(143,388)	
Cash received from hookups and miscellaneous income	126,412	100,376		226,788
Net cash provided by operating activities	<u>249,286</u>	<u>675,504</u>	<u>(48,285)</u>	<u>876,505</u>
Cash flows from noncapital financing activities				
Transfers out	(47,403)	(59,656)	(2,500)	(109,559)
Advances to other funds			(200,000)	(200,000)
Net cash used in noncapital financing activities	<u>(47,403)</u>	<u>(59,656)</u>	<u>(202,500)</u>	<u>(309,559)</u>
Cash flows from capital and related financing activities				
Acquisition and construction of capital assets		(19,485)		(19,485)
Capital contributions	(183)	(396)		(579)
Net cash used in capital and related financing activities	<u>(183)</u>	<u>(19,881)</u>		<u>(20,064)</u>
Cash flows from investing activities				
Investment income	23,512	1,434	18,473	43,419
Net cash provided by investing activities	<u>23,512</u>	<u>1,434</u>	<u>18,473</u>	<u>43,419</u>
Net increase in cash and cash equivalents	225,212	597,401	(232,312)	590,301
Cash and cash equivalents, beginning of year	<u>2,935,007</u>	<u>2,290,853</u>	<u>358,757</u>	<u>5,584,617</u>
Cash and cash equivalents, end of year	<u>\$ 3,160,219</u>	<u>\$ 2,888,254</u>	<u>\$ 126,445</u>	<u>\$ 6,174,918</u>

See accompanying notes to financial statements.

CITY OF HERMANTOWN, MINNESOTA  
 STATEMENT OF CASH FLOWS  
 PROPRIETARY FUNDS  
 FOR THE YEAR ENDED DECEMBER 31, 2015

	Business-type Activities Enterprise Fund			Total Enterprise Funds
	Water Utility Funds	Sewage Disposal Fund	Street Lighting Fund	
Reconciliation of operating income to net cash provided by (used in) operating activities				
Operating income (loss)	\$ (2,443)	\$ 14,682	\$ 77,956	\$ 90,195
Adjustments to reconcile operating income to net cash provided by (used in) operating activities				
Depreciation	168,363	487,917	3,216	659,496
Hookups and miscellaneous income	156,324	114,439		270,763
Change in pension related items	10,145	7,607		17,752
(Increase) decrease in assets				
Accounts receivable	6,555	(28,320)	10,986	(10,779)
Contracts receivable	2,151	(14,063)		(11,912)
Prepaid expenses	(685)	1,784		1,099
Due from other funds		143,388		143,388
Inventories	(4,468)	(814)		(5,282)
Increase (decrease) in liabilities				
Accounts payable	(53,572)	(50,834)	2,945	(101,461)
Wages and related liabilities	3,641	2,825		6,466
Due to other funds			(143,388)	(143,388)
Deferred income	(32,063)			(32,063)
Compensated absences payable	(4,662)	(3,107)		(7,769)
Total adjustments	251,729	660,822	(126,241)	786,310
Net cash provided by (used in) operating activities	\$ 249,286	\$ 675,504	\$ (48,285)	\$ 876,505

See accompanying notes to financial statements.

CITY OF HERMANTOWN, MINNESOTA  
NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015

**NOTE 1      SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The City complies with accounting principles generally accepted (GAAP) in the United States. GAAP includes all relevant Governmental Accounting Standards Board (GASB) pronouncements. The accounting and reporting framework and the more significant accounting policies are discussed in subsequent subsections of this Note.

**Financial Reporting Entity**

The City of Hermantown, Minnesota, was incorporated under the laws of the State of Minnesota and operates under an elected Mayor-Council form of government. In determining the financial reporting entity, the City complies with GAAP and includes all component units of which the City appointed a voting majority of the units' board, either the City is able to impose its will on the unit, or a financial benefit or burden relationship exists. As a result of applying these component unit criteria, the Hermantown Economic Development Authority is considered a component unit and is represented in the City's financial statements as a blended component unit, meaning it is reported as if it were a part of the City. The Hermantown Economic Development Authority does not issue separate financial statements.

**Blended component unit**

The Hermantown Economic Development Authority (HEDA) provides services almost entirely to the City and is governed by a board of seven commissioners, which is substantially the same as the City Council. In 1998, HEDA passed a resolution for the issuance and sale of sales tax revenue bonds to build a new public safety facility. The City was given authority to impose a local sales tax in 1996 that allowed the City to utilize the proceeds to meet the principal and interest payments of the bond. In 2006, this bond was refunded with a new bond that included the construction of the new city hall. The City is financially accountable for HEDA. The City approves the budget, levies taxes (if necessary), and must approve debt issuances. HEDA has had limited activity and meets when called by the City Administrator, usually for its annual meeting. For these reasons, HEDA is recognized as a blended component unit of the City.

**Related organization**

The Hermantown Volunteer Fire Department is a legally separate organization from the City. Related party transactions are limited to payments by the City on a contract for service entered into with the Hermantown Volunteer Fire Department. The City made payments totaling \$375,000 during 2015.

**Basis of Presentation**

***Government-wide Financial Statements***

The government-wide financial statements (statement of net position and statement of activities) report information on all activities of the primary government. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 1      SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

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

Separate financial statements are provided from governmental funds and proprietary funds. Major individual governmental funds and major individual enterprise funds are reported in separate columns in the fund financial statements.

***Fund Financial Statements***

The accounts of the City are organized and operated on the basis of funds. A fund is an independent fiscal and accounting entity with a self-balancing set of accounts. The fund financial statements are provided for governmental funds and proprietary funds. The emphasis of fund financial statements is on the major governmental and enterprise funds, each displayed in a separate column. All remaining governmental and enterprise funds are aggregated and reported as other funds (nonmajor).

The funds of the financial reporting entity are described below:

**Governmental Funds**

***General Fund*** – The General Fund is the general operating fund of the City. It is used to account for all financial resources except those reported in another fund.

***Special Revenue Funds*** – These funds are used to account for and report the proceeds of specific revenue sources that are restricted or committed to expenditure for specified purposes other than debt service or capital projects.

***Debt Service Funds*** – These funds are used to account for the accumulation of resources for and the payment of general long-term obligation principal, interest, and related costs other than those financed by the city sales tax and proprietary funds.

***Capital Projects Funds*** – These funds are used to account for and report financial resources that are restricted, committed, or assigned to expenditure for capital outlays including the acquisition or construction of capital facilities and other capital assets.

**Proprietary Funds**

***Enterprise Funds*** – The Enterprise Funds are used to account for those operations which are financed and operated in a manner similar to private business or for which the board has decided that the determination of revenues earned, costs incurred, and/or net income is necessary for management accountability.

CITY OF HERMANTOWN, MINNESOTA  
NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)

**NOTE 1      SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Major Governmental Funds**

**General Fund** – Accounts for all financial resources except those reported in another fund. It is the general operating fund of the City.

**City Sales Tax Fund** – Accounts for the restricted sales tax revenues collected that are authorized by the Minnesota State Legislature to fund the construction of a public safety facility, city administrative services facility, and Hermantown sewer trunk line and water infrastructure improvements.

**General Obligation Improvement & Utility Revenue Bonds, Series 2007B Fund** – Accounts for the accumulated resources to pay the interest and principal payments on the General Obligation Improvement & Utility Revenue Bonds, Series 2007B.

**General Obligation Improvement Bonds, Series 2009A Fund** – Accounts for the accumulated resources to pay the interest and principal payments on the General Obligation Improvement Bonds, Series 2009A.

**General Obligation Improvement Bonds, Series 2010A Fund** – Accounts for the accumulated resources to pay the interest and principal payments on the General Obligation Improvement Bonds, Series 2010A.

**General Obligation Improvement Bonds, Series 2012B Fund** – Accounts for the accumulated resources to pay the interest and principal payments on the General Obligation Improvement Bonds, Series 2012B.

**Major Proprietary Funds**

**Water Utility Fund** – Accounts for the activity of providing water services to the public.

**Sewage Disposal Fund** – Accounts for the activity of providing sewer disposal services to the public.

**Street Lighting Fund** – Accounts for the activity of lighting and signaling public streets.

**Measurement Focus and Basis of Accounting**

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund statements. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are generally recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

## CITY OF HERMANTOWN, MINNESOTA

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities for the current period. For this purpose, the City considers all revenues, except reimbursement grants, to be available if they are collected within 60 days of the end of the current fiscal year. Reimbursement grants are considered available if they are collected within one year of the end of the current fiscal period. Expenditures generally are recorded when the liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes, sales taxes, franchise fees, special assessments, intergovernmental revenues, charges for service, and interest associated with the current fiscal period are all considered susceptible to accrual and therefore have been recognized as revenues of the current fiscal period. Only the portion of special assessments receivable due within the current fiscal period is considered to be susceptible to accrual as revenue of the current period. All other revenue items are considered to be measurable and available only when cash is received by the City.

**Assets, Liabilities, and Equity****Cash and Cash Equivalents**

Cash balances from all funds are combined and invested to the extent available in certificates of deposit and other short-term securities. Earnings from such investments are allocated to the respective funds on the basis of average cash balance participation by each fund.

Investments are stated at fair value, based on quoted market prices, except for investments in 2a7-like external investment pools, which are stated at amortized cost. Investment income is accrued at the balance sheet date.

For purposes of the proprietary fund-type statements of cash flows, the City considers all legal investments authorized by Minnesota statutes with a maturity of three months or less to be cash equivalents.

**Interfund Transactions**

Activities between funds that are representative of lending/borrowing arrangements are reported as "due to/from other funds" and "advances to/from other funds." Interfund receivables and payables between funds within governmental activities are eliminated in the statement of net position.

**Receivables**

In the government-wide statements, receivables consist of all revenues earned at year-end and not yet received. Allowances for uncollectible receivables are based on historical trends and the periodic aging of accounts. Business-type activities report utilities as their major receivables.

Accounts receivable for utility receivables are shown at a gross amount, since utility receivables are assessable to the property taxes and are collectible upon sale of the assessed property.

CITY OF HERMANTOWN, MINNESOTA  
NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)

**NOTE 1      SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Property Taxes**

Property tax levies are set by the City Council in December of each year and are certified to St. Louis County for collection in the following year. In Minnesota, counties act as collection agents for all property taxes. The County spreads all levies over taxable property. Such taxes become a lien on January 1 and are recorded as receivables by the City on that date. Revenues are accrued and recognized in the year collectible, net of delinquencies. Real property taxes may be paid by taxpayers in two equal installments on May 15 and October 15. Personal property taxes may be paid on February 28 and June 30. The County provides tax settlements to cities and other taxing districts in January, June or July, and November or December.

Delinquent taxes have been offset by a deferred inflow of resources for delinquent taxes not received within 60 days after year-end in the governmental fund financial statements. No allowance for uncollectible taxes has been provided because such amounts are not expected to be material.

**Special Assessments**

Special assessments are levied against benefited properties for the cost or a portion of the cost of special assessment improvement projects in accordance with state statutes. These assessments are collectible by the City over a term of years as approved through City Council Resolution. Collection of annual installments (including interest) is handled by the county auditor in the same manner as property taxes. Property owners are allowed to prepay future installments without interest or prepayment penalties.

Once a special assessment roll is adopted, the amount attributed to each parcel is a lien on that property until full payment is made or the amount is determined to be excessive by the City Council or court action. If special assessments are allowed to become delinquent, the property is subject to tax forfeit sale, and the first proceeds of that sale (after costs, penalties, and expenses of sale) are remitted to the City in payment of delinquent special assessments. Generally, the City will collect the full amount of its special assessments not adjusted by the City Council or court action. Pursuant to state statutes, a property shall be subject to a tax forfeit sale after three years unless it is homesteaded, agricultural, or seasonal recreational land, in which event the property is subject to such sale after five years.

**Prepaid Items**

Payments made to vendors for services that will benefit periods beyond December 31, 2015, are recorded as prepaid items. Prepaid items are reported using the consumption method and recorded as expenditures/expenses at the time of consumption.

**Inventories**

All inventories are valued at cost using the first-in, first-out (FIFO) method. Inventories are recorded as expenditures when consumed rather than when purchased.

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Capital Assets**

Capital assets, which include property, plant, equipment, and infrastructure assets (e.g., roads, bridges, sidewalks, and similar items) and intangible assets such as easements, are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets, including infrastructure assets, are defined by the City as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of two years. In the case of donations, the government values these capital assets at the estimated fair market value on the date of its donation. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed.

Capital assets are depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Land Improvements	10 - 50
Buildings	10 - 40
Equipment	3 - 25
Infrastructure	15 -25
Transmission System, Source of Supply, And Pumping Plant	50 - 99

**Compensated Absences**

It is the City's policy to permit employees to accumulate earned but unused vacation leave and sick pay benefits. Vested employees also receive a lump sum payment to a health care savings plan if they retire. The liability for these compensated absences is recorded as long-term debt in the government-wide financial statements. In the fund financial statements, governmental funds report only the compensated absences liability payable if they have matured, for example, as a result of employee resignations and retirements. The proprietary funds report the liability as it is incurred.

**Long-Term Liabilities**

In the government-wide financial statements and for the proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund-type statement of net position. The recognition of bond premiums and discounts is amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable premium or discount. Bond issuance costs are reported as an expense in the period they occurred.

In the fund financial statements, governmental funds recognize bond premiums and discounts, as well as issuance costs, during the current period. Premiums received on debt issuances are reported as other financing sources, while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

CITY OF HERMANTOWN, MINNESOTA  
NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)

**NOTE 1      SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Pensions**

For the purposes of measuring the net pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about fiduciary net position of the Public Employees Retirement Association (PERA) and additions to/deductions from PERA's fiduciary net position have been determined on the same basis as they are reported by PERA except that PERA's fiscal year is June 30. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

**Other Postemployment Benefits (OPEB)**

The City provides other postemployment benefits (OPEB) to some retired employees based on eligibility established by contracts with bargaining units or other employment contracts. Retirees are required to pay 100% of their premium cost for the City-sponsored group health insurance plan in which they participate.

**Deferred Outflows/Inflows of Resources**

In addition to assets, the statement of financial position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to future period(s) and so will not be recognized as an outflow of resources (expense/expenditure) until then. The City has reported deferred outflows related to pensions for its proportionate shares of collective deferred outflows of resources related to pensions and the City's contributions to pension plans subsequent to the measurement date of the collective net pension liability.

In addition to liabilities, the statement of financial position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The City has reported unavailable revenue from delinquent property taxes, which arises only under a modified accrual basis of accounting, in the governmental funds balance sheet. The City has also reported deferred inflows of resources for its proportionate share of the collective deferred inflows of resources related to pensions.

**Fund Balance Classifications**

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

*Nonspendable* – Consists of amounts that are not in spendable form, such as prepaid items.

*Restricted* – Consists of amounts related to externally imposed constraints established by creditors, grantors, or contributors or constraints imposed by state statutory provisions.

*Committed* – Consists of internally imposed constraints. The City Council will annually, or as deemed necessary, commit specific revenue sources for specified purpose by resolution. This formal action must occur prior to the end of the reporting period; however, the amount to be subject to the constraint may be determined in the subsequent period. To remove the constraint on specified use of committed resources, the City Council shall pass a resolution.

CITY OF HERMANTOWN, MINNESOTA  
NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)

**NOTE 1      SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

*Assigned* – Consists of internally imposed constraints. These constraints reflect the specific purpose for which it is the City's intended use. These constraints are established by the City Council and/or management. Pursuant to City Council resolution, the City's Finance Director is authorized to establish assignments of fund balance.

*Unassigned* – Is the residual classification for the General Fund and also reflects negative residual amounts in other funds.

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

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

The City Council has formally adopted a policy regarding the minimum unrestricted fund balance for the General Fund. The policy establishes a year-end targeted unrestricted fund balance of 35%-50%, no less than five months of the next year's budgeted expenditures. This will assist in maintaining an adequate level of fund balance to provide for cash flow requirements and contingency needs because major revenues, including property taxes and other governmental aids, are received in the second half of the City's fiscal year. At December 31, 2015, the unassigned fund balance for the General Fund was 69% of the subsequent year's budgeted expenditures, or \$3,280,115.

**Net Position**

Net position represents the difference between assets and deferred outflows of resources and liabilities and deferred inflow of resources in the government-wide and proprietary financial statements. Net investment in capital assets consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any long-term debt used to construct or acquire the capital assets. Restricted net position consists of net position with constraints on their use by external restrictions imposed by creditors, grantors, and laws or regulations of other governments. Unrestricted net position is all other net position that does not meet the definition of *restricted or investment in capital assets*.

**Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make 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 revenues and expenses during the reporting period. Actual results could differ from those estimates.

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Implementation of New Standards and Restatement of Prior Year Equity**

During 2015, the City adopted GASB Statement No. 68, *Accounting and Financial Reporting for Pensions* and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – An Amendment of GASB Statement No. 68*. The statements establish standards of accounting and financial reporting for defined benefit pensions provided to employees of local governmental employers. Implementation resulted in recognition of pension expense as well as the reporting of deferred outflows and inflows of resources and a net position liability based on the City's proportional share of those of the plan.

Also, during 2015, there were several errors in the balances reported as of December 31, 2014. Accounts payable was overstated by \$85,148 in the Special Assessment Deficiency Fund. Unearned revenue was overstated by \$181,760 in the Sewer.

The adoption of the new standard and correction of errors resulted in the restatement of net position and fund balance at December 31, 2014 as follows:

	Governmental Activities	Special Assessment Deficiency Fund	Business-type Activities	
			Water Fund	Sewer Fund
Net Position, as previously reported at December 31, 2014	\$ 13,384,389		\$ 10,856,720	\$ 29,516,931
Net pension liability	(1,892,476)		(103,720)	(77,790)
Deferred outflows of resources	237,635		9,435	7,076
Correction to overstated unearned revenue				181,760
Correction to overstated accounts payable	85,148			
Net Position, as restated, at December 31, 2014	<u>\$ 11,814,696</u>		<u>\$ 10,762,435</u>	<u>\$ 29,627,977</u>
Fund balance, as previously reported at December 31, 2014		\$ 688,560		
Correction to accounts payable		85,148		
Fund balance, as restated, at December 31, 2014		<u>\$ 773,708</u>		

**Subsequent Events**

In preparing these financial statements, the City has evaluated events and transactions for potential recognition or disclosure through April 14, 2016, the date the financial statements were available to be issued.

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 1      SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Stewardship, Compliance, and Accountability**

**Budgetary Information**

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

1. Annual budgets are adopted for the General Fund, Special Revenue Fund, and Debt Service Funds. The budget is adopted on a basis consistent with GAAP. Budgetary comparisons presented in this report are on a budgetary basis. Budgeted expenditure appropriations lapse at year-end. Budgeted amounts are as originally adopted or as amended by the City Council.
2. The budget is legally enacted through passage of a resolution.
3. The government's department heads may make transfers of appropriations within a department. The City Council may authorize transfer of budgeted amounts between departments.
4. Formal budgetary integration is employed as a management control device during the year.

Budgetary control for capital project funds is accomplished through the use of project controls.

**NOTE 2      DEPOSITS AND INVESTMENTS**

**Deposits**

Minn. Stats. 118A.02 and 118A.03 authorize the City to designate, as a depository for public funds, one or more financial institutions. Minn. Stat. 118A.03 requires that all governmental deposits be protected by insurance, surety bond, or collateral. The market value of collateral pledged shall be at least 10 percent more than the amount on deposit at the close of the financial institution's banking day. The financial institution may furnish both a surety bond and collateral aggregating the required amount.

The following are the allowable forms of collateral in lieu of a corporate surety bond: treasury bills, notes, and bonds; issues of U.S. government agencies; general obligations rated "A" or better; revenue obligations rated "AA" or better; general obligation securities of a local government with taxing powers pledged as collateral against funds deposited by that same local government entity; irrevocable standby letters of credit issued by the Federal Home Loan Bank; and certificates of deposit. Minn. Stat. 118A.03 reads: "All collateral shall be placed in safekeeping in a restricted account at a Federal Reserve Bank, or in an account at a trust department of a commercial bank or other financial institution that is not owned or controlled by the financial institution furnishing the collateral."

**Custodial Credit Risk – Deposits.** Custodial credit risk is the risk that in the event of financial institution failure, the City's deposits may not be returned to it. The City requires collateral for deposits over FDIC insurance amounts. The City has no additional deposit policies addressing custodial credit risk. As of December 31, 2015, the City's deposits were not exposed to custodial credit risk.

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 2 DEPOSITS AND INVESTMENTS (Continued)**

**Investments**

Minn. Stats. 118A.04, 118A.05, and 118A.06 generally authorize the following types of investments as available to the City:

- (1) Public funds may be invested in governmental bonds, notes, bills, mortgages (excluding high-risk mortgage-backed securities), and other securities that 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;
- (2) Funds may be invested in the following state and local securities: any security that is a general obligation of any state or local government with taxing powers and is rated "A" or better by a national bond rating service; any security that is a revenue obligation of any state or local government with taxing powers and is rated "AA" or better by a national bond rating service; and a general obligation of the Minnesota housing finance agency that is a moral obligation of the state of Minnesota and is rated "A" or better by a national bond rating agency;
- (3) Time deposits: Funds may be invested in time deposits that are fully insured by the Federal Deposit Insurance Corporation or bankers' acceptances of United States banks;
- (4) Commercial paper issued by United States corporations or their Canadian subsidiaries that is rated in the highest quality category by at least two nationally recognized rating agencies and matures in 270 days or less;
- (5) With certain restrictions, in repurchase agreements, securities lending agreements, joint powers investment trusts, and guaranteed investment contracts; and
- (6) Investments, contracts, and agreements may be held in safekeeping with any Federal Reserve Bank; any bank authorized under the laws of the United States or any state to exercise corporate trust powers, including but not limited to the bank from which the investment is purchased; a primary reporting dealer in United States government securities to the Federal Reserve Bank of New York; or a securities broker-dealer, or an affiliate of it, that meets the following requirements: it is registered as a broker-dealer under Chapter 80A or is exempt from the registration requirements; it is regulated by the Securities and Exchange Commission; and it maintains insurance through the Securities Investor Protection Corporation or excess insurance coverage in an amount equal to or greater than the value of the securities held, provided that the government entity's ownership of all securities is evidenced by written acknowledgements identifying the securities by the names of the issuers, maturity dates, interest rates, CUSIP number, or other distinguishing marks.

**Custodial Credit Risk – Investments** – For investments in securities, custodial credit risk is the risk that in the event of failure of the counterparty to a transaction, the City will not be able to recover the value of its investment securities that are in the possession of an outside party. Investments in investment pools and money markets are not evidenced by securities that exist in physical or book entry form, and therefore are not subject to custodial credit risk disclosures. The City's investment policy does not address custodial credit risk. However, investments in securities are held by the City's broker-dealer, and \$500,000 of these is insured through SIPC (Securities Investor Protection Corporation). Each broker-dealer has provided additional protection by providing additional insurance. This insurance is subject to aggregate limits applied to all of the broker-dealer accounts.

## CITY OF HERMANTOWN, MINNESOTA

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)

**NOTE 2 DEPOSITS AND INVESTMENTS (Continued)**

At December 31, 2015, the City had the following investments:

<u>Investment Type</u>	<u>Fair Value</u>	<u>Maturities</u>		
		<u>Less Than 1 Year</u>	<u>1-5 Years</u>	<u>Over 5 Years</u>
Government agencies	\$ 615,060	\$ 418,265	\$ 100,023	\$ 96,772
State and Local Government Securities	1,531,924	1,531,924		
Negotiable CDs	9,513,930	2,396,979	5,769,319	1,347,632
Money Market	762,791	762,791		
External investment pool	1,773,109	1,773,109		
Total investments	<u>\$ 14,196,814</u>	<u>\$ 6,883,068</u>	<u>\$ 5,869,342</u>	<u>\$ 1,444,404</u>

**Interest Rate Risk** – Interest rate risk is the risk that the market value of securities in the portfolio will fall because of changes in the general interest rate. The City's policy is to minimize interest rate risk by structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, thereby avoiding the need to sell securities on the open market prior to maturity.

**Credit Risk** – Generally, credit risk is the risk of loss because of failure of the security issuer or backer. Thus, designated depositories shall have insurance through the FDIC (Federal Deposit Insurance Corporation) or the SIPC (Securities Investor Protection Corporation). It is the City's policy to invest only in securities that meet the ratings requirements set by state statute. Furthermore, the City Council will approve all financial institutions, brokers, and advisers with which the City will do business. The Minnesota Money Market Mutual Fund ("4M Fund") is an external investment pool not registered with the Securities and Exchange Commission (SEC) that follows the same regulatory rules of the SEC under Rule 2a7. The 4M Fund is an unrated 2a7-like pool, and the fair value of the position of the pool is the same as the value of pool shares.

The following chart summarizes the ratings for the City's investments as rated by Standard and Poor's as of December 31, 2015

<u>Credit Rating</u>	<u>Fair Value</u>
AAA	1,061,174
Aaa	316,676
Not rated	12,818,964
Total	<u>\$ 14,196,814</u>

## CITY OF HERMANTOWN, MINNESOTA

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)

**NOTE 2 DEPOSITS AND 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. To ensure safety, it is the policy of the City that when considering an investment, all depositories under consideration be cross-checked against existing investments to make certain that funds in excess of insurance limits are not made in the same institution unless collateralized.

At December 31, 2015 the City had no investments in any one issuer that represents 5 percent or more of the City's investments (investments in external investment pools, mutual funds and US government securities are exempt).

The City's deposits and investments at December 31, 2015 consist of the following:

Cash on hand	\$ 700
Deposits	4,478,070
Investments	14,196,814
Total deposits and investments	<u>\$ 18,675,584</u>

**NOTE 3 RECEIVABLES**

Significant receivable balances not expected to be collected within one year of December 31, 2015 are as follows:

	<u>Governmental Activities</u>	<u>Business-type Activities</u>
Taxes receivable	\$ 130,139	\$
Special assessments	<u>5,713,115</u>	<u>187,152</u>
Total	<u>\$ 5,843,254</u>	<u>\$ 187,152</u>

## CITY OF HERMANTOWN, MINNESOTA

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)

**NOTE 4 CAPITAL ASSETS**

Capital assets activity for the year ended December 31, 2015 was as follows:

	Balance 12/31/2014	Additions	Deletions	Balance 12/31/2015
<b>Governmental activities</b>				
Capital assets not being depreciated				
Land	\$ 2,001,208	\$	\$	\$ 2,001,208
Construction in progress	606,118	205,854	(642,664)	169,308
Total capital assets not being depreciated	<u>2,607,326</u>	<u>205,854</u>	<u>(642,664)</u>	<u>2,170,516</u>
Capital assets being depreciated				
Land improvements	1,412,976			1,412,976
Buildings	11,645,734			11,645,734
Equipment and vehicles	2,285,610	88,719	(63,821)	2,310,508
Infrastructure	30,466,323	825,764		31,292,087
Total capital assets being depreciated	<u>45,810,643</u>	<u>914,483</u>	<u>(63,821)</u>	<u>46,661,305</u>
Less accumulated depreciation				
Land improvements	524,046	62,740		586,786
Buildings	4,006,845	309,180		4,316,025
Equipment and vehicles	1,417,864	145,626	63,821	1,499,669
Infrastructure	21,782,299	773,643		22,555,942
Total accumulated depreciation	<u>27,731,054</u>	<u>1,291,189</u>	<u>63,821</u>	<u>28,958,422</u>
Total capital assets being depreciated, net	<u>18,079,589</u>	<u>(376,706)</u>		<u>17,702,883</u>
Governmental activities capital assets, net	<u>\$ 20,686,915</u>	<u>\$ (170,852)</u>	<u>\$ (642,664)</u>	<u>\$ 19,873,399</u>

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 4      CAPITAL ASSETS (Continued)**

	Balance 12/31/2014	Additions	Deletions	Balance 12/31/2015
<b>Business-type activities</b>				
Capital assets not being depreciated				
Land and permanent easements	\$ 607,514	\$	\$	\$ 607,514
Capital assets being depreciated				
Buildings and Infrastructure	40,858,696			40,858,696
Equipment	1,037,657	19,486	(12,939)	1,044,204
Total capital assets being depreciated	41,896,353	19,486	(12,939)	41,902,900
Less accumulated depreciation				
Buildings and Infrastructure	7,100,708	614,554		7,715,262
Equipment	552,623	44,942	(12,939)	584,626
Total accumulated depreciation	7,653,331	659,496	(12,939)	8,299,888
Total capital assets being depreciated, net	34,243,022	(640,010)		33,603,012
Business-type activities capital assets, net	<u>\$ 34,850,536</u>	<u>\$ (640,010)</u>	<u>\$</u>	<u>\$ 34,210,526</u>

## CITY OF HERMANTOWN, MINNESOTA

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)

**NOTE 4 CAPITAL ASSETS (Continued)**

Depreciation expense was charged to functions/programs of the City as follows at December 31, 2015:

Governmental activities	
General government	\$ 159,808
Public safety	189,342
Public works	865,108
Community and economic development	1,003
Culture and recreation	<u>75,928</u>
Total governmental activities depreciation expense	<u>\$ 1,291,189</u>
Business-type activities	
Water utility	\$ 168,363
Sewage disposal	487,917
Street lighting	<u>3,216</u>
Total depreciation expense - Business type activities	<u>\$ 659,496</u>

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 5      LONG-TERM OBLIGATIONS**

The City had the following long-term obligations at December 31, 2015:

General Obligation Bonds

General Obligation Improvement and Utility Revenue Bonds, Series 2007B were issued at a par value of \$2,180,000, carry a net interest rate of 4.0 percent and mature in 2028.	\$ 1,615,000
General Obligation Improvement Bonds, Series 2009A were issued at a par value of \$5,515,000, carry a net interest rate of 3.48 percent and mature in 2030.	4,160,000
General Obligation Improvement Bonds, Series 2010A were issued at a par value of \$3,955,000, carry a net interest rate of 2.74 percent and mature in 2031.	3,070,000
General Obligation Improvement Refunding Bonds, Series 2012A were issued at a par value of \$2,500,000, carry a net interest rate of 1.94 percent and mature in 2026.	1,915,000
General Obligation Improvement Bonds, Series 2012B were issued at a par value of \$3,155,000, carry a net interest rate of 2.0 percent and mature in 2034.	3,020,000
General Obligation Improvement Bonds, Series 2014A were issued at a par value of \$2,170,000, carry a net interest rate of 2.0 percent and mature in 2028.	2,170,000
Total General Obligation Bonds	<u>\$ 15,950,000</u>

Revenue Bonds

Public Project Revenue Bonds, Series 2006A purchased December 5, 2006 by the Hermantown Economic Development Authority in the amount of \$9,630,000 at an interest rate of 4.0 percent and mature in 2027.	<u>\$ 6,895,000</u>
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Capital Lease Obligations

The City entered into a capital lease agreement on July 9, 2013 to finance the purchase of a lawn mower. The agreement calls for annual payments ranging from \$5,000 to \$9,907, including interest through July 9, 2017.	<u>\$ 18,558</u>
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CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 5 LONG-TERM OBLIGATIONS (Continued)**

Certificate of Indebtedness

Certificates of Indebtedness, Series 2014 issued at a par value of \$167,000, carry an interest rate of 2.07 percent, and mature in 2018.

\$ 120,003

The following is a summary of change in long-term obligations:

	Balance 12/31/2014 Restated	Additions	Reductions	Balance 12/31/2015	Amount Due Within One Year
<b>Governmental activities</b>					
Bonds payable					
General Obligation Bonds	\$ 17,965,000	\$ 2,015,000	\$ 2,015,000	\$ 15,950,000	\$ 1,280,000
Revenue Bonds	7,265,000		370,000	6,895,000	425,000
Capital lease	27,293		8,735	18,558	9,110
Certificate of indebtedness	186,023		66,020	120,003	47,318
Less deferred amounts					
Unamortized bond discount	(66,487)		(5,325)	(61,162)	(5,325)
Unamortized bond premium	173,087		11,626	161,461	11,626
Sub-total	25,549,916		2,466,056	23,083,860	1,767,729
Postemployment health care obligation	385,501	75,782	11,012	450,271	
Compensated absences	247,920	178,476	209,796	216,600	
Net pension liability	1,892,476	495,177	260,398	2,127,255	
<b>Total long term liabilities</b>	<u>\$ 28,075,813</u>	<u>\$ 749,435</u>	<u>\$ 2,947,262</u>	<u>\$ 25,877,986</u>	<u>\$ 1,767,729</u>
<b>Business-type activities</b>					
Compensated absences	\$ 70,613	\$ 29,943	\$ 37,711	\$ 62,845	
Net pension liability	181,510	34,974	19,498	196,986	
<b>Total long term liabilities</b>	<u>\$ 252,123</u>	<u>\$ 64,917</u>	<u>\$ 57,209</u>	<u>\$ 259,831</u>	<u>\$</u>

The annual requirements to amortize all outstanding obligations at December 31, 2015 are as follows:

	General Obligation Bonds		
	Principal	Interest	Total
2016	\$ 1,280,000	\$ 709,508	\$ 1,989,508
2017	1,220,000	663,464	1,883,464
2018	1,270,000	613,834	1,883,834
2019	1,285,000	561,192	1,846,192
2020	1,345,000	506,074	1,851,074
2021-2025	6,025,000	1,604,696	7,629,696
2026-2030	2,760,000	348,117	3,108,117
2031-2034	765,000	37,988	802,988
<b>Total</b>	<u>\$ 15,950,000</u>	<u>\$ 5,044,873</u>	<u>\$ 20,994,873</u>

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 5      LONG-TERM OBLIGATIONS (Continued)**

	Revenue Bonds		
	Principal	Interest	Total
2016	\$ 425,000	\$ 271,307	\$ 696,307
2017	475,000	253,307	728,307
2018	495,000	233,907	728,907
2019	515,000	213,707	728,707
2020	540,000	192,608	732,608
2021-2025	3,020,000	613,195	3,633,195
2026-2030	1,425,000	59,863	1,484,863
<b>Total</b>	<b>\$ 6,895,000</b>	<b>\$ 1,837,894</b>	<b>\$ 8,732,894</b>

	Capital Lease Obligations		
	Principal	Interest	Total
2016	\$ 9,110	\$ 797	\$ 9,907
2017	9,448	459	9,907
<b>Total</b>	<b>\$ 18,558</b>	<b>\$ 1,256</b>	<b>\$ 19,814</b>

	Certificate of Indebtedness		
	Principal	Interest	Total
2016	\$ 47,318	\$ 2,229	\$ 49,547
2017	48,297	1,250	49,547
2018	24,388	251	24,639
<b>Total</b>	<b>\$ 120,003</b>	<b>\$ 3,730</b>	<b>\$ 123,733</b>

General Obligation bonds, revenue bonds, and the certificate of indebtedness are paid from Debt Service Funds. The interest expense and fiscal fees paid in 2015 for all bonds and certificate of indebtedness totaled \$748,196.

Compensated absences and postemployment health care obligations are paid from the General Fund. Net pension liability is paid from the General Fund, Water Utility Fund and Sewage Disposal Fund.

## CITY OF HERMANTOWN, MINNESOTA

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)

**NOTE 6 CONDUIT DEBT OBLIGATIONS**

The Hermantown Economic Development Authority (HEDA) has issued revenue bonds for the purpose of providing capital financing to various entities. Even though the debt bears HEDA's name, HEDA is not responsible for the payment of the original debt. The debt is secured by the payments agreed to be paid by these entities under the terms of the agreement between HEDA and the entity. The general description of the transactions and the outstanding balance as of December 31, 2015, are as follows:

<u>Enterprises</u>	<u>Year of Issue</u>	<u>Outstanding Balance 12/31/2015</u>
Marshall School 2004B	2004	\$ 478,194
Saints-Hilltoppers Arena Project 2010	2010	549,535
Marshall School 2011	2011	<u>314,923</u>
Total Outstanding		<u>\$ 1,342,652</u>

**NOTE 7 INTERFUND TRANSACTIONS**

The composition of interfund balances as of December 31, 2015, is as follows:

Due to/from balances are caused by either timing differences or the elimination of negative cash balances within the various funds. All interfund balances are expected to be repaid within one year.

Due to/from Other Funds

	<u>Due From</u>	<u>Due To</u>
Governmental Funds		
General Fund	\$ 706,419	\$
Other Governmental funds:		
Cable Television Fund		21,445
Soccer Fund		14,519
Certificate of Indebtedness fund		38,658
G.O. Utility Revenue Refunding Bonds, Series 2007A fund		177,077
G.O. Improvement bonds, Series 2012A Fund		231,700
Municipal State Aid Streets Fund		167,894
TIF District #1 Improvements Fund		13,295
Arrowhead Regional Health and Wellness Fund		41,831
Total	<u>\$ 706,419</u>	<u>\$ 706,419</u>

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 7 INTERFUND TRANSACTIONS (Continued)**

Advances to/from Other Funds

	<u>Advance To</u>	<u>Advance From</u>
Governmental Funds		
General Fund	\$ 117,107	\$
Other Governmental Funds		
Cable Television Fund	150,000	
TIF District #1 Improvements Fund		700,000
HEDA Fleet Projects Fund		117,107
Total Governmental Funds	<u>267,107</u>	<u>817,107</u>
Proprietary Funds		
Street Lighting Fund	<u>550,000</u>	
Total	<u>\$ 817,107</u>	<u>\$ 817,107</u>

Advances were made from to fund various ongoing projects. The advance bears interest at 4 percent. There is no due date for repayment.

Interfund transfers

Transfers are indicative of funding for capital projects, lease payments or debt service, subsidies of various City operations and re-allocations of special revenues. The following schedule briefly summarizes the City's transfer activity:

In the year ended December 31, 2015, the City made the following one-time transfers, which are included in the amounts presented above:

	<u>Transfer In</u>	<u>Transfer Out</u>
Governmental Funds		
General Fund	\$ 76,000	\$ 386,500
City Sales Tax Fund		1,354,861
G.O. Improvement & Utility Revenue		
Bonds, Series 2007B Fund	95,874	
G.O. Improvement Bonds, Series 2009A Fund	146,691	
G.O. Improvement Bonds, Series 2010A Fund	289,030	
G.O. Improvement Bonds, Series 2012B Fund	59,665	
Other Funds		
Police Liaison Education Fund	15,000	
Public Project Revenue Bonds		
Series 2006A Fund	660,008	
G.O. Utility Revenue Refunding Bonds		
Series 2007A Fund	180,439	
G.O. Improvement Bonds, Series 2012A Fund	191,476	
Special Assessment Deficiency Fund		194,763
General Capital Projects Fund	370,000	
Municipal Building Reserve Fund		36,000
Special Assessment Projects Fund		2,500
Total Governmental Funds	<u>2,084,183</u>	<u>1,974,624</u>

## CITY OF HERMANTOWN, MINNESOTA

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)

**NOTE 7 INTERFUND TRANSACTIONS (Continued)**

	<u>Transfer In</u>	<u>Transfer Out</u>
Proprietary Funds		
Water Utility Fund	1,500	48,903
Sewage Disposal Fund		59,656
Street Lighting Fund		2,500
Total Proprietary Funds	<u>1,500</u>	<u>111,059</u>
 Total	 <u>\$ 2,085,683</u>	 <u>\$ 2,085,683</u>

**NOTE 8 FUND BALANCE/NET POSITION**

Fund balance was nonspendable for the following purposes at December 31, 2015:

Prepaid Items	
General Fund	\$ 90,447
City Sales Tax Fund	108
Other Governmental Funds	
Cable Television Fund	<u>74</u>
	<u>\$ 90,629</u>

Governmental net position and fund balances were restricted for the following purposes at December 31, 2015:

	<u>Net Position</u>	<u>Fund Balance</u>
City Sales Tax Fund		
Debt service	\$ 4,059,868	\$ 4,059,868
G.O. Improvement & Utility Revenue Bonds		
Series 2007B Fund		
Debt service	1,260,735	80,273
G.O. Improvement Bonds Series 2009A		
Debt service	1,418,202	256,315
G.O. Improvement Bonds Series 2010A		
Debt service	1,327,790	330,560
G.O. Improvement Bonds Series 2012B		
Debt service	3,109,181	1,153,155
Other Governmental Funds		
Police programs	41,006	41,006
Park improvements	208,530	208,530
Debt service	<u>2,303,181</u>	<u>2,282,381</u>
 Total restricted	 <u>\$ 13,728,493</u>	 <u>\$ 8,412,088</u>

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 8 FUND BALANCE/NET POSITION (Continued)**

Fund balances were committed for the following purposes at December 31, 2015:

General Fund	
Community development infrastructure	\$ 106,586
Other Governmental Funds	
Economic development	73,841
Park improvements	90,691
Wetland restoration	84,391
Cable TV	309,523
Debt service	<u>611,760</u>
Total committed	<u>\$ 1,276,792</u>

Fund balances were assigned for the following purposes at December 31, 2015:

Other Governmental Funds	
Police liaison/DARE	\$ 41,945
Municipal buildings	724,731
Capital projects	<u>5,519</u>
Total assigned	<u>\$ 772,195</u>

The following funds had an unassigned fund balance deficit at December 31, 2015:

Other Governmental Funds	
Soccer Fund	\$ 14,519
Certificate of Indebtedness Fund	37,944
G.O. Utility Revenue Refunding Bonds, Series 2007A Fund	176,672
G.O. Improvement Bonds, Series 2012A Fund	229,769
Municipal State Aid Streets fund	2,242
TIF District 1 Improvement Fund	714,438
HEDA Fleet Project Fund	<u>117,464</u>
	<u>\$ 1,293,048</u>

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 9      DEFINED BENEFIT PENSION PLANS**

**Public Employee Retirement Association (PERA)**

**A. Plan Description**

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

1. General Employees Retirement Fund (GERF)

All full-time and certain part-time employees of the City are covered by the General Employees Retirement Fund (GERF). GERF members belong to either the Coordinated Plan or the Basic Plan. Coordinated Plan members are covered by Social Security and Basic Plan members are not. The Basic Plan was closed to new members in 1967. All new members must participate in the Coordinated Plan.

2. Public Employees Police and Fire Fund (PEPFF)

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

**Benefits Provided**

PERA provides retirement, disability, and death benefits. Benefit provisions are established by state statute and can only be modified by the state legislature.

Benefit increases are provided to benefit recipients each January. Increases are related to the funding ratio of the plan. Members in plans that are at least 90% funded for two consecutive years are given 2.5% increases. Members in plans that have not exceeded 90% funded, or have fallen below 80%, are given 1% increases.

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

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 9      DEFINED BENEFIT PENSION PLANS (Continued)**

1. GERF Benefits

Benefits are based on a member's highest average salary for any five successive years of allowable service, age, and years of credit at termination of service. Two methods are used to compute benefits for PERA's Coordinated and Basic Plan members. The retiring member receives 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% of average salary for each of the first 10 years of service and 2.7% for each remaining year. The annuity accrual for a Coordinated Plan member is 1.2% of average salary for each of the first 10 years and 1.7% for each remaining year. Under Method 2, the annuity accrual rate is 2.7% of average salary for Basic Plan members and 1.7% for Coordinated Plan members for each year of service. For members hired prior to July 1, 1989, a full annuity is available when age plus years of service equal 90 and normal retirement age is 65. For members hired on or after July 1, 1989, normal retirement age is the age for unreduced Social Security benefits capped by 66. Disability benefits are available for vested members, and are based upon years of service and average high-five salary.

2. PEPFF Benefits

Benefits for the PEPFF members first hired after June 30, 2010, but before July 1, 2014, vest on a prorated basis from 50% after five years up to 100% after ten years of credited service. Benefits for PEPFF members first hired after June 30, 2014, vest on a prorated basis from 50% after ten years up to 100% after twenty years of credited service. The annuity accrual rate is 3% of average salary for each year of service. For PEPFF who were first hired prior to July 1, 1989, a full annuity is available when age plus years of service equal at least 90.

**B. Contributions**

Minnesota Statutes Chapter 353 sets the rates for employer and employee contributions. These statutes are established and amended by the state legislature.

1. GERF Contributions

Basic Plan members and Coordinated Plan members were required to contribute 9.1% and 6.5%, respectively, of their annual covered salary in calendar year 2015. The City was required to contribute 11.78% of pay for Basic Plan members and 7.5% for Coordinated Plan members in calendar year 2015. The City's contributions to the GERF for the year ended December 31, 2015 were \$81,908. The City's contribution was equal to the contractually required contribution as set by state statute.

2. PEPFF Contributions

Plan members were required to contribute 10.8% of their annual covered salary in calendar year 2015. The City was required to contribute 16.20% of pay for PEPFF members in 2015. The City's contributions to the PEPFF for the year ended December 31, 2015 were \$185,428. The City's contributions were equal to the required contribution as set by state statute.

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 9      DEFINED BENEFIT PENSION PLANS (Continued)**

**C. Pension Costs**

1. GERF Pension Costs

At December 31, 2015, the City reported a liability of \$938,036 for its proportionate share of GERF's net pension liability. The net pension liability was measured as of June 30, 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The City's proportion of the net pension liability was based on the City's contributions received by PERA during the measurement period for employer payroll paid dates from July 1, 2014, through June 30, 2015, relative to the total employer contributions received from all of PERA's participating employers. At June 30, 2015, the City's proportion was 0.0181%.

For the year ended December 31, 2015, the City recognized pension expense of \$84,528 for its proportionate share of GERF's pension expense.

At December 31, 2015, the City reported its proportionate share of the GERF's deferred outflows of resources and deferred inflows of resources from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Differences between expected and actual economic experience	\$	\$ 47,293
Net difference between projected and actual investment earnings on plan investments	88,800	
Changes in proportion		14,092
Contributions paid to PERA subsequent to the measurement date	40,378	
<b>Total</b>	<u>\$ 129,178</u>	<u>\$ 61,385</u>

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 9      DEFINED BENEFIT PENSION PLANS (Continued)**

\$40,378 reported as deferred outflows of resources related to pensions resulting from City contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2016. Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

<u>Year ended December 31,</u>	<u>Pension Expense Amount</u>
2016	\$     42,117
2017	1,739
2018	1,737
2019	22,200
2020	0

2. PEPFF Pension Costs

At December 31, 2015, the City reported a liability of \$1,386,205 for its proportionate share of PEPFF's net pension liability. The net pension liability was measured as of June 30, 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The City's proportion of the net pension liability was based on the City's contributions received by PERA during the measurement period for employer payroll paid dates from July 1, 2014, through June 30, 2015, relative to the total employer contributions received from all of PERA's participating employers. At June 30, 2015, the City's proportion was 0.122%.

For the year ended December 31, 2015, the City recognized pension expense of \$134,260 for its proportionate share of PEPFF's pension expense. The City also recognized \$10,980 for the year ended December 31, 2015, as pension expense (and grant revenue) for its proportionate share of the State of Minnesota's on-behalf contributions to PEPFF. Legislation passed in 2013 required the State of Minnesota to begin contribution 59 million to the PEPFF each year, starting in fiscal year 2014.

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 9      DEFINED BENEFIT PENSION PLANS (Continued)**

At December 31, 2015, the City reported its proportionate share of the PEPFF's deferred outflows of resources and deferred inflows of resources from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Differences between expected and actual economic experience	\$	\$ 224,797
Changes in proportion	108,004	
Net difference between projected and actual investment earnings on plan investments	241,523	
Contributions paid to PERA subsequent to the measurement date	93,090	
Total	<u>\$ 442,617</u>	<u>\$ 224,797</u>

\$93,090 reported as deferred outflows of resources related to pensions resulting from City contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2016. Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

<u>Year ended December 31,</u>	<u>Pension Expense Amount</u>
2016	\$ 114,540
2017	21,450
2018	21,450
2019	60,380
2020	0

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 9      DEFINED BENEFIT PENSION PLANS (Continued)**

**D. Actuarial Assumptions**

The total pension liability in the June 30, 2015, actuarial valuation was determined using the entry age normal actuarial cost method and the following actuarial assumptions:

Inflation	2.75% per year
Active Member Payroll Growth	3.50% per year
Investment Rate of Return	7.90%

Salary increases were based on a service-related table. Mortality rates for active members, retirees, survivors and disabilitants were based on RP-2000 tables for males or females, as appropriate, with slight adjustments. Benefit increases for retirees are assumed to be 1% effective every January 1<sup>st</sup> through 2026 and 2.5% thereafter.

Actuarial assumptions used in the June 30, 2015, valuation were based on the results of actuarial experience studies. The experience study in the GERP was for the period July 1, 2004, through June 30, 2008, with an update of economic assumptions in 2014. Experience studies have not been prepared for PERA's other plans, but assumptions are reviewed annually.

There were no changes in actuarial assumptions in 2015.

The long-term expected rate of return on pension plan investments is 7.9%. The State Board of Investment, which manages the investments of PERA, prepares an analysis of the reasonableness of the long-term expected rate of return on a regular basis using a building-block method in which best-estimates ranges of expected future rates of return are developed for each major asset class. These ranges are combined to produce an expected long-term rate of return by weighting the expected future rates of return by the target asset allocation percentages. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
Domestic Stocks	45%	5.50%
International Stocks	15%	6.00%
Bonds	18%	1.45%
Alternative Assets	20%	6.40%
Cash	2%	0.50%
Total	<u>100%</u>	

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 9      DEFINED BENEFIT PENSION PLANS (Continued)**

**E. Discount Rate**

The discount rate used to measure the total pension liability was 7.9%. The projection of cash flows used to determine the discount rate assumed that employee and employer contributions will be made at the rates specified in statute. Based on these assumptions, each of the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

**F. Pension Liability Sensitivity**

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

Discount Rate	<u>1% Decrease in Discount Rate</u> 6.90%	<u>Discount Rate</u> 7.90%	<u>1% Increase in Discount Rate</u> 8.90%
City's proportionate share of the GERF net pension liability	\$ 1,474,926	\$ 938,036	\$ 494,647
City's proportionate share of the PEPFF net pension liability	\$ 2,701,729	\$ 1,386,205	\$ 299,354

**G. Pension Plan Fiduciary Net Position**

Detailed information about GERF's fiduciary net position is available in a separately-issued PERA financial report. That report can be obtained at [www.mnpera.org](http://www.mnpera.org); by writing to PERA at 60 Empire Drive #200, St. Paul, Minnesota, 55103-2088; or by calling (651)296-7460 or 1-800-652-9026.

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 10      DEFINED CONTRIBUTION PLAN**

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

Plan benefits depend solely on amounts contributed to the plan plus investment earnings, less administrative expenses. Minnesota Statutes, Chapter 353D.03, specifies plan provisions, including the employee and employer contribution rates for those qualified personnel who elect to participate. An eligible elected official who decides to participate contributes 5% of salary which is matched by the elected official's employer. For ambulance service personnel, employer contributions are determined by the employer, and for salaried employees must be a fixed percentage of salary. Employer contributions for volunteer personnel may be a unit value for each call or period of alert duty. Employees who are paid for their services may elect to make member contributions in an amount not to exceed the employer share. Employer and employee contributions are combined and used to purchase share in one or more of the seven accounts of the Minnesota Supplemental Investment Fund. For administering the plan, PERA receives 2% of employer contributions and twenty-five hundredths of 1% (.0025) of the assets in each member's account annually.

Total contributions made by the City during 2015 were:

Contribution amount		Percentage of covered payroll		Required
Employee	Employer	Employee	Employer	Rates
\$ 1,610	\$ 1,610	5%	5%	5%

**NOTE 11      POSTEMPLOYMENT HEALTH CARE PLAN**

Plan Description

The City administers a single-employer defined benefit plan OPEB plan with allows retired employees to remain on the City's plan after severing employment from the City (implicit rate subsidy) at the retiree's expense. The plan does not issue a stand alone financial report.

Funding

Employer contribution requirements are established and may be amended as set forth in the applicable employment and bargaining unit agreements. The plan is finance on a pay-as-you-go basis.

Annual OPEB Cost and Net OPEB Obligation

The City of Hermantown's annual other postemployment benefit (OPEB) cost (expense) is calculated based on the *annual required contribution of the employer (ARC)*, an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years.

CITY OF HERMANTOWN, MINNESOTA  
 NOTES TO FINANCIAL STATEMENTS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

**NOTE 11      POSTEMPLOYMENT HEALTH CARE PLAN (Continued)**

The following table shows the components of the City of Hermantown's annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the City's net OPEB obligation as of December 31, 2015:

Annual required contribution (ARC)	\$ 82,655
Interest on net OPEB obligation	15,420
Adjustment to ARC (amortization of NOO)	<u>(22,293)</u>
Annual OPEB cost	<u>75,782</u>
 City contributions	 <u>(11,012)</u>
 Increase in OPEB obligation	 64,770
 Net OPEB obligation, December 31, 2014	 <u>385,501</u>
 Net OPEB obligation, December 31, 2015	 <u><u>\$ 450,271</u></u>

The City of Hermantown's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for were as follows:

Year ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
2013	61,124	23.00%	322,286
2014	73,459	13.95%	385,501
2015	75,782	14.53%	450,271

Funded Status and Funding Progress

As of January 1, 2014, the most recent actuarial valuation date, the plan was 100 percent unfunded. The actuarial value of plan assets and the funded ratio are both \$0. The actuarial accrued liability and the unfunded actuarial accrued liability (UAAL) for benefits were \$510,985. The covered payroll (annual payroll of active employees covered by the plan) was \$2,002,313, and the ratio of the UAAL to the covered payroll is 25.52 percent.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the health care cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

CITY OF HERMANTOWN, MINNESOTA  
NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)

**NOTE 11      POSTEMPLOYMENT HEALTH CARE PLAN (Continued)**

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood between the employer and plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the January 1, 2014, actuarial valuation, the projective unit credit cost method was used. The actuarial assumptions included a discount rate of 4-percent and health care trend rates ranging from 7.5 percent initially, reduced by decrements to an ultimate rate of 5 percent to eight years. The rates included a 3 percent inflation assumption. The UAAL is being amortized as a level dollar amount over 30 years on an open period. The benefits are not based on salary; therefore, no assumption was made regarding salary increases.

**NOTE 12      FIRE RELIEF ASSOCIATION**

Plan Description

Firefighters of the Hermantown Volunteer Fire Department, Inc., a Minnesota Corporation, are members of a defined benefit pension plan administered by the Hermantown Fire Fighters Relief Association (Association). The plan is a single-employer pension plan available to members operating under the provisions of Minnesota Statute Section 69.772, as amended. The plan is governed by a six-member board of trustees elected by the members of the Association for one year terms. Two City Council members and the Fire Chief are ex officio, nonvoting members of the board of trustees.

Benefit Provisions

Each member who is at least 50 years of age, has retired from the Fire Department, has served at least 10 years of active service with the Fire Department before retirement and has been a member of the Association in good standing at least 10 years prior to retirement, is entitled to a lump-sum pension on retirement in the amount of \$3,800 for each year of active service. According to the bylaws of the Association, a member who retires with less than 20 years of service is eligible for a reduced service pension. If a member of the Association becomes permanently and totally disabled the member will receive the sum of \$3,800 for each year or partial year the member was an active member.

## CITY OF HERMANTOWN, MINNESOTA

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)

**NOTE 12 FIRE RELIEF ASSOCIATION (Continued)**Funding Policy

Plan members are not required to contribute to the plan. The City is required by state statute to contribute the amount certified annually to the Office of the State Auditor. The State of Minnesota provides specific aids used to fund the pension as well. The City's required contribution for the year ended December 31, 2015 was \$0. The City's actual contributions for the years ended December 31, 2015, 2014 and 2013, were \$28,275, \$28,138, and \$27,900, respectively.

The Association issues a financial report that includes financial statements and required supplemental information. That report may be obtained from Hermantown Fire Department Relief Association, 5111 Maple Grove Road, Hermantown, Minnesota 55811.

**NOTE 13 COMPENSATED ABSENCES**

It is the City's policy to permit employees to accumulate earned but unused vacation and sick pay benefits. Upon retirement, in accordance with various employment and union contracts, the value of the qualifying banked sick hours will be submitted as a Health Care Savings Plan (HCSP) contribution to the Minnesota State Retirement System (MSRS) to be used to pay the employee's health insurance premiums. The year-end accrued sick leave and accrued vacation balance decreased by \$7,770 in the proprietary funds and by \$31,320 in the governmental funds. As of December 31, 2015, eleven employees were vested for sick leave. The present value of future benefits is recorded as compensated absences in the statement of net position at December 31, 2015, in the amount of \$279,443. Any employee who is at the maximum accumulation of sick leave and who is credited for sick leave during a year in excess of the maximum sick leave shall, as of December 31 of the year in question, have 20 percent of such excess credit towards sick leave deposited in the State of Minnesota Health Care Savings Plan at the employees December 31 wage rate of the year in question. The City paid \$1,664 to the MSRS for this employee benefit in 2015.

**NOTE 14 LEASES**

In October 2011, a lease extension agreement was made between HEDA and Independent School District No. 700 to extend the term of the Lease from February 2, 2012 to June 30, 2017 ("Initial Extension Term"). The Lease term shall automatically be renewed for additional one-year term(s) ("Extension Term") unless either party advises the other party six months prior to the end of any term of such party's determination to terminate the term of the lease at the end of their term. This is a noncancelable lease, and the School District is using the building for its Early Childhood Education Program.

Future payments to be received under the lease are as follows:

<u>Year End</u>	<u>Amount</u>
2016	\$ 1,000
2017	1,000
Total	<u>\$ 2,000</u>

## CITY OF HERMANTOWN, MINNESOTA

NOTES TO FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2015  
(Continued)**NOTE 15 CONTINGENCIES AND COMMITMENTS**

The City entered into construction contracts for various projects during the year. The City's commitment under those contracts for future work totaled \$32,900 at December 31, 2015.

Amounts received or receivable from grantor agencies are subject to audit and adjustment by grantor agencies, principally the federal government. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount, if any, of expenditures that may be disallowed by the grantor cannot be determined at this time, although the City expects such amounts, if any, to be immaterial.

**NOTE 16 RISK MANAGEMENT**

The City purchases commercial insurance coverage through the League of Minnesota Cities Insurance Trust with other cities in the state, which is a public entity risk pool, currently operating as a common risk management and insurance program. The City pays an annual premium to the League for its insurance coverage. The League of Minnesota Cities Insurance Trust is self-sustaining, through commercial companies, for excess claims. The City is covered through the pool for any claims incurred but unreported, but retains risk for the deductible portion of its insurance policies. The amount of these deductibles is considered immaterial to the financial statements.

There were no significant reductions in insurance coverage from coverage in the prior year, and there were no insurance claims or settlements exceeding insurance coverage in the past three years.

**NOTE 17 FUTURE ACCOUNTING STANDARDS**

Government Accounting Standards Board (GASB) Statement No. 75, Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions, is effective for the City for the year ended December 31, 2018. This statement replaces the requirements of GASB 45, Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions. This statement establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources and expense/expenditures, and identifies the methods and assumptions that are required to be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. The City has not completed the process of evaluating GASB Statement No. 75, but implementation is expected to impact the City's recognition of OPEB liabilities and expense/expenditures.

**REQUIRED SUPPLEMENTARY INFORMATION**

CITY OF HERMANTOWN, MINNESOTA  
 INFORMATION ABOUT THE CITY'S OTHER POSTEMPLOYMENT  
 HEALTH CARE PLAN  
 FOR THE YEAR ENDED DECEMBER 31, 2015

Schedule of Funding Progress by Valuation Date

<u>Actuarial Valuation Date</u>	<u>Value of assets</u>	<u>Actuarial Accrued Liability Projected Unit Credit</u>	<u>Unfunded Actuarial Accrued Liability</u>	<u>Funded Ratio</u>	<u>Covered Payroll</u>	<u>Unfunded Actuarial Accrued Liability as a percentage of covered payroll</u>
January 1, 2008	\$ 0	\$ 652,164	652,164	0%	\$ 1,795,951	36.31%
January 1, 2011	0	521,682	521,682	0%	1,670,124	31.24%
January 1, 2014	0	510,985	510,985	0%	2,002,313	25.52%

Schedule of Employer Contributions

<u>Year Ended December 31,</u>	<u>Annual Required Contributions</u>	<u>Percentage Contributed</u>
2008	76,872	23.72%
2009	75,827	26.45%
2010	81,448	15.76%
2011	57,436	20.32%
2012	59,267	21.70%
2013	61,124	23.00%
2014	73,459	13.95%
2015	75,782	14.53%

CITY OF HERMANTOWN, MINNESOTA  
 INFORMATION ABOUT THE CITY'S NET PENSION LIABILITY  
 FOR THE YEAR ENDED DECEMBER 31, 2015

Schedule of Employer's Share of Net Pension Liability

**GERF**

<b>Source</b>	<b>2015</b>
City's proportion of the net pension liability	.0181%
City's proportionate share of the net pension liability	\$ 938,036
District's covered-employee payroll	\$ 1,062,157
District's proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll	88.3%
Plan fiduciary net position as a percentage of the total pension liability	78.2%

**PEPFF**

<b>Source</b>	<b>2015</b>
City's proportion of the net pension liability	0.122%
City's proportionate share of the net pension liability	\$ 1,386,205
City's covered-employee payroll	\$ 1,111,297
City's proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll	124.7%
Plan fiduciary net position as a percentage of the total pension liability	86.6%

CITY OF HERMANTOWN, MINNESOTA  
 INFORMATION ABOUT THE CITY'S NET PENSION LIABILITY  
 FOR THE YEAR ENDED DECEMBER 31, 2015

Schedule of Employer's Contributions

**GERF**

<b>Source</b>	<b>2015</b>
Statutorily required contribution	\$ 81,908
Contributions in relation to the statutorily required contribution	\$ 81,908
Contribution deficiency (excess)	\$ 0
City's covered-employee payroll	\$ 1,092,079
Contributions as a percentage of covered-employee payroll	7.50%

**PEPFF**

<b>Source</b>	<b>2015</b>
Statutorily required contribution	\$ 185,428
Contributions in relation to the statutorily required contribution	\$ 185,428
Contribution deficiency (excess)	\$ 0
City's covered-employee payroll	\$ 1,144,614
Contributions as a percentage of covered-employee payroll	16.20%

**SUPPLEMENTARY INFORMATION**

## CITY OF HERMANTOWN, MINNESOTA

COMBINING BALANCE SHEET  
OTHER GOVERNMENTAL FUNDS  
DECEMBER 31, 2015

	Special Revenue Funds						
	Hermantown Economic Development Authority Fund	Park Dedication Fund	Hermantown Wetland Mitigation Fund	Police Liaison Education Fund	Police Program Fund	Cable Television Fund	
<b>Assets</b>							
Cash and cash equivalents	\$ 73,745	\$ 303,703	\$ 84,391	\$ 41,945	\$ 39,622	\$ 161,062	\$
Accounts receivable					1,384	20,734	75,961
Interest receivable		518					
Delinquent taxes receivable	441						
Special assessments receivable							
Prepaid items						74	
Advance to other funds						150,000	
<b>Total assets</b>	<u>74,186</u>	<u>304,221</u>	<u>84,391</u>	<u>41,945</u>	<u>41,006</u>	<u>331,870</u>	<u>75,961</u>
<b>Deferred outflows of resources</b>							
<b>Total assets and deferred outflows of resources</b>	<u>\$ 74,186</u>	<u>\$ 304,221</u>	<u>\$ 84,391</u>	<u>\$ 41,945</u>	<u>\$ 41,006</u>	<u>\$ 331,870</u>	<u>\$ 75,961</u>
<b>Liabilities</b>							
Accrued wages and related liabilities	\$	\$	\$	\$	\$	\$ 203	\$
Accounts payable	345					625	
Due to other funds						21,445	14,519
Deposits payable		5,000					
Advance to other funds							
Unearned revenue							75,961
<b>Total liabilities</b>	<u>345</u>	<u>5,000</u>				<u>22,273</u>	<u>90,480</u>
<b>Deferred inflows of resources</b>							
Delinquent property tax							
Unavailable special assessments							
<b>Total deferred inflow of resources</b>							
<b>Fund balance (deficit)</b>							
Nonspendable						74	
Restricted		208,530			41,006		
Committed	73,841	90,691	84,391			309,523	
Assigned				41,945			
Unassigned (deficit)							(14,519)
<b>Total fund balance (deficit)</b>	<u>73,841</u>	<u>299,221</u>	<u>84,391</u>	<u>41,945</u>	<u>41,006</u>	<u>309,597</u>	<u>(14,519)</u>
<b>Total liabilities, deferred inflows of resources, and fund balance (deficit)</b>	<u>\$ 74,186</u>	<u>\$ 304,221</u>	<u>\$ 84,391</u>	<u>\$ 41,945</u>	<u>\$ 41,006</u>	<u>\$ 331,870</u>	<u>\$ 75,961</u>

## CITY OF HERMANTOWN, MINNESOTA

COMBINING BALANCE SHEET  
OTHER GOVERNMENTAL FUNDS  
DECEMBER 31, 2015  
(Continued)

	Debt Service Funds					Special Assessment Deficiency Fund
	Certificate of Indebtedness Fund	Public Project Revenue Bonds Series 2006A Fund	General Obligation Utility Revenue Refunding Bonds Series 2007A Fund	General Obligation Improvement Bonds Series 2012A Fund	General Obligation Improvement Bonds Series 2014A Fund	
<b>Assets</b>						
Cash and cash equivalents	\$	\$ 760,906	\$	\$	\$ 1,521,475	\$ 609,612
Accounts receivable						
Interest receivable						
Delinquent taxes receivable	3,359		405	2,151		
Special assessments receivable			215,621	539,757		673,594
Prepaid items						
Advance to other funds						
<b>Total assets</b>	<u>3,359</u>	<u>760,906</u>	<u>216,026</u>	<u>541,908</u>	<u>1,521,475</u>	<u>1,283,206</u>
<b>Deferred outflows of resources</b>						
<b>Total assets and deferred outflows of resources</b>	<u>\$ 3,359</u>	<u>\$ 760,906</u>	<u>\$ 216,026</u>	<u>\$ 541,908</u>	<u>\$ 1,521,475</u>	<u>\$ 1,283,206</u>
<b>Liabilities</b>						
Accrued wages and related liabilities	\$	\$	\$	\$	\$	\$
Accounts payable						
Due to other funds	38,658		177,077	231,700		
Deposits payable						
Advance to other funds						
Unearned revenue						
<b>Total liabilities</b>	<u>38,658</u>		<u>177,077</u>	<u>231,700</u>		
<b>Deferred inflows of resources</b>						
Delinquent property tax	2,645			220		
Unavailable special assessments			215,621	539,757		671,446
<b>Total deferred inflow of resources</b>	<u>2,645</u>		<u>215,621</u>	<u>539,977</u>		<u>671,446</u>
<b>Fund balance (deficit)</b>						
Nonspendable						
Restricted		760,906			1,521,475	
Committed						611,760
Assigned						
Unassigned (deficit)	(37,944)		(176,672)	(229,769)		
<b>Total fund balances</b>	<u>(37,944)</u>	<u>760,906</u>	<u>(176,672)</u>	<u>(229,769)</u>	<u>1,521,475</u>	<u>611,760</u>
<b>Total liabilities, deferred inflows of resources, and fund balance (deficit)</b>	<u>\$ 3,359</u>	<u>\$ 760,906</u>	<u>\$ 216,026</u>	<u>\$ 541,908</u>	<u>\$ 1,521,475</u>	<u>\$ 1,283,206</u>

## CITY OF HERMANTOWN, MINNESOTA

COMBINING BALANCE SHEET  
OTHER GOVERNMENTAL FUNDS  
DECEMBER 31, 2015  
(Continued)

	Capital Project Funds						Total Other Governmental Funds
	General Capital Projects Fund	Municipal Building Reserve Fund	Municipal State Aid Streets Fund	TIF District 1 Improvement Fund	HEDA Fleet Projects Fund	Special Assessment Projects Fund	
<b>Assets</b>							
Cash and cash equivalents	\$ 423,128	\$ 301,603	\$	\$	\$	\$ 1,700	\$ 4,322,892
Accounts receivable			167,894				313,559
Interest receivable							518
Delinquent taxes receivable							6,356
Special assessments receivable							1,428,972
Prepaid items							74
Advance to other funds							150,000
<b>Total assets</b>	<u>423,128</u>	<u>301,603</u>	<u>167,894</u>			<u>1,700</u>	<u>6,222,371</u>
<b>Deferred outflows of resources</b>							
<b>Total assets and deferred outflows of resources</b>	<u>\$ 423,128</u>	<u>\$ 301,603</u>	<u>\$ 167,894</u>	<u>\$</u>	<u>\$</u>	<u>\$ 1,700</u>	<u>\$ 6,222,371</u>
<b>Liabilities</b>							
Accrued wages and related liabilities	\$	\$	\$	\$	\$	\$	\$ 203
Accounts payable			2,242	1,143	357		6,648
Due to other funds			167,894	13,295		41,831	706,419
Deposits payable							5,000
Advance to other funds				700,000	117,107		817,107
Unearned revenue							75,961
<b>Total liabilities</b>			<u>170,136</u>	<u>714,438</u>	<u>117,464</u>		<u>1,611,338</u>
<b>Deferred inflows of resources</b>							
Delinquent property tax							2,865
Unavailable special assessments							1,426,824
<b>Total deferred inflow of resources</b>							<u>1,429,689</u>
<b>Fund balance (deficit)</b>							
Nonspendable							74
Restricted							2,531,917
Committed							1,170,206
Assigned	423,128	301,603				1,700	772,195
Unassigned (deficit)			(2,242)	(714,438)	(117,464)		(1,293,048)
<b>Total fund balances</b>	<u>423,128</u>	<u>301,603</u>	<u>(2,242)</u>	<u>(714,438)</u>	<u>(117,464)</u>	<u>1,700</u>	<u>3,181,344</u>
<b>Total liabilities, deferred inflows of resources, and fund balance (deficit)</b>	<u>\$ 423,128</u>	<u>\$ 301,603</u>	<u>\$ 167,894</u>	<u>\$</u>	<u>\$</u>	<u>\$ 1,700</u>	<u>\$ 6,222,371</u>

## CITY OF HERMANTOWN, MINNESOTA

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

	Special Revenue Funds						
	Hermantown Economic Development Authority Fund	Park Dedication Fund	Hermantown Wetland Mitigation Fund	Police Liaison Education Fund	Police Program Fund	Cable Television Fund	Soccer Fund
Revenues							
Taxes	\$ 39,790	\$	\$	\$	\$	\$ 41,804	\$
Special Assessments							
Licenses and permits		62,625					
Intergovernmental							
Charges for services				64,576			
Fines and forfeitures				2,340	10,754		
Investment income	48	3,888	79	77	10	7,895	
Miscellaneous	3,770	13,534	11,909	4,862	12,332		27,884
Total revenues	<u>43,608</u>	<u>80,047</u>	<u>11,988</u>	<u>71,855</u>	<u>23,096</u>	<u>49,699</u>	<u>27,884</u>
Expenditures							
Current							
Public safety				81,315	4,170		
Community and economic development	28,132		2,400				
Culture and recreation						19,424	
Capital outlay						1,510	
Debt service							
Principal							
Interest and fiscal charges							
Total expenditures	<u>28,132</u>	<u></u>	<u>2,400</u>	<u>81,315</u>	<u>4,170</u>	<u>20,934</u>	<u></u>
Excess (deficiency) of revenues over expenditures	<u>15,476</u>	<u>80,047</u>	<u>9,588</u>	<u>(9,460)</u>	<u>18,926</u>	<u>28,765</u>	<u>27,884</u>
Other financing sources (uses)							
Transfer in				15,000			
Transfer out							
Net other financing sources (uses)				<u>15,000</u>			
Net change in fund balance	15,476	80,047	9,588	5,540	18,926	28,765	27,884
Fund balance (deficit), beginning, restated	58,365	219,174	74,803	36,405	22,080	280,832	(42,403)
Fund balance (deficit), ending	<u>\$ 73,841</u>	<u>\$ 299,221</u>	<u>\$ 84,391</u>	<u>\$ 41,945</u>	<u>\$ 41,006</u>	<u>\$ 309,597</u>	<u>\$ (14,519)</u>

## CITY OF HERMANTOWN, MINNESOTA

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

	Debt Service Funds					Special Assessment Deficiency Fund
	Certificate of Indebtedness Fund	Public Project Revenue Bonds Series 2006A Fund	General Obligation Utility Revenue Refunding Bonds Series 2007A Fund	General Obligation Improvement Bonds Series 2012A Fund	General Obligation Improvement Bonds Series 2014A Fund	
Revenues						
Taxes	\$	\$	\$	\$	\$	\$
Special assessments			28,199	94,227		29,962
Licenses and permits						
Intergovernmental						
Charges for services						
Fines and forfeitures						
Investment income					1,588	2,853
Miscellaneous						
Total revenues	<u>        </u>	<u>        </u>	<u>28,199</u>	<u>94,227</u>	<u>1,588</u>	<u>32,815</u>
Expenditures						
Current						
Public safety						
Community and economic development						
Culture and recreation						
Capital outlay						
Debt service						
Principal	66,020	370,000	175,000	250,000	770,000	
Interest and fiscal charges	2,525	289,901	18,621	34,079	34,246	
Total expenditures	<u>68,545</u>	<u>659,901</u>	<u>193,621</u>	<u>284,079</u>	<u>804,246</u>	
Excess (deficiency) of revenues over expenditures	<u>(68,545)</u>	<u>(659,901)</u>	<u>(165,422)</u>	<u>(189,852)</u>	<u>(802,658)</u>	<u>32,815</u>
Other financing sources (uses)						
Transfer in		660,008	180,439	191,476		
Transfer out						(194,763)
Net other financing sources (uses)		<u>660,008</u>	<u>180,439</u>	<u>191,476</u>		<u>(194,763)</u>
Net change in fund balance	(68,545)	107	15,017	1,624	(802,658)	(161,948)
Fund balance (deficit), beginning, restated	30,601	760,799	(191,689)	(231,393)	2,324,133	773,708
Fund balance (deficit), ending	<u>\$ (37,944)</u>	<u>\$ 760,906</u>	<u>\$ (176,672)</u>	<u>\$ (229,769)</u>	<u>\$ 1,521,475</u>	<u>\$ 611,760</u>

CITY OF HERMANTOWN, MINNESOTA  
 COMBINING STATEMENT OF REVENUES, EXPENDITURES,  
 AND CHANGES IN FUND BALANCES  
 OTHER GOVERNMENTAL FUNDS  
 FOR THE YEAR ENDED DECEMBER 31, 2015  
 (Continued)

	Capital Project Funds							Total Other Governmental Funds
	General Capital Projects Fund	Municipal Building Reserve Fund	Municipal State Aid Streets Fund	TIF District 1 Improvement Fund	HEDA Fleet Projects Fund	Special Assessment Projects Fund	Arrowhead Regional Health and Wellness Center Fund	
<b>Revenues</b>								
Taxes	\$	\$	\$	\$	\$	\$	\$	\$ 81,594
Special assessments								152,388
Licenses and permits								62,625
Intergovernmental			132,492				156,077	288,569
Charges for services								64,576
Fines and forfeitures								13,094
Investment income								16,438
Miscellaneous						4,200		78,491
Total revenues			132,492			4,200	156,077	757,775
<b>Expenditures</b>								
Current								
Public safety								85,485
Community and economic development				73,768	113,402		152,258	369,960
Culture and recreation								19,424
Capital outlay			172,488	14,553				188,551
Debt service								
Principal								1,631,020
Interest and fiscal charges				20,000				399,372
Total expenditures			172,488	108,321	113,402		152,258	2,693,812
Excess (deficiency) of revenues over expenditures			(39,996)	(108,321)	(113,402)	4,200	3,819	(1,936,037)
<b>Other financing sources (uses)</b>								
Transfer in	370,000							1,416,923
Transfer out		(36,000)				(2,500)		(233,263)
Net other financing sources (uses)	370,000	(36,000)				(2,500)		1,183,660
Net change in fund balance	370,000	(36,000)	(39,996)	(108,321)	(113,402)	1,700	3,819	(752,377)
Fund balance (deficit), beginning, restated	53,128	337,603	37,754	(606,117)	(4,062)			3,933,721
Fund balance (deficit), ending	\$ 423,128	\$ 301,603	\$ (2,242)	\$ (714,438)	\$ (117,464)	\$ 1,700	\$ 3,819	\$ 3,181,344

**OTHER REPORTS**



## **Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters**

To the Honorable City Council  
City of Hermantown  
Hermantown, Minnesota

We have audited in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hermantown, Minnesota ("City"), as of and for the year ended December 31, 2015, and the related notes to the financial statements, which collectively comprise the City's basic financial statements and have issued our report thereon dated April 14, 2016.

### **Internal Control over Financial Reporting**

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

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

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 entity's financial statements will not be prevented or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and questioned costs as items 2015-001 to be a material weakness.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

**City's Response to Findings**

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

**Purpose of this Report**

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



Wipfli LLP

April 14, 2016  
Duluth, Minnesota



## Independent Auditor's Report on Legal Compliance for the State of Minnesota

To the Honorable City Council  
City of Hermantown  
Hermantown, Minnesota

We have audited, in accordance with auditing standards generally accepted in the United States, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hermantown, Minnesota (City), as of and for the year ended December 31, 2015, and the related notes to the financial statements, and have issued our report thereon dated April 14, 2016.

The *Minnesota Legal Compliance Audit Guide for Cities*, promulgated by the State Auditor pursuant to Minnesota Statutes Sec. 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.

In connection with our audit, nothing came to our attention that caused us to believe that the City failed to comply with the provisions of the *Minnesota Legal Compliance Audit Guide for Cities*, except as described in the Schedule of Findings and Responses as items 2015-002 and 2015-003. However, our audit was not directed primarily towards 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 purpose of this report is solely to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in cursive script that reads "Wipfli LLP".

Wipfli LLP

April 14, 2016  
Duluth, Minnesota

CITY OF HERMANTOWN, MINNESOTA  
 SCHEDULE OF FINDINGS AND RESPONSES  
 FOR THE YEAR ENDED DECEMBER 31, 2015

**Financial Statement Findings**

The City is responsible for establishing and maintaining internal control. This responsibility includes the internal control over the various accounting cycles, the fair presentation of the financial statements and related notes, and the accuracy and completeness of all financial records and related information. The existence of significant deficiencies or material weaknesses may be known to management and may represent a conscious decision by management or those charged with governance to accept that degree of risk because of cost or other considerations. Management is responsible for making decisions concerning costs and the related benefits. The auditors are responsible for communicating significant deficiencies and material weaknesses, regardless of management's decisions.

**A. Material Weaknesses in Internal Control**

**Item 2015-001 - Significant Audit Adjustments**

**Condition** - The City is responsible for controls over the period-end financial reporting process, including controls over procedures used to enter transaction totals into the general ledger; initiate, record, and process journal entries into the general ledger; and record recurring and nonrecurring adjustments to the financial statements. During our audit, we proposed material adjustments to convert the City's financial records to the financial statements as reported.

**Criteria** - Controls should be in place to ensure accurate financial reporting.

**Cause** - The City's controls over period-end financial reporting did not prevent or detect misstatements of the financial statements.

**Effect** - Without controls over procedures that will detect or prevent a misstatement when entering transactions or making adjustment to the financial statements, the financial statements may be misstated.

**City's response** - The City will review the current internal control procedures and make adjustments as needed. Between those adjustments and more personnel stability in the accounting department the City will strive to prevent future misstatements.

**Legal Compliance Findings**

**2015-002** Minn. Stat. 118A.03 requires depositories of municipal funds to pledge securities as collateral for deposits that exceed federal depository insurance coverage (FDIC). The market value of the collateral pledged must exceed 110% of the uninsured deposits. We tested the last day of each month during the fiscal year. We found insufficient insurance and collateral one day at one financial institution.

**City's response** - The City will monitors collateral pledged by each financial institution to ensure that the City's deposits are fully insured and collateralized.

**2015-003** MSA 475.61 requires the City to levy an amount such that it, together with estimated collections of special assessments and other revenues pledged for the payment of the obligations, will produce at least five percent in excess of the amount needed to meet the principal and interest payments of long-term debt when due. The City did not levy a sufficient amount on the 2015 tax levy to produce at least five percent in excess of the amount needed to meet the principal and interest payments due.

**City's response** - There was an error in the amount certified to the County in 2014 for collection in 2015. The City understands the requirement to levy a sufficient amount to produce at least five percent in excess of the amount needed to meet the principal and interest payments due and will levy the proper amount in future years.

## CITY OF HERMANTOWN, MINNESOTA

SCHEDULE OF PRIOR YEAR FINDINGS AND RESPONSES  
FOR THE YEAR ENDED DECEMBER 31, 2015**Financial Statement Findings****Significant Deficiency in Internal Control**

**Item 2014-001 - Significant Audit Adjustments** – A material weakness for significant audit adjustments was reported in 2015 as item 2015-001.