Management Report

for

City of Saint Peter, Minnesota

December 31, 2016

THIS PAGE INTENTIONALLY LEFT BLANK

CERTIFIED PUBLIC ACCOUNTANTS

**PRINCIPALS**
Thomas A. Karnowski, CPA
Paul A. Radosevich, CPA
William J. Lauer, CPA
James H. Eichten, CPA
Aaron J. Nielsen, CPA
Victoria L. Holinka, CPA/CMA

To the City Council and Management
City of Saint Peter, Minnesota

We have prepared this management report in conjunction with our audit of the City of Saint Peter, Minnesota's (the City) financial statements for the year ended December 31, 2016. We have organized this report into the following sections:

- Audit Summary
- Governmental Funds Overview
- Enterprise Funds Overview
- Debt Service
- Government-Wide Financial Statements
- Legislative Updates
- Accounting and Auditing Updates

We would be pleased to further discuss any of the information contained in this report or any other concerns that you would like us to address. We would also like to express our thanks for the courtesy and assistance extended to us during the course of our audit.

The purpose of this report is solely to provide those charged with governance of the City, management, and those who have responsibility for oversight of the financial reporting process comments resulting from our audit process and information relevant to city finances in Minnesota. Accordingly, this report is not suitable for any other purpose.

Malloy, Montague, Karnowski, Radosevich & Co., P.A.

Minneapolis, Minnesota
June 28, 2017

Malloy, Montague, Karnowski, Radosevich & Co., P.A.
5353 Wayzata Boulevard • Suite 410 • Minneapolis, MN 55416 • Phone: 952-545-0424 • Fax: 952-545-0569 • www.mmkr.com

THIS PAGE INTENTIONALLY LEFT BLANK

## AUDIT SUMMARY

The following is a summary of our audit work, key conclusions, and other information that we consider important or that is required to be communicated to the City Council, administration, or those charged with governance of the City.

### OUR RESPONSIBILITY UNDER AUDITING STANDARDS GENERALLY ACCEPTED IN THE UNITED STATES OF AMERICA AND *GOVERNMENT AUDITING STANDARDS*

We have audited the financial statements of the governmental activities, the business-type activities, the discretely presented component units, each major fund, and the aggregate remaining fund information of the City as of and for the year ended December 31, 2016, and the related notes to basic financial statements. Professional standards require that we provide you with information about our responsibilities under auditing standards generally accepted in the United States of America and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. We have communicated such information to you verbally and in our audit engagement letter. Professional standards also require that we communicate the following information related to our audit.

### AUDITOR'S RESPONSIBILITY FOR COMPONENT UNITS

Our responsibility is to express opinions on the City's financial statements based on our audit. We did not audit the discretely presented component units' financial statements. This includes the financial statements of the River's Edge Hospital and Clinic and the financial statements of the Housing and Redevelopment Authority. Those statements were audited by other auditors whose reports have been furnished to us. Our opinion on the basic financial statements, insofar as it relates to the amounts included for these organizations as component units of the City, is based solely on the reports of the other auditors.

### PLANNED SCOPE AND TIMING OF THE AUDIT

We performed the audit according to the planned scope and timing previously discussed and coordinated in order to obtain sufficient audit evidence and complete an effective audit.

### AUDIT OPINION AND FINDINGS

Based on our audit of the City's financial statements for the year ended December 31, 2016:

- We issued the following opinions on the City's basic financial statements:

| Opinion Unit | Type of Opinion |
|---|---|
| Governmental activities | Qualified |
| Business-type activities | Unmodified |
| Discretely presented component units | Unmodified |
| General Fund | Unmodified |
| Capital Projects – Permanent Improvement Fund | Unmodified |
| Capital Projects – Parkland Dedication Fund | Unmodified |
| Capital Projects – Traverse Green TIF District Fund | Unmodified |
| Each major enterprise fund | Unmodified |
| Aggregate remaining fund information | Unmodified |

**Basis for Qualified Opinion on Governmental Activities**

Management has not adopted the standards for pension plans within Governmental Accounting Standards Board (GASB) Statement No. 68 related to the Saint Peter Fire Relief Association Pension Plan. Accounting principles generally accepted in the United States of America require the reporting of a net pension liability related to the plan, which would change the deferred outflows of resources, liabilities, deferred inflows of resources, net position, and expenses of the governmental activities of the City. The amount by which this departure would affect the deferred outflows of resources, liabilities, deferred inflows of resources, net position, and expenses of the governmental activities has not been determined.

- We reported one finding related to our testing of internal controls over financial reporting.

  1. We reported that due to the small number of office staff, the City has a limited segregation of duties in several areas, which we consider a significant deficiency in internal controls.

- The results of our testing disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards.*

- We reported two findings based on our testing of the City's compliance with Minnesota laws and regulations.

  1. When contracting for construction services with a value exceeding $100,000, the City is required to obtain performance and payment bonds from the contractor. For one such contract awarded during the year, the City did not receive performance or payment bonds from the contractor.

  2. Minnesota Statutes require two weeks published notice of the request for bids in the City's official newspaper. For one of the two bids selected for testing, the City was unable to provide documentation that the bid advertisement was published as required.

## FOLLOW-UP ON PRIOR YEAR FINDINGS AND RECOMMENDATIONS

As part of our audit of the City's financial statements for the year ended December 31, 2016, we performed procedures to follow-up on the findings and recommendations that resulted from our prior year audit. We reported the following finding that was corrected by the City in the current year:

- Minnesota Statutes require cities to pay each vendor obligation according to the terms of each contract or within 35 days after the receipt of the goods or services or the invoice for the goods or services. For 2 of 40 disbursements selected for testing in the prior year, the City did not pay the obligation within the required time period, and did not pay interest on the unpaid obligation. No such late disbursements were noted in the current year.

## SIGNIFICANT ACCOUNTING POLICIES

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the City are described in Note 1 of the notes to basic financial statements.

No new accounting policies were adopted and the application of existing policies was not changed during the year ended December 31, 2016. We noted no transactions entered into by the City during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

## ACCOUNTING ESTIMATES AND MANAGEMENT JUDGMENTS

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were:

- **Depreciation** – Management's estimates of depreciation expense are based on the estimated useful lives of the assets.

- **Self-Insurance Reserves** – Management's estimates of costs for unreported claims are based on the past history of claims reported.

- **Compensated Absences** – Management's estimate based on current rates of pay and sick leave balances.

- **Net Pension Liability** – The City has recorded a liability and activity for pension benefits. This obligation is calculated using actuarial methodologies described in GASB Statement No. 68. These actuarial calculations include significant assumptions, including projected changes, healthcare insurance costs, investment returns, retirement ages, proportionate share, and employee turnover.

- **Allowance for Doubtful Accounts** – Management's estimate of the allowance for doubtful accounts is based on historical water and sewer revenues, historical loss levels, and an analysis of the collectability of individual accounts.

We evaluated the key factors and assumptions used by management in the areas discussed above in determining that they are reasonable in relation to the financial statements taken as a whole.

The financial statement disclosures are neutral, consistent, and clear.

## CORRECTED AND UNCORRECTED MISSTATEMENTS

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management.

We proposed two uncorrected audit adjustments to the financial statements. The adjustments are as follows:

- Net other post-employment benefit (OPEB) liability of $13,730.

- Federal Insurance Contributions Act liability on the related compensated absences liability of $67,404.

Management has determined that the effects of the uncorrected adjustments are immaterial, both individually and in the aggregate, to the financial statements taken as a whole. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to each opinion unit's financial statements taken as a whole.

## DIFFICULTIES ENCOUNTERED IN PERFORMING THE AUDIT

We encountered no significant difficulties in dealing with management in performing and completing our audit.

## DISAGREEMENTS WITH MANAGEMENT

For purposes of this report, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

## MANAGEMENT REPRESENTATIONS

We have requested certain representations from management that are included in the management representation letter dated June 28, 2017.

## MANAGEMENT CONSULTATIONS WITH OTHER INDEPENDENT ACCOUNTANTS

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the City's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

## OTHER AUDIT FINDINGS OR ISSUES

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the City's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

## OTHER MATTERS

We applied certain limited procedures to the management's discussion and analysis and the pension-related required supplementary information (RSI) that supplements the basic financial statements. Our procedures consisted of inquiries of management regarding 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 did not audit the RSI and do not express an opinion or provide any assurance on the RSI.

We were engaged to report on the supplemental information accompanying the financial statements, which is not RSI. With respect to this supplementary information, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

We were not engaged to report on the introductory and other information sections which accompany the financial statements but are not RSI. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statement and, accordingly, we do not express an opinion or provide any assurance on it.

## GOVERNMENTAL FUNDS OVERVIEW

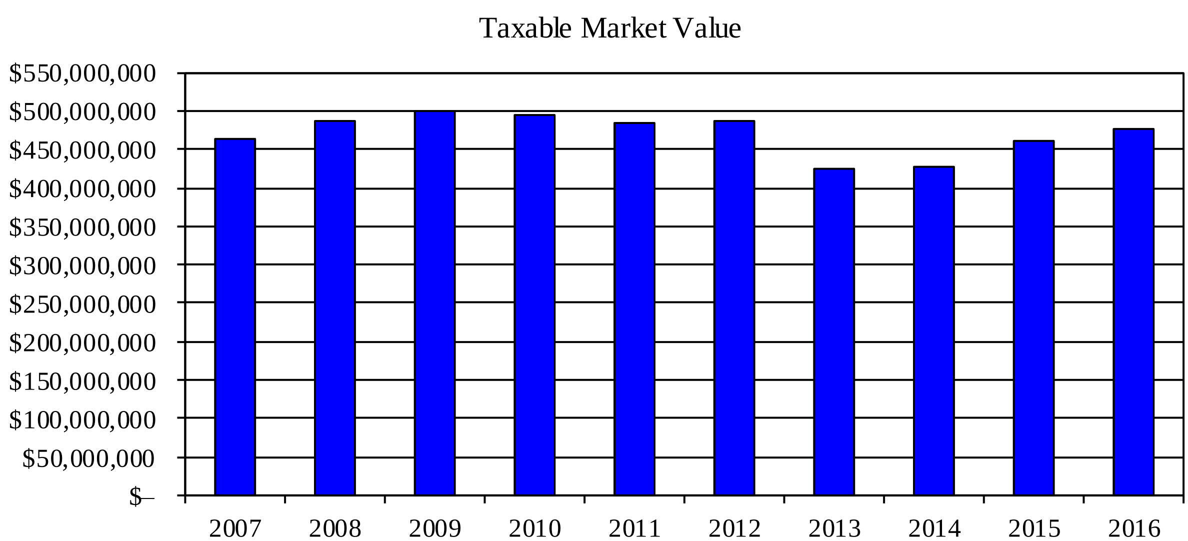
This section of the report provides you with an overview of the financial trends and activities of the City's governmental funds, which includes the General, special revenue, debt service, and capital project funds. These funds are used to account for the basic services the City provides to all of its citizens, which are financed primarily with property taxes. The governmental fund information in the City's financial statements focuses on budgetary compliance and the sufficiency of each governmental fund's current assets to finance its current liabilities.

### PROPERTY TAXES

Minnesota cities rely heavily on local property tax levies to support their governmental fund activities. For the 2015 fiscal year, local ad valorem property tax levies provided 39.8 percent of the total governmental fund revenues for cities over 2,500 in population, and 35.6 percent for cities under 2,500 in population. Property tax levies certified by Minnesota cities for 2016 increased about 4.8 percent over 2015, compared to an increase of 4.0 percent the prior year.

The total market value of property in Minnesota cities increased about 5.7 percent for the 2016 levy year. While the percentage of market value growth was less than the 8.5 percent increase for levy year 2015, it was considerably larger than the 1.1 percent growth experienced in levy year 2014. Market values increased across all property categories for 2016, with gains in the market values of nonhomestead residential properties (9.1 percent) and other properties (7.3 percent) outpacing the market value gain of residential homestead properties (5.0 percent), commercial/industrial properties (4.9 percent), and farms (0.1 percent). The market values used for levying property taxes are based on the previous fiscal year (e.g., market values for taxes levied in 2016 were based on assessed values as of January 1, 2015), so the trend of change in these market values lags somewhat behind the housing market and economy in general.

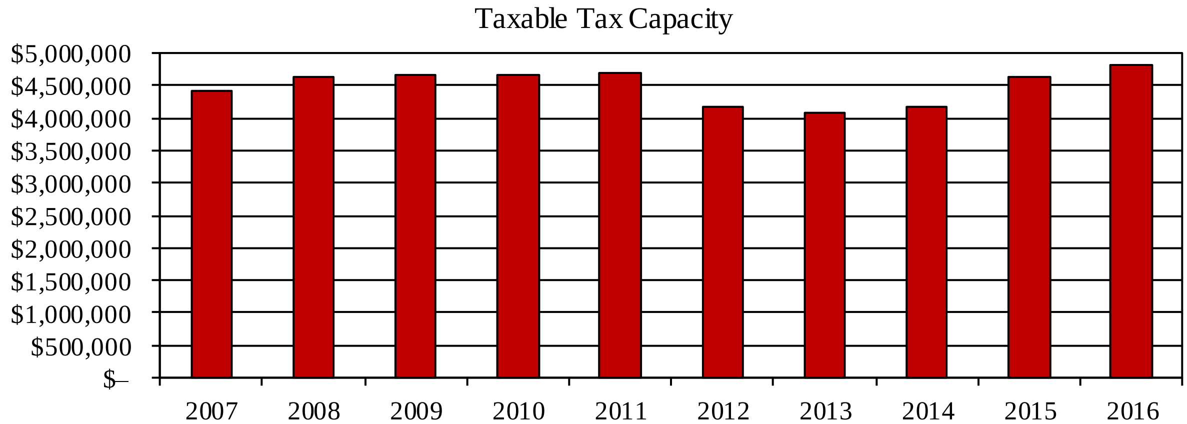
The City's taxable market value increased 7.6 percent for taxes payable in 2015 and increased 3.4 percent for taxes payable in 2016. The following graph shows the City's changes in taxable market value over the past 10 years:




The data in this graph does not include the drop in taxable market value as a result of the legislative change to the Market Value Homestead Credit (MVHC) Program in fiscal 2012.

Tax capacity is considered the actual base available for taxation. It is calculated by applying the state's property classification system to each property's market value. Each property classification, such as commercial or residential, has a different calculation and uses different rates. Consequently, a city's total tax capacity will change at a different rate than its total market value, as tax capacity is affected by the proportion of the City's tax base that is in each property classification from year-to-year, as well as legislative changes to tax rates. The City's tax capacity increased 11.1 percent and 4.2 percent for taxes payable in 2015 and 2016, respectively.

The following graph shows the City's change in tax capacities over the past 10 years:




Some of the increase in the taxable tax capacity in 2015 is related to the decertification of tax increments by the City.

The significant drop in taxable tax capacity is the result of the legislative change to the MVHC Program in fiscal 2012.

The "city" portion of the average state-wide tax rates for 2016 showed small decreases from the prior year, as levy increases were offset by improvements in property tax capacities. The following table presents the average tax rates applied to city residents for each of the last two levy years, along with comparative state-wide rates:

Rates expressed as a percentage of net tax capacity

| | All Cities State-Wide | | City of Saint Peter | |
|---|---|---|---|---|
| | 2015 | 2016 | 2015 | 2016 |
| **Average tax rate** | | | | |
| City | 46.9 | 46.5 | 46.8 | 47.3 |
| County | 44.7 | 44.1 | 49.4 | 52.6 |
| School | 27.1 | 27.5 | 17.0 | 36.6 |
| Special taxing | 6.9 | 6.9 | 0.5 | 0.5 |
| Total | 125.6 | 125.0 | 113.7 | 137.0 |

The City's portion of the average property tax rate for city residents was similar to state-wide averages in 2016.

## GOVERNMENTAL FUNDS REVENUE

The following table presents the per capita revenue of the City's governmental funds for the past three years, along with state-wide averages.

We have included the most recent comparative state-wide averages available from the Office of the State Auditor to provide a benchmark for interpreting the City's data. The amounts received from the typical major sources of governmental fund revenue will naturally vary between cities based on factors such as a city's stage of development, location, size and density of its population, property values, services it provides, and other attributes. It will also differ from year-to-year due to the effect of inflation and changes in its operation. Also, certain data on these tables may be classified differently than how they appear in the City's financial statements in order to be more comparable to the state-wide information, particularly in separating capital expenditures from current expenditures.

We have designed this section of our management report using per capita data in order to better identify unique or unusual trends and activities of your city. We intend for this type of comparative and trend information to complement, rather than duplicate, information in the management's discussion and analysis. An inherent difficulty in presenting per capita information is the accuracy of the population count, which for most years is based on estimates.

**Governmental Funds Revenue per Capita**
With State-Wide Averages by Population Class

| | State-Wide | | | City of Saint Peter | | |
|---|---|---|---|---|---|---|
| Year | December 31, 2015 | | | 2014 | 2015 | 2016 |
| Population | 2,500–10,000 | 10,000–20,000 | 20,000–100,000 | 11,758 | 11,784 | 11,784 |
| Property taxes | $ 443 | $ 414 | $ 443 | $ 198 | $ 186 | $ 195 |
| Tax increments | 26 | 33 | 37 | 58 | 59 | 61 |
| Franchise and other taxes | 33 | 42 | 39 | 12 | 12 | 12 |
| Special assessments | 59 | 52 | 59 | 43 | 3 | 3 |
| Licenses and permits | 31 | 31 | 43 | 27 | 21 | 36 |
| Intergovernmental revenues | 285 | 322 | 156 | 437 | 324 | 354 |
| Charges for services | 110 | 85 | 94 | 40 | 40 | 46 |
| Other | 69 | 62 | 58 | 84 | 92 | 112 |
| Total revenue | $ 1,056 | $ 1,041 | $ 929 | $ 898 | $ 735 | $ 818 |

The City's lower than average tax revenue is primarily the result of the City relying on enterprise fund activities to finance the City's activities. This is due to the large amount of nontaxable property within the City.

In 2016, governmental funds revenue per capita increased $83 per capita. The largest increase was in intergovernmental revenues, which increased mainly as a result of a one-time grant received in 2016.

It is important to note that this table does not include operating transfers, which are used by the City to support governmental fund activities. This information is not included in the table as the comparable information is not available.

## GOVERNMENTAL FUNDS EXPENDITURES

The expenditures of governmental funds will also vary from state-wide averages and from year-to-year, based on the City's circumstances. Expenditures are classified into three types as follows:

- **Current** – These are typically the general operating type expenditures occurring on an annual basis, and are primarily funded by general sources such as taxes and intergovernmental revenues.

- **Capital Outlay and Construction** – These expenditures do not occur on a consistent basis, more typically fluctuating significantly from year-to-year. Many of these expenditures are project-oriented, and are often funded by specific sources that have benefited from the expenditure, such as special assessment improvement projects.

- **Debt Service** – Although the expenditures for debt service may be relatively consistent over the term of the respective debt, the funding source is the important factor. Some debt may be repaid through specific sources such as special assessments or redevelopment funding, while other debt may be repaid with general property taxes.

The City's expenditures per capita of its governmental funds for the past three years, together with state-wide averages, are presented in the following table:

**Governmental Funds Expenditures per Capita**
With State-Wide Averages by Population Class

| | State-Wide | | | City of Saint Peter | | |
|---|---|---|---|---|---|---|
| Year | December 31, 2015 | | | 2014 | 2015 | 2016 |
| Population | 2,500–10,000 | 10,000–20,000 | 20,000–100,000 | 11,758 | 11,784 | 11,784 |
| Current | | | | | | |
| General government | $ 134 | $ 109 | $ 89 | $ 101 | $ 111 | $ 111 |
| Public safety | 255 | 244 | 261 | 222 | 222 | 234 |
| Street maintenance and lighting | 119 | 117 | 99 | 106 | 109 | 117 |
| Parks and recreation | 88 | 108 | 94 | 132 | 135 | 139 |
| All other | 64 | 70 | 89 | 63 | 107 | 90 |
| | $ 660 | $ 648 | $ 632 | $ 624 | $ 684 | $ 691 |
| Capital outlay and construction | $ 372 | $ 389 | $ 286 | $ 420 | $ 51 | $ 487 |
| Debt service | | | | | | |
| Principal | $ 181 | $ 178 | $ 117 | $ 87 | $ 116 | $ 121 |
| Interest and fiscal | 51 | 40 | 33 | 29 | 28 | 25 |
| | $ 232 | $ 218 | $ 150 | $ 116 | $ 144 | $ 146 |

The City's current governmental funds current per capita expenditures increased by $7 per capita in fiscal 2016. Increases in public safety and street maintenance and lighting expenditures were offset by decreases in miscellaneous revenue received.

## GOVERNMENTAL FUND BALANCES

The following table summarizes the changes in the fund balances of the City's governmental funds during the year ended December 31, 2016, presented both by fund balance classification and by fund:

**Governmental Funds Change in Fund Balance**

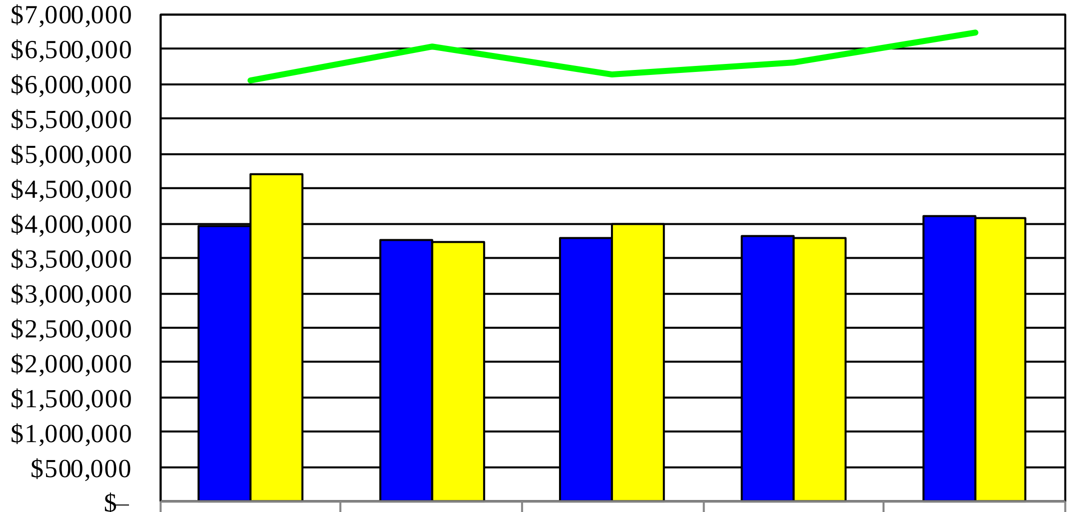
| | Fund Balance as of December 31, 2015 | Fund Balance as of December 31, 2016 | Increase (Decrease) |
|---|---|---|---|
| Fund balances of governmental funds | | | |
| Total by classification | | | |
| Nonspendable | $ 3,499 | $ 17,625 | $ 14,126 |
| Restricted | 5,310,945 | 4,467,374 | (843,571) |
| Committed | 1,091,452 | 1,076,717 | (14,735) |
| Assigned | 321,737 | 449,041 | 127,304 |
| Unassigned | 3,292,446 | 2,519,558 | (772,888) |
| Total governmental funds | $ 10,020,079 | $ 8,530,315 | $ (1,489,764) |
| Total by fund | | | |
| General | $ 3,824,821 | $ 4,103,391 | $ 278,570 |
| Capital Projects – Permanent Improvement | 1,432,967 | 1,475,888 | 42,921 |
| Capital Projects – Parkland Dedication | 927,560 | (911,729) | (1,839,289) |
| Capital Projects – Traverse Green TIF District | (3,398) | 155,795 | 159,193 |
| Nonmajor | 3,838,129 | 3,706,970 | (131,159) |
| Total governmental funds | $ 10,020,079 | $ 8,530,315 | $ (1,489,764) |

In total, the fund balances of the City's governmental funds decreased by $1,489,764 during the year ended December 31, 2016. The majority of this decrease was in the Capital Projects – Parkland Dedication Fund totaling $1,839,289, due to park construction costs incurred in 2016.

**GENERAL FUND**

The City's General Fund accounts for the financial activity of the basic services provided to the community. The primary services included within this fund are the administration of the municipal operation, police and fire protection, building inspection, street and highway maintenance, parks and recreation, and economic development. The graph below illustrates the change in the General Fund financial position over the last five years. We have also included a line representing annual expenditures to reflect the change in the size of the General Fund operation over the same period.

General Fund Financial Position
Year Ended December 31,




| | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|
| Fund Balance | $3,963,763 | $3,746,297 | $3,775,595 | $3,824,821 | $4,103,391 |
| Net Cash Balance | $4,696,521 | $3,731,502 | $3,982,254 | $3,794,828 | $4,089,794 |
| Expenditures | $6,048,566 | $6,546,358 | $6,149,467 | $6,313,124 | $6,737,933 |

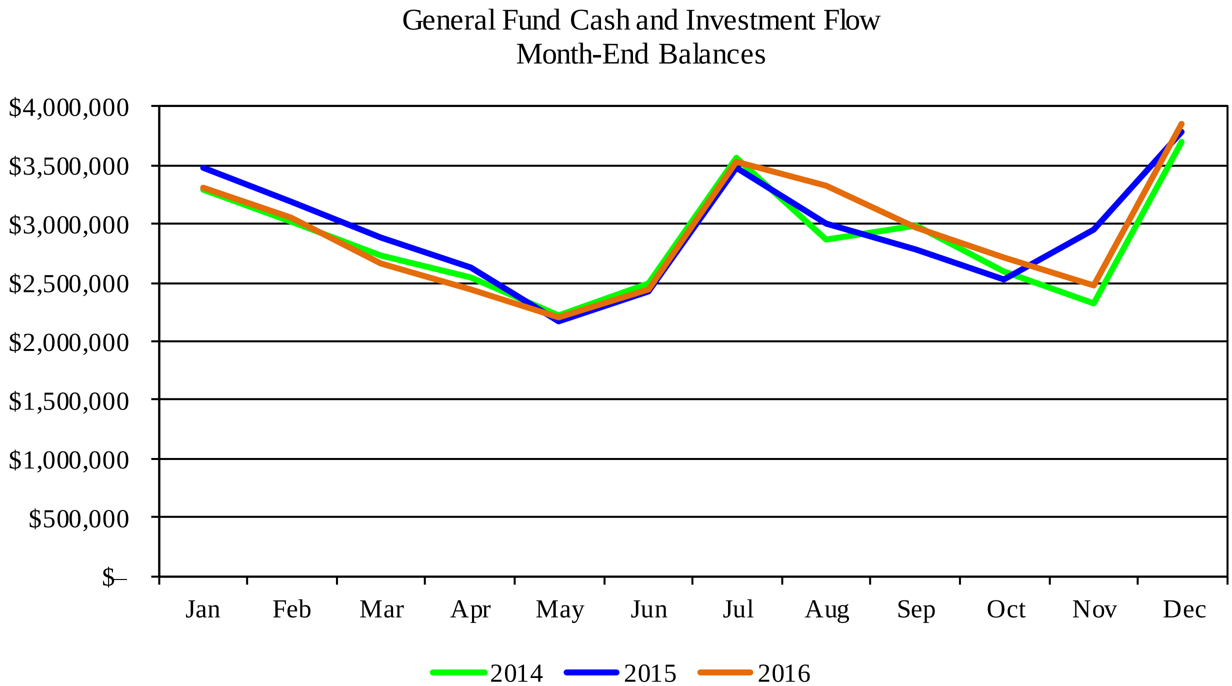
The City's General Fund cash and investment balance and fund balance increased in the current year. The total fund balance at December 31, 2016 was $4,103,391, an increase of $278,570, which was less than the budgeted increase of $498,083.

As the graph illustrates, the City has generally been able to maintain healthy cash and fund balance levels as the volume of financial activity has grown. This is an important factor because a government, like any organization, requires a certain amount of equity to operate. A healthy financial position allows the City to avoid volatility in tax rates; helps minimize the impact of state funding changes; allows for the adequate and consistent funding of services, repairs, and unexpected costs; and is a factor in determining the City's bond rating and resulting interest costs. Maintaining an adequate fund balance has become increasingly important given the fluctuations in state funding for cities in recent years.

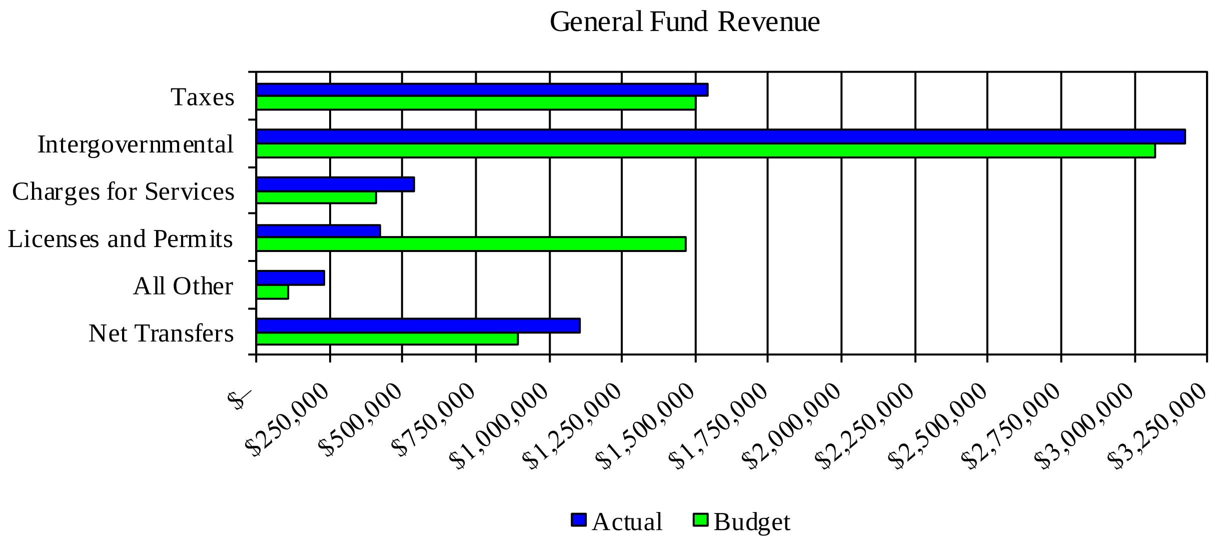
The City Council has formally adopted a fund balance policy regarding the fund balance for the General Fund. The policy establishes that the City will strive to maintain an unassigned fund balance in the General Fund in the range of 35.0–50.0 percent of the following year's budgeted expenditures. At December 31, 2016, the unassigned fund balance of the General Fund was 49.7 percent of the subsequent year's budgeted expenditures.

A trend that is typical to Minnesota local governments, especially the General Fund of cities, is the unusual cash flow experienced throughout the year. The City's General Fund cash disbursements are made fairly evenly during the year other than the impact of seasonal services such as snowplowing, street maintenance, and park activities. Cash receipts of the General Fund are quite a different story. Taxes and state aids comprise almost 80 percent of the fund's total annual revenue. Approximately half of these revenues are received by the City in July and the rest in December. Consequently, the City needs to have adequate cash reserves to finance its everyday operations between these payments.

The following graph illustrates the monthly cash flow of the General Fund in recent years (excluding interfund borrowing). Adequate fund balances in the General Fund have provided for positive month-end balances for all three years presented.

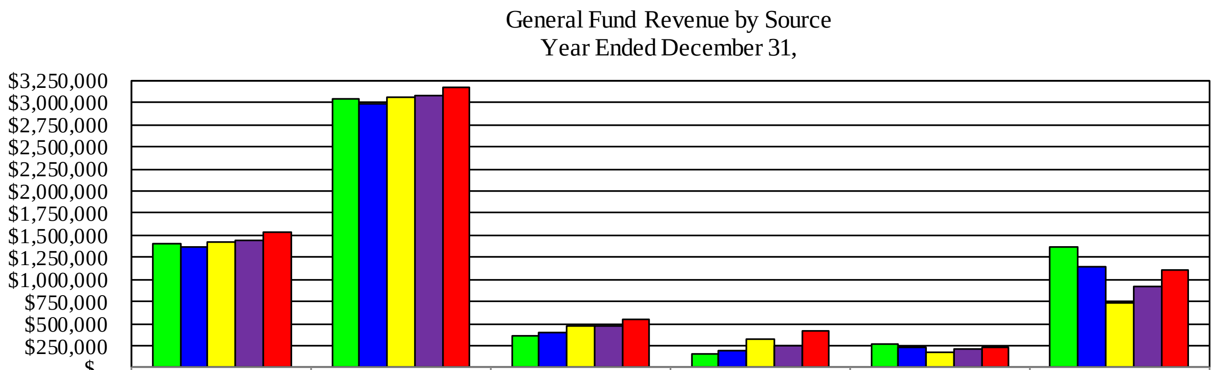


The following graph reflects the City's General Fund revenues and net transfers, budget and actual, for 2016:




Total General Fund revenues and net transfers in 2016 were $7,016,503, which was $427,414 less than the final budget. The majority of this variance is in licenses and permits, which was under budget by $1,039,720 relating to expected building permits for projects that were delayed until after 2016.

The following graph presents the City's General Fund revenue sources for the last five years:

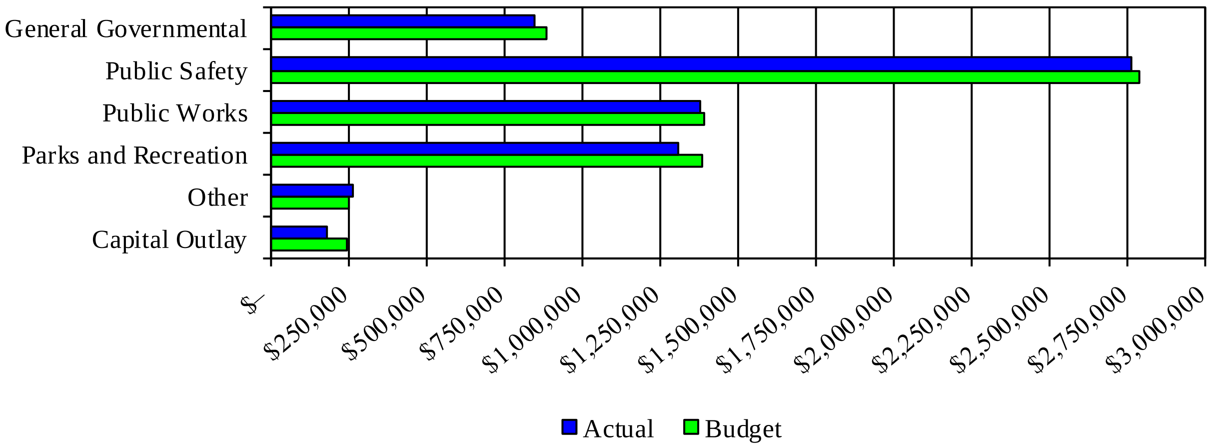



| | Taxes | Intergovernmental | Charges for Services | Licenses and Permits | All Other | Net Transfers |
|---|---|---|---|---|---|---|
| 2012 | $1,403,809 | $3,042,060 | $365,805 | $163,510 | $271,912 | $1,367,899 |
| 2013 | $1,364,783 | $2,996,269 | $398,820 | $191,505 | $230,809 | $1,146,706 |
| 2014 | $1,420,809 | $3,054,414 | $467,977 | $316,846 | $181,196 | $737,523 |
| 2015 | $1,434,939 | $3,088,098 | $469,790 | $244,557 | $212,568 | $912,398 |
| 2016 | $1,540,462 | $3,176,714 | $539,878 | $423,760 | $232,181 | $1,103,508 |

Revenues and net transfers for the year ended December 31, 2016 increased by $654,153, which was the result of increases across each source of revenue. Due to the large amount of tax exempt property in the City, the City has historically relied heavily on intergovernmental revenue (mainly state aid) and transfers from its enterprise funds to help support General Fund operations.

The following graph provides the components of the City's General Fund spending for 2016 compared to budget:

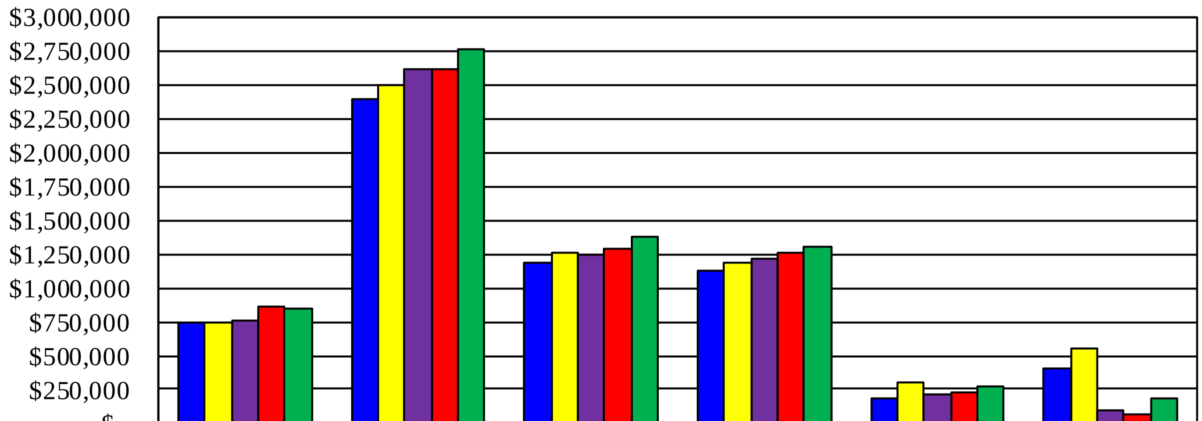
General Fund Expenditures
Budget and Actual




Total General Fund expenditures for 2016 were $6,737,933, which was $207,901 less than budget. Most functions were under budget in the current year.

The following graph presents the components of the City's General Fund spending for the past five years:

General Fund Expenditures by Function
Year Ended December 31,




| | General Governmental | Public Safety | Public Works | Parks and Recreation | Other | Capital Outlay |
|---|---|---|---|---|---|---|
| 2012 | $741,273 | $2,394,611 | $1,187,139 | $1,132,686 | $183,104 | $409,753 |
| 2013 | $741,971 | $2,496,385 | $1,259,768 | $1,183,925 | $307,035 | $557,274 |
| 2014 | $764,766 | $2,611,444 | $1,246,956 | $1,222,334 | $208,982 | $94,985 |
| 2015 | $865,083 | $2,619,901 | $1,284,150 | $1,258,730 | $221,580 | $63,680 |
| 2016 | $846,187 | $2,760,271 | $1,379,018 | $1,305,776 | $265,885 | $180,796 |

In 2016, total General Fund expenditures increased by $424,809. Public safety increased by $140,370, mainly due to wage increases and the filling of vacant positions.

## ENTERPRISE FUNDS OVERVIEW

The City maintains a number of enterprise funds to account for services the City provides that are financed primarily through fees charged to those utilizing the service. This section of the report provides you with an overview of the financial trends and activities of the City's enterprise funds.

The enterprise funds comprise a considerable portion of the City's activities. These funds help to defray overhead and administrative costs and provide additional support to general government operations by way of annual transfers. We understand the City is proactive in reviewing these activities on an ongoing basis and we want to reiterate the importance of continually monitoring these operations. Over the years we have emphasized to our city clients the importance of these utility operations being self-sustaining, preventing additional burdens on general governmental funds. This would include the accumulation of net position for future capital improvements and to provide a cushion in the event of a negative trend in operations.

### ENTERPRISE FUNDS FINANCIAL POSITION

The following table summarizes the changes in the financial position of the City's enterprise funds during the years ended December 31, 2015 and 2016, presented both by classification and by fund:

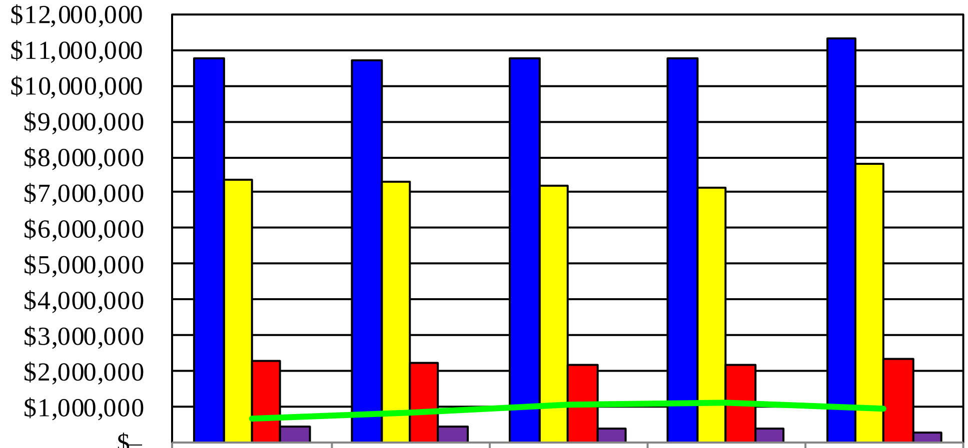
**Enterprise Funds Change in Financial Position**

| | Net Position as of December 31, 2015 | Net Position as of December 31, 2016 | Increase (Decrease) |
|---|---|---|---|
| Net position of enterprise funds | | | |
| Total by classification | | | |
| Net investment in capital assets | $ 47,205,913 | $ 47,717,968 | $ 512,055 |
| Restricted for debt service | 1,168,228 | 1,168,229 | 1 |
| Restricted for capital replacement | 577,441 | 633,305 | 55,864 |
| Unrestricted | 3,025,081 | 3,309,927 | 284,846 |
| Total enterprise funds | $ 51,976,663 | $ 52,829,429 | $ 852,766 |
| Total by fund | | | |
| Electric | $ 16,612,510 | $ 16,603,714 | $ (8,796) |
| Water | 8,564,881 | 8,639,396 | 74,515 |
| Environmental Services | 194,283 | 151,966 | (42,317) |
| Wastewater | 18,331,549 | 19,212,935 | 881,386 |
| Heartland Transit | 97,915 | 155,620 | 57,705 |
| Storm Water | 5,890,818 | 5,824,341 | (66,477) |
| Telecommunications Conduit | 215,604 | 201,508 | (14,096) |
| Long-Term Care Facility | (722,467) | (697,749) | 24,718 |
| Medical Office Building | 2,791,570 | 2,737,698 | (53,872) |
| Total enterprise funds | $ 51,976,663 | $ 52,829,429 | $ 852,766 |

## ELECTRIC FUND

The following graph presents five years of comparative data for the City's Electric Fund:

Electric Fund Operation
Year Ended December 31,




| | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|
| Operating Revenue | $10,751,186 | $10,726,029 | $10,776,761 | $10,774,242 | $11,341,733 |
| Purchased Power | $7,357,680 | $7,276,105 | $7,163,849 | $7,136,405 | $7,793,201 |
| Operating Expense | $2,292,370 | $2,223,702 | $2,140,138 | $2,177,580 | $2,330,813 |
| Net Other Expense | $437,112 | $420,464 | $396,635 | $380,329 | $286,153 |
| Income Before Transfers | $664,024 | $805,758 | $1,076,139 | $1,079,928 | $931,566 |

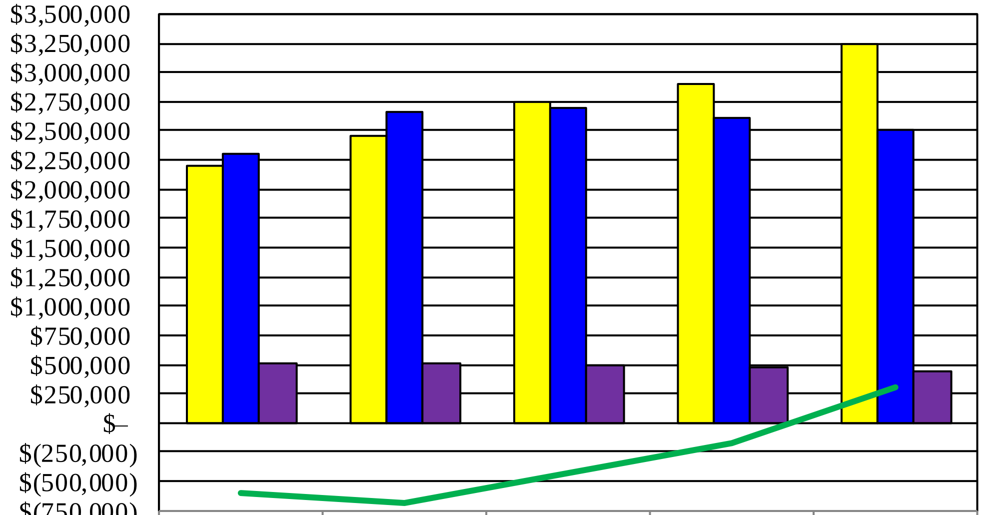
At December 31, 2016, the Electric Fund had a total net position of $16,603,714, of which $1,061,428 was restricted for debt service; $13,994,350 was the net investment in capital assets; and $1,547,936 was unrestricted. The Electric Fund ended the year with working capital of $1,349,888.

The Electric Fund operating revenue was $11,341,733 for 2016, an increase of $567,491 (5.3 percent) from increased rates and usage. Purchased power increased $656,796, or 9.2 percent. Operating expenses (excluding purchased power) increased by $153,233 (7.0 percent) in 2016, mainly due to increases in personal services.

**WATER FUND**

The following graph presents selected data for the City's Water Fund for the past five years:

Water Fund Operation
Year Ended December 31,




| | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|
| Operating Revenue | $2,204,700 | $2,464,354 | $2,745,745 | $2,902,935 | $3,247,341 |
| Operating Expense | $2,304,782 | $2,657,623 | $2,693,569 | $2,606,868 | $2,502,713 |
| Net Other Expense | $507,560 | $501,126 | $487,055 | $470,710 | $448,346 |
| Income (Loss) Before Transfers | $(607,642) | $(694,395) | $(434,879) | $(174,643) | $296,282 |

At December 31, 2016, the Water Fund had a total net position of $8,639,396, of which $8,224,531 was the net investment in capital assets and $414,865 was unrestricted. The Water Fund ended the year with a deficit working capital balance of ($265,920).

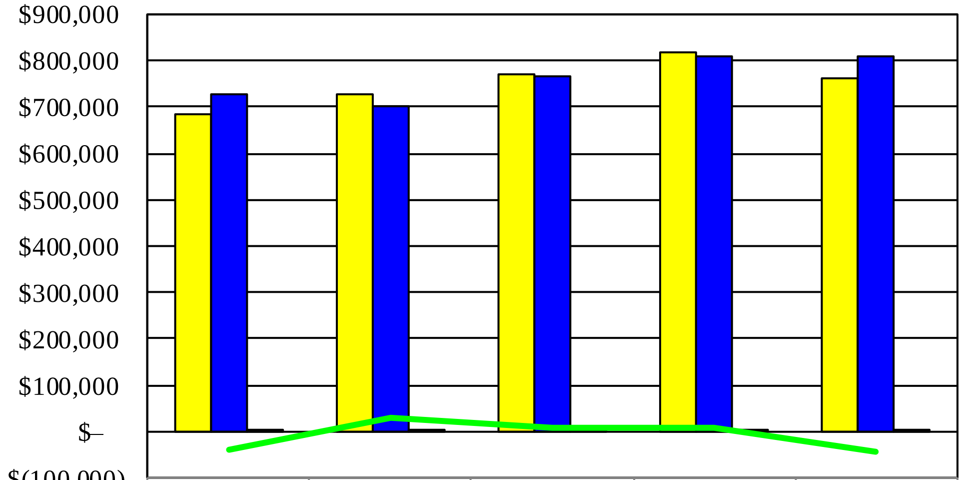
The Water Fund's operating revenue was $3,247,341 for 2016, an increase of $344,406, or 11.9 percent, which was primarily the result of an increase in the water rates. Operating expenses decreased by $104,155, or 4.0 percent, mainly due to older, large assets becoming fully depreciated in the prior year.

Although this fund is in a positive financial position, we suggest that the City continue to review the water rates on an annual basis. Water rates are generally designed to cover operating costs and provide an accumulation of resources for significant repairs and replacements, and an operating cushion for potential negative years in financial operations.

**ENVIRONMENTAL SERVICES FUND**

The following graph presents selected data for the City's Environmental Services Fund for the past five years:

Environmental Services Fund
Year Ended December 31,




| | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|
| Operating Revenue | $683,726 | $727,614 | $769,938 | $815,663 | $761,540 |
| Operating Expense | $725,109 | $701,516 | $764,224 | $810,888 | $808,216 |
| Net Other Revenue | $2,136 | $1,711 | $1,687 | $1,755 | $4,359 |
| Change in Net Position | $(39,247) | $27,809 | $7,401 | $6,530 | $(42,317) |

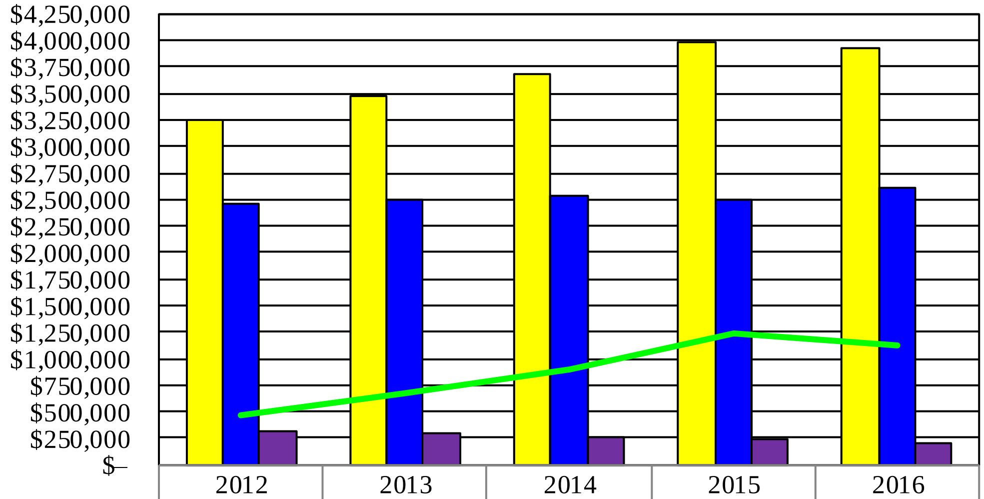
At December 31, 2016, the Environmental Services Fund had a total net position of $151,966, of which $34,322 was the net investment in capital assets and $117,644 was unrestricted. The Environmental Services Fund ended the year with working capital of $228,994.

The Environmental Services Fund operating revenue was $761,540 for 2016, a decrease of $54,123 (6.6 percent). Operating expenses decreased about $2,672 (0.3 percent) compared to the prior year.

**WASTEWATER FUND**

The following graph presents selected data for the City's Wastewater Fund for the past five years:

Wastewater Fund
Year Ended December 31,



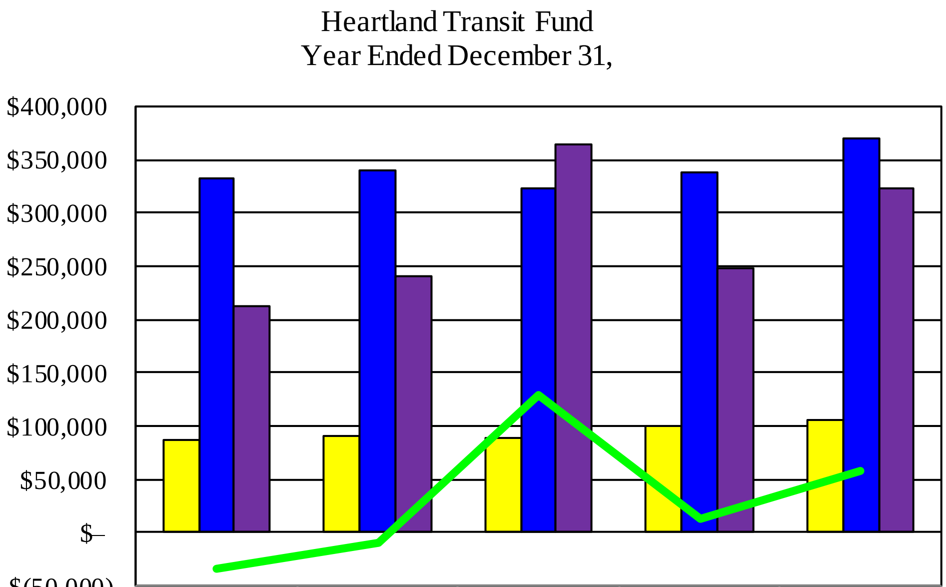

| | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|
| Operating Revenue | $3,253,915 | $3,473,518 | $3,689,500 | $3,978,265 | $3,935,525 |
| Operating Expense | $2,456,689 | $2,505,529 | $2,536,210 | $2,492,423 | $2,602,508 |
| Net Other Expense | $323,534 | $298,305 | $260,526 | $240,099 | $209,625 |
| Income (Loss) Before Transfers | $473,692 | $669,684 | $892,764 | $1,245,743 | $1,123,392 |

At December 31, 2016, the Wastewater Fund had a total net position of $19,212,935, of which $17,834,050 was the net investment in capital assets; $633,305 was restricted; and $745,580 was unrestricted. The Wastewater Fund ended the year with a working capital balance of $467,437.

The Wastewater Fund operating revenue was $3,935,525 for 2016, a decrease of $42,740, or 1.1 percent, while operating expenses increased $110,085, or 4.4 percent.

**HEARTLAND TRANSIT FUND**

The following graph presents selected data for the City's Heartland Transit Fund for the past five years:




| | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|
| Operating Revenue | $85,947 | $90,601 | $89,151 | $100,220 | $105,230 |
| Operating Expense | $332,038 | $340,293 | $323,696 | $337,148 | $370,353 |
| Net Other Revenue | $212,307 | $240,307 | $363,293 | $248,882 | $322,828 |
| Change in Net Position | $(33,784) | $(9,385) | $128,748 | $11,954 | $57,705 |

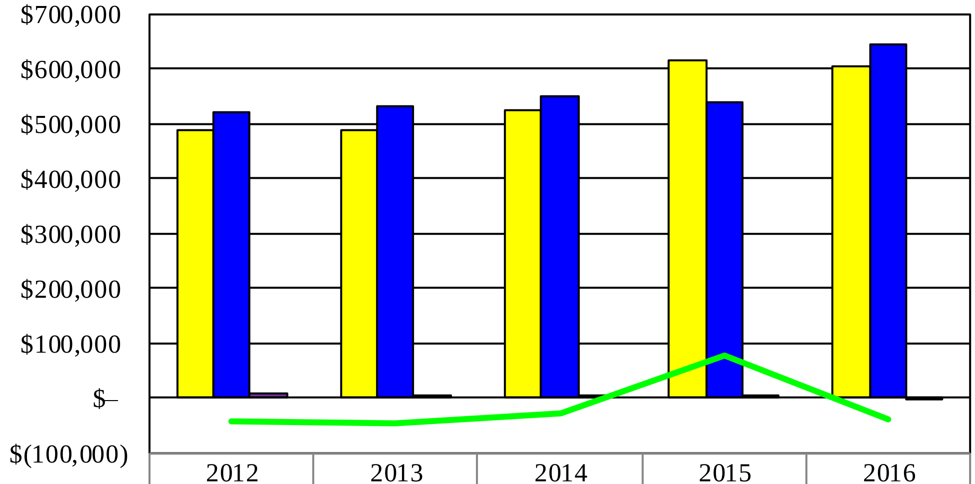
At December 31, 2016, the Heartland Transit Fund had a total net position of $155,620, of which $156,630 was the net investment in capital assets and a deficit balance of ($1,010) was unrestricted. The Heartland Transit Fund ended the year with a working capital balance of $72,417.

The Heartland Transit Fund operating revenue was $105,230 for 2016, an increase of $5,010 (5.0 percent). Operating expenses increased by $33,205 (9.8 percent).

**STORM WATER FUND**

The following graph presents selected data for the City's Storm Water Fund for the past five years:

Storm Water Fund
Year Ended December 31,



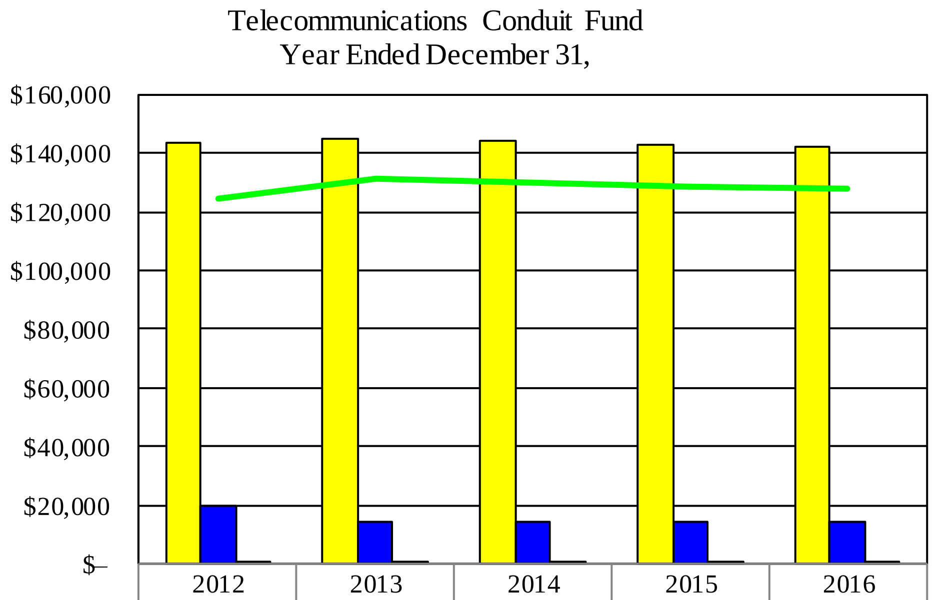

| | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|
| Operating Revenue | $488,622 | $489,138 | $526,528 | $615,673 | $605,664 |
| Operating Expense | $522,787 | $531,102 | $551,279 | $537,817 | $643,298 |
| Net Other Expense | $6,864 | $5,687 | $2,830 | $1,159 | $(494) |
| Income (Loss) Before Transfers | $(41,029) | $(47,651) | $(27,581) | $76,697 | $(38,128) |

At December 31, 2016, the Storm Water Fund had a total net position of $5,824,341, of which $5,411,018 was the net investment in capital assets and $413,323 is considered unrestricted. The Storm Water Fund ended the year with working capital of $521,343.

The Storm Water Fund operating revenue was $605,664 for 2016, a decrease of $10,009, or 1.6 percent. Operating expenses increased $105,481, or 19.6 percent, due to wage increases, filling vacant positions, and an increase in depreciation expense related to new equipment.

**TELECOMMUNICATIONS CONDUIT FUND**

The following graph presents selected data for the City's Telecommunications Conduit Fund for the past five years:




| | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|
| Operating Revenue | $143,736 | $145,219 | $144,071 | $142,669 | $142,273 |
| Operating Expense | $19,670 | $14,264 | $14,264 | $14,264 | $14,264 |
| Net Other Revenue | $193 | $301 | $381 | $135 | $168 |
| Income Before Transfers | $124,259 | $131,256 | $130,188 | $128,540 | $128,177 |

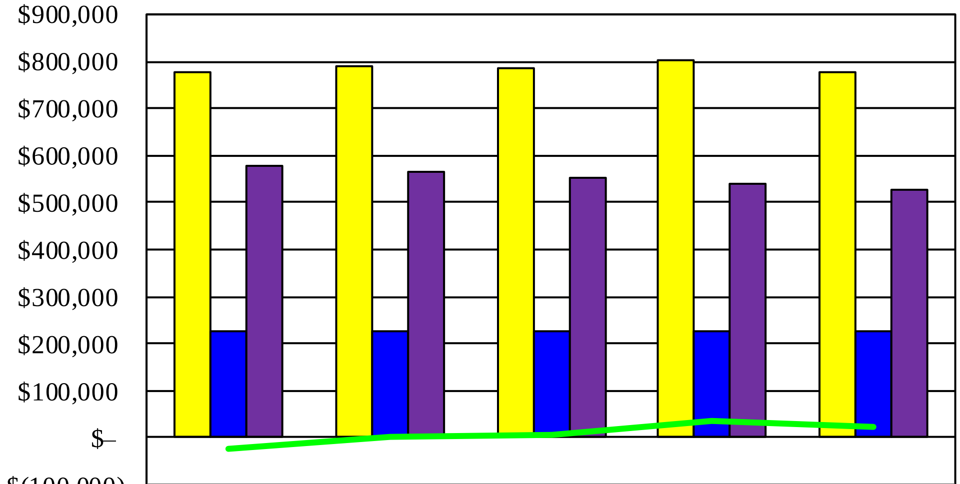
At December 31, 2016, the Telecommunications Conduit Fund had a total net position of $201,508, of which $197,028 was the net investment in capital assets and $4,480 was considered unrestricted. The Telecommunications Conduit Fund ended the year with working capital of $4,480.

The Telecommunications Conduit Fund operating revenue was $142,273 for 2016, a decrease of $396. Operating expenses were consistent with the prior year.

## LONG-TERM CARE FACILITY FUND

The following graph presents selected data for the City's Long-Term Care Facility Fund for the past five years:

Long-Term Care Facility Fund
Year Ended December 31,



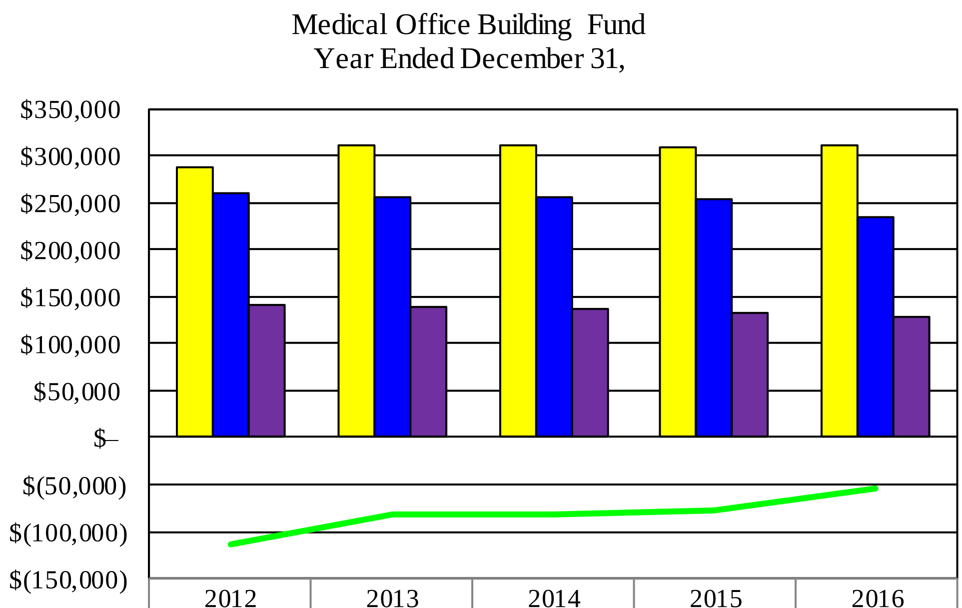

| | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|
| Operating Revenue | $776,165 | $790,338 | $785,719 | $801,544 | $778,119 |
| Operating Expense | $225,323 | $226,148 | $225,640 | $226,248 | $226,621 |
| Net Other Expense | $575,618 | $564,314 | $552,419 | $539,760 | $526,780 |
| Change in Net Position | $(24,776) | $(124) | $7,660 | $35,536 | $24,718 |

At December 31, 2016, the Long-Term Care Facility Fund had a total net position deficit of ($697,749), of which a deficit of ($800,095) was the net investment in capital assets, $106,801 was restricted for debt service, and a deficit balance of ($4,455) was considered unrestricted.

The Long-Term Care Facility Fund is used to collect lease revenue and pay debt service on the long-term care facility.

**MEDICAL OFFICE BUILDING FUND**

The following table presents selected data for the City's Medical Office Building Fund for the past five years:




| | 2012 | 2013 | 2014 | 2015 | 2016 |
|---|---|---|---|---|---|
| Operating Revenue | $288,242 | $311,363 | $311,715 | $310,107 | $310,515 |
| Operating Expense | $260,117 | $255,149 | $256,076 | $254,673 | $234,919 |
| Net Other Expense | $141,690 | $138,213 | $137,392 | $132,840 | $129,468 |
| Change in Net Position | $(113,565) | $(81,999) | $(81,753) | $(77,406) | $(53,872) |

At December 31, 2016, the Medical Office Building Fund had a total net position of $2,737,698, of which $2,666,134 was the net investment in capital assets and $71,564 was unrestricted.

The Medical Office Building Fund is used to account for the construction of a medical office building. This fund is also used to collect lease revenue and pay debt service on this same facility.

## DEBT SERVICE

The following table shows outstanding debt per capita for the City's governmental activities and comparable state-wide averages:

Outstanding Debt per Capita
Governmental Activities
With State-Wide Comparable Information

| Bond Type | State-Wide as of December 31, 2014 | State-Wide as of December 31, 2015 | City of Saint Peter as of December 31, 2014 | City of Saint Peter as of December 31, 2015 | City of Saint Peter as of December 31, 2016 |
|---|---|---|---|---|---|
| General obligation | $ 476 | $ 486 | $ 227 | $ 203 | $ 186 |
| Tax increment | 96 | 96 | 332 | 285 | 440 |
| Special assessment | 483 | 475 | – | – | – |
| General obligation revenue | 373 | 384 | 401 | 376 | 350 |
| Revenue | 230 | 219 | – | – | – |
| Other | 8 | 5 | – | – | – |
| Governmental activities total | $ 1,666 | $ 1,665 | $ 960 | $ 864 | $ 976 |

The following table shows outstanding debt per capita for the City's enterprise funds and comparable state-wide averages:

Outstanding Debt per Capita
Enterprise Funds
With State-Wide Comparable Information

| Fund | State-Wide as of December 31, 2014 | State-Wide as of December 31, 2015 | City of Saint Peter as of December 31, 2014 | City of Saint Peter as of December 31, 2015 | City of Saint Peter as of December 31, 2016 |
|---|---|---|---|---|---|
| Electric | $ 439 | $ 396 | $ 746 | $ 691 | $ 624 |
| Water | 179 | 185 | 1,571 | 1,491 | 1,413 |
| Wastewater | 196 | 203 | 889 | 784 | 686 |
| Storm water | 19 | 19 | 12 | 9 | 7 |
| Total enterprise funds | $ 833 | $ 803 | $ 3,218 | $ 2,975 | $ 2,730 |
| Government-wide totals | $ 2,499 | $ 2,468 | $ 4,178 | $ 3,839 | $ 3,706 |

As seen in the table above, the City has more outstanding debt per capita than the average Minnesota city. This higher than average debt balance is mostly related to balances within the Water and Wastewater Funds, which are related to recent capital improvements in these funds.

## GOVERNMENT-WIDE FINANCIAL STATEMENTS

In addition to fund-based information, the current reporting model for governmental entities also requires the inclusion of two government-wide financial statements designed to present a clear picture of the City as a single, unified entity. These government-wide financial statements provide information on the total cost of delivering services, including capital assets and long-term liabilities.

### STATEMENT OF NET POSITION

The Statement of Net Position essentially tells you what your city owns and owes at a given point in time, the last day of the fiscal year. Theoretically, net position represents the resources the City has leftover to use for providing services after its debts are settled. However, those resources are not always in spendable form, or there may be restrictions on how some of those resources can be used. Therefore, net position is divided into three components: net investment in capital assets, restricted, and unrestricted.

The following table presents the components of the City's net position as of December 31, 2015 and 2016, for governmental activities and business-type activities:

| | As of December 31, 2015 | As of December 31, 2016 | Increase (Decrease) |
|---|---|---|---|
| Net position | | | |
| Governmental activities | | | |
| Net investment in capital assets | $ 22,242,676 | $ 24,742,817 | $ 2,500,141 |
| Restricted | 7,581,011 | 6,219,284 | (1,361,727) |
| Unrestricted | 1,236,415 | 2,716,042 | 1,479,627 |
| Total governmental activities | 31,060,102 | 33,678,143 | 2,618,041 |
| Business-type activities | | | |
| Net investment in capital assets | 47,205,913 | 47,717,968 | 512,055 |
| Restricted | 1,745,669 | 1,801,534 | 55,865 |
| Unrestricted | 3,025,081 | 3,309,927 | 284,846 |
| Total business-type activities | 51,976,663 | 52,829,429 | 852,766 |
| Total net position | $ 83,036,765 | $ 86,507,572 | $ 3,470,807 |

Much of the City's net position is restricted by virtue of external restrictions (statutory reserves) or by the nature of the fund it is in. Further, a significant portion of net position has been identified as invested in capital assets, net of related debt, which leaves the balance unrestricted.

## STATEMENT OF ACTIVITIES

The Statement of Activities tracks the City's yearly revenues and expenses, as well as any other transactions that increase or reduce total net position. These amounts represent the full cost of providing services. The Statement of Activities provides a more comprehensive measure than just the amount of cash that changed hands, as reflected in the fund-based financial statements. This statement includes the cost of supplies used, depreciation of long-lived capital assets, and other accrual-based expenses.

The following table presents the change in the net position of the City for the years ended December 31, 2015 and 2016:

| | 2015 | 2016 | | |
|---|---|---|---|---|
| | Net Difference | Expenses | Program Revenues | Net Difference |
| Net (expense) revenue | | | | |
| Governmental activities | | | | |
| General government | $ (768,953) | $ 1,415,551 | $ 598,320 | $ (817,231) |
| Public safety | (2,214,369) | 3,625,331 | 993,111 | (2,632,220) |
| Public works | (1,982,248) | 2,367,278 | 2,514,367 | 147,089 |
| Parks and recreation | (1,719,129) | 2,027,639 | 255,567 | (1,772,072) |
| Economic development | (712,229) | 1,429,316 | 906,335 | (522,981) |
| Interest on long-term debt | (316,573) | 308,080 | – | (308,080) |
| Business-type activities | | | | |
| Electric | 1,057,183 | 10,431,567 | 11,346,611 | 915,044 |
| Water | (181,889) | 2,958,714 | 3,290,348 | 331,634 |
| Environmental services | 5,101 | 808,216 | 764,392 | (43,824) |
| Wastewater | 1,240,620 | 2,823,122 | 3,991,642 | 1,168,520 |
| Transit | 11,917 | 370,353 | 427,240 | 56,887 |
| Storm water | 73,494 | 646,864 | 606,393 | (40,471) |
| Telecommunications conduit | 128,405 | 14,264 | 142,273 | 128,009 |
| Long-term care facility | 34,618 | 754,276 | 778,119 | 23,843 |
| Medical office building | (78,155) | 364,668 | 310,515 | (54,153) |
| | (5,422,207) | $ 30,345,239 | $ 26,925,233 | (3,420,006) |
| General revenues | | | | |
| Taxes | 3,015,476 | | | 3,154,083 |
| Unrestricted grants and contributions | 3,368,538 | | | 3,443,533 |
| Investment earnings | 95,959 | | | 92,573 |
| Other revenues | 51,352 | | | 172,499 |
| Gain on sale of assets | 113,426 | | | 28,125 |
| Total general revenues | 6,644,751 | | | 6,890,813 |
| Change in net position | 1,222,544 | | | 3,470,807 |
| Net position – beginning | 81,814,221 | | | 83,036,765 |
| Net position – ending | $ 83,036,765 | | | $ 86,507,572 |

One of the goals of this statement is to provide a side-by-side comparison to illustrate the difference in the way the City's governmental and business-type operations are financed. The table clearly illustrates the dependence of the City's governmental operations on general revenues, such as property taxes and unrestricted grants. It also shows if the City's business-type activities are generating sufficient program revenues (service charges and program-specific grants) to cover expenses. This is critical given the current downward pressures on the general revenue sources.

## LEGISLATIVE UPDATES

The 2016 legislative session, falling in the second half of the state's fiscal biennium, was scheduled to be a short session lasting only 11 weeks. Since biennial budgets are adopted in odd-year legislative sessions, less time is usually needed for the even-year sessions. However, because the 2015 Legislature adjourned without passing funding bills in several significant areas, it was anticipated that the 2016 legislative session would be considerably more active than the typical short session. In spite of this, only a few funding bills were brought forth to the Governor by the end of the 2016 regular legislative session, including a supplemental budget bill and an omnibus tax bill. The Governor chose not to sign the tax bill due to a drafting error that would have resulted in an unintended reduction of state revenues. When the framework for a special session could not be agreed upon, the fiscal year ended without the adoption of a new tax bill, capital bonding bill, or transportation funding package.

The following is a summary of recent legislation affecting Minnesota cities:

**Border-to-Border Broadband Grants** – The 2016 supplemental budget act appropriated $35 million in fiscal 2017 for a Border-to-Border Broadband Grant Program. The grants, available through the Office of Broadband Development in the Department of Employment and Economic Development (DEED), provide funding to help communities meet state goals for the development of state-wide high-speed broadband access, focusing on areas currently considered to be underserved or with a high concentration of low-income households.

**Equity-Related Programs and Grants** – The 2016 supplemental budget act also appropriated $35 million in fiscal 2017 for the financing of equity-related programs through DEED, the majority of which was allocated for programs and grants for communities of color, people with disabilities, seniors, and youth.

**Sales Tax Exemption** – Effective January 1, 2017, the sales tax exemption on the purchase of goods or services enacted for cities in 2014 is expanded to include all special districts; city, county, or township instrumentalities; economic development authorities; housing and redevelopment authorities; and all joint power boards or organizations.

**Taxes Covered Under Debt Management Services** – Amendments were made to the statutes governing debt management and debt settlement services to clarify the status of delinquent taxes owed to Minnesota local governments and political subdivisions as debt with regard to those services, and include those entities as creditors for the purpose of debt management services.

**Elections** – An omnibus elections law was passed making several changes to elections administration requirements. In addition to establishing a presidential primary to take the place of the current caucus system beginning in 2020, the law modified election procedures in a number of areas, including: absentee balloting, voting station dimensions, election canvassing, candidate filing, the extension of polling hours to accommodate voters in line at closing, and emergency election plans.

**Police-Worn Body Cameras** – A number of new laws were enacted related to portable recording systems (police-worn body cameras) and the data derived from their use, addressing: data retention and destruction, permitted uses of the systems, audits of the data, and vendor practices. Among the changes are a requirement for gathering public input before purchasing or implementing the use of portable recording systems, and requirements for the adoption and dissemination of written policies over the use of portable recording systems.

**Veteran Preference Act** – New language was added to state statutes clarifying that Minnesota cities and towns may require a veteran to complete an initial probationary period when hired.

**Charitable Gambling** – Cities that require charitable gambling organizations to contribute 10 percent of their net profits to the city for charitable purposes are now required to acknowledge the source of the funds, either in communications about the receipt or distribution of the funds.

**Donation of Surplus Equipment –** Local governments are now permitted to donate surplus public works equipment, cell phones, or emergency medical and firefighting equipment to nonprofit organizations. The donation of surplus equipment was added to the list of exceptions to municipal tort liability. Prior to making any such donations, a city must adopt a policy on how it will determine what equipment is considered surplus and eligible for donation and how it will determine which nonprofit organizations will receive such donations. The policy must address the city's obligation to disclose that the donated equipment may be defective and cannot be relied upon for safety.

**Temporary Family Health Care Housing Permits** – A new special land use permit system was established for a specific type of mobile health care-related mobile housing, intended to provide transitional housing for seniors. Cities will be required to implement the new permit system unless they officially act to opt out of the program. The program sets forth requirements for structure and placement, the permit process and duration, applicants, inspections, and the process for opting out.

**Partition Fence Viewing Exemption** – Cities now have the authority to pass a resolution to exempt adjoining owners or occupants from the partition fence law when their land is considered to be less than 20 acres combined, thereby relieving the city of the responsibility of participating in a potentially costly "fence-viewing" process to mediate disputes between adjoining landowners required to share the costs of constructing fences.

## ACCOUNTING AND AUDITING UPDATES

### GASB STATEMENT NO. 73, *ACCOUNTING AND FINANCIAL REPORTING FOR PENSIONS AND RELATED ASSETS THAT ARE NOT WITHIN THE SCOPE OF GASB STATEMENT 68, AND AMENDMENTS TO CERTAIN PROVISIONS OF GASB STATEMENTS 67 AND 68*

This statement extends the approach to accounting and financial reporting established in GASB Statement No. 68 to all pensions, including those not administered through a trust. Governmental employers participating in such plans will be required to report the total of any unfunded pension liability related to the plan in their accrual basis financial statements, rather than the net pension liability. The requirements of this statement that address accounting and financial reporting by employers and governmental nonemployer contributing entities for pensions not within the scope of GASB Statement No. 68, are effective for financial statements for fiscal years beginning after June 15, 2016.

This statement also clarified the application of certain provisions of GASB Statement Nos. 67 and 68 regarding 10-year schedules of required supplementary information (RSI) and other recognition issues pertaining to employers and nonemployer contributing entities effective for financial statements for fiscal years beginning after June 15, 2015.

### GASB STATEMENT NO. 74, *FINANCIAL REPORTING FOR POSTEMPLOYMENT BENEFIT PLANS OTHER THAN PENSION PLANS*

This statement establishes new accounting and financial reporting requirements for other post-employment benefits (OPEB) plans, replacing GASB Statement Nos. 43 and 57. It also includes requirements for defined contribution OPEB plans that replace the requirements for those OPEB plans in GASB Statement Nos. 25, 43, and 50.

This statement will improve financial reporting primarily through enhanced note disclosures and schedules of RSI that will be presented by OPEB plans administered through trusts meeting the specified criteria. The new information will enhance the decision-usefulness of the financial reports of those OPEB plans, their value for assessing accountability, and their transparency by providing information about measures of net OPEB liabilities and explanations of how and why those liabilities changed from year-to-year. The net OPEB liability information, including ratios, will offer an up-to-date indication of the extent to which the total OPEB liability is covered by the fiduciary net position of the OPEB plan. The comparability of the reported information for similar types of OPEB plans will be improved by the changes related to the attribution method used to determine the total OPEB liability. The contribution schedule will provide measures to evaluate decisions related to the assessment of contribution rates in comparison with actuarially determined rates, if such rates are determined. In addition, new information about rates of return on OPEB plan investments will inform financial report users about the effects of market conditions on the OPEB plan’s assets over time and provide information for users to assess the relative success of the OPEB plan’s investment strategy and the relative contribution that investment earnings provide to the OPEB plan’s ability to pay benefits to plan members when they come due.

This statement is effective for financial statements for fiscal years beginning after June 15, 2016. Earlier application is encouraged.

### GASB STATEMENT NO. 75, *ACCOUNTING AND FINANCIAL REPORTING FOR POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS*

GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, establishes new accounting and financial reporting requirements for governments whose employees are provided with OPEB, as well as for certain nonemployer governments that have a legal obligation to provide financial support for OPEB provided to the employees of other entities. This statement replaces the requirements of GASB Statement Nos. 45 and 57.

This statement establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures. Similar to changes implemented for pensions, this statement requires the liability of employers and nonemployer contributing entities to employees for defined benefit OPEB (net OPEB liability) to be measured as the portion of the present value of projected benefit payments to be provided to current active and inactive employees that is attributed to those employees' past periods of service (total OPEB liability), less the amount of the OPEB plan's fiduciary net position. Note disclosure and RSI requirements about defined benefit OPEB also are addressed.

This statement is effective for fiscal years beginning after June 15, 2017. Earlier application is encouraged.

### GASB STATEMENT NO. 80, *BLENDING REQUIREMENTS FOR CERTAIN COMPONENT UNITS—AN AMENDMENT OF GASB STATEMENT NO. 14*

The objective of this statement is to clarify the financial statement presentation requirements for certain component units. This statement amends the blending requirements for the financial statement presentation of component units of all state and local governments. The additional criterion requires blending of a component unit incorporated as a not-for-profit corporation in which the primary government is the sole corporate member. The additional criterion does not apply to component units included in the financial reporting entity pursuant to the provisions of GASB Statement No. 39, *Determining Whether Certain Organizations Are Component Units—an amendment of GASB Statement No. 14*.

The requirements of this statement are effective for reporting periods beginning after June 15, 2016. Earlier application is encouraged.

### GASB STATEMENT NO. 81, *IRREVOCABLE SPLIT-INTEREST AGREEMENTS*

This statement provides recognition and measurement guidance for the accounting and financial reporting of irrevocable split-interest agreements by governments that are the beneficiary of such an agreement. Split-interest agreements are a type of giving agreement used by donors to provide resources to two or more beneficiaries, including governments.

This statement requires that a government that receives resources pursuant to an irrevocable split-interest agreement (1) recognize assets, liabilities, and deferred inflows of resources at the inception of the agreement, (2) recognize assets representing its beneficial interests in irrevocable split-interest agreements that are administered by a third party if the government controls the present service capacity of the beneficial interests, and (3) recognize revenue when the resources become applicable to the reporting period.

The requirements of this statement are effective for financial statements for periods beginning after December 15, 2016, and should be applied retroactively. Earlier application is encouraged.

**GASB STATEMENT NO. 82, *PENSION ISSUES—AN AMENDMENT OF GASB STATEMENTS NO. 67, NO. 68, AND NO. 73***

The intent of this statement is to address certain issues raised with respect to GASB Statement Nos. 67, 68, and 73.

This statement amends GASB Statement Nos. 67 and 68, changing the definition of "covered payroll" utilized in schedules of RSI from the payroll of employees that are provided with pensions through the pension plan, to the payroll on which contributions to a pension plan are based. It clarifies that a deviation, as the term is used in Actuarial Standards of Practice, is not considered to be in conformity with the requirements of GASB Statement Nos. 67, 68, or 73 for the selection of assumptions used in determining the total pension liability and related measures. It also clarifies that payments made by an employer to satisfy contribution requirements that are identified by the pension plan terms as plan member contribution requirements should be classified as plan member contributions for purposes of Statement No. 67 and as employee contributions for purposes of Statement No. 68, and requires that an employer's expense and expenditures for those amounts be recognized in the period for which the contribution is assessed and classified in the same manner as the employer classifies similar compensation other than pensions.

The requirements of this statement are effective for reporting periods beginning after June 15, 2016, except for the requirements of this statement for the selection of assumptions in a circumstance in which an employer's pension liability is measured as of a date other than the employer's most recent fiscal year-end. In that circumstance, the requirements for the selection of assumptions are effective for that employer in the first reporting period in which the measurement date of the pension liability is on or after June 15, 2017. Earlier application is encouraged.

**GASB STATEMENT NO. 83, *CERTAIN ASSET RETIREMENT OBLIGATIONS***

This statement addresses accounting and financial reporting for certain asset retirement obligations (ARO), which are legally enforceable liabilities associated with the retirement of a tangible capital asset.

This statement establishes criteria for determining the timing and pattern of recognition of a liability and a corresponding deferred outflow of resources for ARO. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability when it is both incurred and reasonably estimable. The measurement of an ARO is required to be based on the best estimate of the current value of outlays expected to be incurred, and a deferred outflow of resources associated with an ARO is required to be measured at the amount of the corresponding liability upon initial measurement.

This statement requires the current value of a government's AROs to be adjusted for the effects of general inflation or deflation at least annually, and a government to evaluate all relevant factors at least annually to determine whether the effects of one or more of the factors are expected to significantly change the estimated asset retirement outlays. A government should remeasure an ARO only when the result of the evaluation indicates there is a significant change in the estimated outlays. Deferred outflows of resources should be reduced and recognized as outflows of resources in a systematic and rational manner over the estimated useful life of the tangible capital asset.

If a government owns a minority interest in a jointly owned tangible asset where a nongovernmental entity is the majority owner or has operational responsibility for the jointly owned asset, the government's minority share of an ARO should be reported using the measurement produced by the nongovernmental majority owner or the nongovernmental minority owner that has operational responsibility, without adjustment to conform to the liability measurement and recognition requirements of this statement.

The statement also requires disclosures of any funding or financial assurance requirements a government has related to the performance of asset retirement activities, along with any assets restricted for the payment of the government's AROs. This statement also requires disclosure of information about the nature of a government's AROs, the methods and assumptions used for the estimates of the liabilities, and the estimated remaining useful life of the associated tangible capital assets. If an ARO (or portions thereof) has been incurred by a government but is not yet recognized because it is not reasonably estimable, the government is required to disclose that fact and the reasons therefor. This statement requires similar disclosures for a government's minority shares of AROs.

The requirements of this statement are effective for reporting periods beginning after June 15, 2018. Earlier application is encouraged.

## GASB STATEMENT NO. 84, *FIDUCIARY ACTIVITIES*

This statement establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities.

An activity meeting the criteria should be reported in a fiduciary fund in the basic financial statements, which should present a statement of fiduciary net position and a statement of changes in fiduciary net position. This statement describes four fiduciary funds that should be reported, if applicable: (1) pension (and other employee benefit) trust funds, (2) investment trust funds, (3) private-purpose trust funds, and (4) custodial funds. Custodial funds generally should report fiduciary activities that are not held in a trust or equivalent arrangement that meets specific criteria.

A fiduciary component unit, when reported in the fiduciary fund financial statements of a primary government, should combine its information with its component units that are fiduciary component units and aggregate that combined information with the primary government's fiduciary funds.

This statement also provides for recognition of a liability to the beneficiaries in a fiduciary fund when an event has occurred that compels the government to disburse fiduciary resources, defined as when a demand for the resources has been made or when no further action, approval, or condition is required to be taken or met by the beneficiary to release the assets.

The requirements of this statement are effective for reporting periods beginning after December 15, 2018. Earlier application is encouraged.