

CITY OF PEQUOT LAKES, MINNESOTA

AUDITED FINANCIAL STATEMENTS

DECEMBER 31, 2018

SCHLENNER WENNER & CO.
Certified Public Accountants
& Business Consultants

**CITY OF PEQUOT LAKES, MINNESOTA
TABLE OF CONTENTS**

INTRODUCTORY SECTION:

CITY COUNCIL AND OFFICIALS 1

FINANCIAL SECTION:

INDEPENDENT AUDITORS' REPORT 2

REQUIRED SUPPLEMENTARY INFORMATION:

Management’s Discussion and Analysis 5

BASIC FINANCIAL STATEMENTS:

Government-wide Financial Statements

Statement of Net Position 14

Statement of Activities 15

Fund Financial Statements

Balance Sheet – Governmental Funds 16

Reconciliation of the Balance Sheet – Governmental Funds
to the Statement of Net Position 17

Statement of Revenues, Expenditures and
Changes in Fund Balances – Governmental Funds 18

Reconciliation of Changes in Fund Balance of Governmental
Funds to the Statement of Activities 19

Statement of Net Position – Proprietary Funds 20

Statement of Revenues, Expenses and
Changes in Net Position – Proprietary Funds 21

Statement of Cash Flows – Proprietary Funds 22

Notes to the Basic Financial Statements 24

REQUIRED SUPPLEMENTARY INFORMATION:

Budgetary Comparison Schedule – General Fund 57

Budgetary Comparison Schedule – Fire Department Fund 58

Schedule of City’s Proportionate Share of the Net Pension Liability 59

Schedule of City Pension Contributions 60

Schedule of Changes in Net Pension Liability (Asset) 61

Schedule of Changes in City’s Net OPEB Liability 62

Notes to the Required Supplementary Information 63

SUPPLEMENTARY INFORMATION:

Combining Balance Sheet – Nonmajor Governmental Funds 66

Combining Statement of Revenues, Expenditures and
Changes in Fund Balances – Nonmajor Governmental Funds 67

Schedule of Indebtedness 68

OTHER REQUIRED REPORTS:

Independent Auditors’ Report on Internal Control Over Financial
Reporting and on Compliance and Other Matters Based on an
Audit of Financial Statements Performed in Accordance with
Government Auditing Standards 69

Independent Auditors’ Report on Minnesota Legal Compliance 71

Schedule of Findings and Responses 72

Corrective Action Plans 75

**INTRODUCTORY
SECTION**

**CITY OF PEQUOT LAKES, MINNESOTA
CITY COUNCIL AND OFFICIALS
FOR THE YEAR ENDED DECEMBER 31, 2018**

CITY COUNCIL

Term Expires

Nancy Adams	Mayor	December 31, 2018
Jerry Akerson	Council Member	December 31, 2018
Randy Loukota	Council Member	December 31, 2018
Scott Pederson	Council Member	December 31, 2020
Mimi Swanson	Council Member	December 31, 2020

CITY OFFICIALS

Nancy Malecha	City Administrator
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**FINANCIAL
SECTION**

INDEPENDENT AUDITORS' REPORT

May 28, 2019

Honorable Mayor and City Council
City of Pequot Lakes, Minnesota

Report on the Financial Statements

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

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

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 Pequot Lakes, Minnesota as of December 31, 2018, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

Change in Accounting Principle

As discussed in Note 1.G. to the financial statements, the City of Pequot Lakes, Minnesota has adopted Governmental Standards Board Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. Our opinions are not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis, Budgetary Comparison Schedules, Schedule of City's Proportionate Share of the Net Pension Liability, Schedule of City Pension Contributions, Schedule of Changes in Net Pension Liability (Asset), and Schedule of Changes in City's Net OPEB Liability be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Supplementary Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's basic financial statements. The Introductory Section, Combining Nonmajor Fund Financial Statements and Schedule of Indebtedness, as listed in the table of contents, are presented for the purposes of additional analysis and are not a required part of the basic financial statements.

The Introductory Section, Combining Nonmajor Fund Financial Statements and Schedule of Indebtedness have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated May 28, 2019 on our consideration of the City of Pequot Lakes' internal control over financial reporting and 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 effectiveness of the City's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City of Pequot Lakes' internal control over financial reporting and compliance.

Report on Other Legal and Regulatory Requirements

In accordance with Minnesota Statutes, we have also issued our report dated May 28, 2019 on our consideration of the City of Pequot Lakes' compliance with provisions of the *Minnesota Legal Compliance Audit Guide for Cities*, promulgated by the State Auditor pursuant to Minnesota Statute Section 6.65. The purpose of the report is to determine if the City has complied with Minnesota laws and regulations. That report is an integral part of an audit performed in the State of Minnesota.

SCHLENNER WENNER & CO.
St. Cloud, Minnesota

**REQUIRED SUPPLEMENTARY
INFORMATION**

**CITY OF PEQUOT LAKES, MINNESOTA
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2018**

Our discussion and analysis of the City of Pequot Lakes' financial performance provides an overview of the City's financial activities for the year ended December 31, 2018. Please read it in conjunction with the independent auditor's report on page two and the City's financial statements, which begin on page fourteen.

FINANCIAL HIGHLIGHTS

- The City's net position increased \$5,737,620 compared to the prior year as a result of this year's operations.
- The City recorded a change in accounting principle in the current year for the implementation of Governmental Accounting Standards Board Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. The implementation of this standard increased beginning net position in the government-wide statements by \$112,353.
- In the City's business-type activities, revenues decreased \$18,478 (or 2.86 percent) and program expenses increased \$53,845 (or 14.96 percent). The decrease in revenues is due primarily to a decrease in sewer access charges in the Sewer Fund. The increase in expenses is due to various increases in operational costs.
- Total cost of all of the City's programs increased \$146,722 (or 5.39 percent).
- The City of Pequot Lakes received local government aid in the amount of \$20,029.
- The City's General Fund generated less revenue than budgeted of \$1,924,821, excluding transfers in from other funds. Expenditures were less than budgeted by \$5,319,784, excluding transfers to other funds. Such variances are primarily the result of differences between the amount of debt which was expected to be issued for capital outlay, versus the actual amount of debt issued and capital outlay expenditures incurred throughout the year. See additional details related to debt starting on page thirty-eight.

USING THIS ANNUAL REPORT

This annual report consists of series of financial statements. The Statement of Net Position and the Statement of Activities (on pages fourteen and fifteen) provide information about the activities of the City as a whole and present a longer-term view of the City's finances. Fund financial statements start on page sixteen. These statements tell how governmental activity services were financed in the short term as well as what remains for future spending. Fund financial statements also report the City's operations in more detail than the government-wide statements by providing information about the City's most significant funds.

Reporting the City as a Whole

Our analysis of the City as a whole begins on page seven. One of the most important questions asked about the City's finances is, "Is the City as a whole better off or worse off as a result of the year's activities?" The Statement of Net Position and the Statement of Activities report information about the City as a whole and about its activities in a way that helps answer this question. These statements include all assets, deferred outflows/inflows of resources, and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the City's net position and changes in net position. You can think of the City's net position (assets plus deferred outflows, less liabilities plus deferred inflows) as one way to measure the City's financial health, or financial position. Over time, increases or decreases in the City's net position are one indicator of whether its financial health is improving or deteriorating. You will need to consider other nonfinancial factors, however, such as changes in the City's property tax base, costs associated with current and future construction projects, and the condition of the City's roads in order to assess the overall health of the City.

**CITY OF PEQUOT LAKES, MINNESOTA
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2018**

USING THIS ANNUAL REPORT (Continued)

Reporting the City as a Whole (Continued)

In the Statement of Net Position and the Statement of Activities, we divide the City into two kinds of activities:

- **Governmental Activities** – Most of the City's basic services are reported here, including the police, fire, public works, parks departments and general administration. Property taxes, special assessments, licenses, permits and fees and state aids finance most of these activities.
- **Business-type Activities** – The City charges a fee to customers to help it cover all or most of the cost of certain services it provides. The City's water and sewer systems are reported here.

Reporting the City's Most Significant Funds

Our analysis of the City's major funds begins on page ten. The fund financial statements begin on page sixteen and provide detailed information about the most significant funds - not the City as a whole. Some funds are required to be established by State law and by bond covenants. However, the City Council may establish other funds to help it control and manage money for particular purposes or to show that it is meeting legal responsibilities for using certain taxes, grants and other money. The City's two kinds of funds (governmental and proprietary) use different accounting approaches.

- **Governmental Funds** – Most of the City's basic services are reported in governmental funds, which focus on how money flows into and out of those funds and the balances left at year-end that are available for spending. These funds are reported using an accounting method called modified accrual accounting, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund statements provide a detailed, short-term view of the City's general government operations and the basic services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the City's programs. We describe the relationship (or differences) between governmental activities (reported in the Statement of Net Position and the Statement of Activities) and governmental funds in reconciliations following the governmental fund financial statements.
- **Proprietary Funds** – When the City charges customers for the services it provides, these services are generally reported in proprietary funds. Proprietary funds are reported in the same way that all activities are reported in the Statement of Net Position and the Statement of Activities. In fact, the City's enterprise funds are the same as the business-type activities we report in the government-wide statements but provide more detail and additional information, such as cash flows, for proprietary funds.

**CITY OF PEQUOT LAKES, MINNESOTA
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2018**

THE CITY AS A WHOLE

The City's combined net position increased \$5,849,973 from a year ago. Our analysis below focuses on the net position (Table 1) and changes in net position (Table 2) of the City's governmental and business-type activities.

**Table 1
Net Position**

	Governmental Activities		Business-Type Activities		Total Government	
	2018	2017	2018	2017	2018	2017
Current Assets	\$ 6,719,030	\$ 3,093,943	\$ 2,013,722	\$ 1,857,894	\$ 8,732,752	\$ 4,951,837
Noncurrent Assets	9,587,286	7,765,508	2,842,892	2,809,934	12,430,178	10,575,442
Total Assets	16,306,316	10,859,451	4,856,614	4,667,828	21,162,930	15,527,279
Deferred Outflows of Resources	612,929	802,362	5,572	6,558	618,501	808,920
Current Liabilities	277,069	237,630	220,948	170,787	498,017	408,417
Noncurrent Liabilities	1,237,109	1,572,031	888,765	952,986	2,125,874	2,525,017
Total Liabilities	1,514,178	1,809,661	1,109,713	1,123,773	2,623,891	2,933,434
Deferred Inflows of Resources	913,804	1,009,764	8,318	7,556	922,122	1,017,320
Net Position:						
Net Investment in						
Capital Assets	8,499,823	6,597,011	1,929,950	1,836,276	10,429,773	8,433,287
Restricted	126,453	94,559	-	-	126,453	94,559
Unrestricted	5,864,987	2,150,818	1,814,205	1,706,781	7,679,192	3,857,599
Total Net Position	<u>\$ 14,491,263</u>	<u>\$ 8,842,388</u>	<u>\$ 3,744,155</u>	<u>\$ 3,543,057</u>	<u>\$ 18,235,418</u>	<u>\$ 12,385,445</u>

The net position of the City's governmental activities increased by \$5,648,875 (63.88 percent). Unrestricted net position (the part of net position that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation, or other legal requirements) increased by \$3,714,169 compared to the prior year.

The net position of the City's business-type activities increased by \$201,098 (5.68 percent) from the prior year. Such increase can be attributed to the results of current year operations.

**CITY OF PEQUOT LAKES, MINNESOTA
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2018**

THE CITY AS A WHOLE (Continued)

**Table 2
Changes in Net Position**

	Governmental Activities		Business-Type Activities		Total Government	
	2018	2017	2018	2017	2018	2017
REVENUE						
Charges for Services	\$ 329,816	\$ 347,771	\$ 592,784	\$ 624,668	\$ 922,600	\$ 972,439
Operating Grants and Contributions	149,284	138,418	-	-	149,284	138,418
Capital Grants and Contributions	5,586,322	782,000	-	-	5,586,322	782,000
Taxes	1,604,118	1,613,181	-	-	1,604,118	1,613,181
Tax Increment	-	29,083	-	-	-	29,083
Intergovernmental	61,995	40,415	294	144	62,289	40,559
Unrestricted Investment Income	78,712	30,257	23,967	16,248	102,679	46,505
Other	199,543	120,161	9,742	4,205	209,285	124,366
Total Revenues	8,009,790	3,101,286	626,787	645,265	8,636,577	3,746,551
PROGRAM EXPENSES						
General Government	538,889	557,236	-	-	538,889	557,236
Public Safety	1,016,110	980,807	-	-	1,016,110	980,807
Public Works	594,661	559,906	-	-	594,661	559,906
Parks and Recreation	180,722	180,998	-	-	180,722	180,998
Economic Development	100,705	57,841	-	-	100,705	57,841
Debt Service	22,865	24,287	-	-	22,865	24,287
Water	-	-	260,754	203,779	260,754	203,779
Sewer	-	-	152,977	156,107	152,977	156,107
Total Expenses	2,453,952	2,361,075	413,731	359,886	2,867,683	2,720,961
Gain (Loss) on Disposal of Assets	(33,774)	4,992	2,500	-	(31,274)	4,992
Transfers	21,198	(5,000)	(21,198)	5,000	-	-
Change in Net Position	5,543,262	740,203	194,358	290,379	5,737,620	1,030,582
Net Position - Beginning of Year	8,842,388	8,102,185	3,543,057	3,252,678	12,385,445	11,354,863
Change in Accounting Principle	105,613	-	6,740	-	112,353	-
Net Position - End of Year	<u>\$14,491,263</u>	<u>\$ 8,842,388</u>	<u>\$ 3,744,155</u>	<u>\$ 3,543,057</u>	<u>\$18,235,418</u>	<u>\$12,385,445</u>

The City's total revenues increased by \$4,890,026 (130.52 percent) from the prior year, largely due to revenues from State and County contributions. During 2018, the City accepted ownership of three roadways within city limits at a combined value of approximately \$977,000, which were previously the property of the State and County. As compensation for accepting the responsibility for the maintenance and future repairs of these roadways, the City also received a cash payment of \$4,604,000.

**CITY OF PEQUOT LAKES, MINNESOTA
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2018**

THE CITY AS A WHOLE (Continued)

The total cost of all programs and services increased by \$146,722 (5.39 percent). The most significant factor driving this increase was the increase in economic development expenditures recognized in the Governmental Funds, along with an increase in water program expenses.

Our following analysis separately considers the operations of governmental and business-type activities.

Governmental Activities

Revenue for the City's governmental activities increased by \$4,908,504 (158.27 percent), primarily due to the increase in capital grants and contributions previously discussed. Total expenses increased \$92,877 (3.93 percent), largely due to increased professional service expenditures in the current year.

Table 3 presents the cost of each of the City's programs (general government, public safety, public works, parks and recreation, economic development and debt service)-as well as each program's net cost (total cost less revenues generated by the activities). The net cost shows the financial burden that was placed on the City's taxpayers by each of these functions. Activities (net of capital outlay which is excluded from Table 3) were generally comparable to the prior year as operations remained fairly consistent with the prior year, with the exception of:

- Public safety net cost of services increased due to a decrease in charges for services revenue along with increases in various operating costs in the current year.
- Public works experienced net revenue from services due to the State and County contributions previously discussed.
- Economic Development net cost of services increased primarily due to increased engineering costs in the current year.

**Table 3
Governmental Activities**

	Total Cost of Services		Net Cost (Revenue) of Services	
	2018	2017	2018	2017
General Government	\$ 538,889	\$ 558,619	\$ 467,171	\$ 486,488
Public Safety	1,016,110	980,807	629,801	578,858
Public Works	594,661	559,906	(5,001,836)	(227,050)
Parks and Recreation	180,722	180,998	169,824	173,845
Economic Development	100,705	57,841	100,705	57,841
Debt Service	22,865	22,904	22,865	22,904
Totals	\$ 2,453,952	\$ 2,361,075	\$ (3,611,470)	\$ 1,092,886

Business-type Activities

Revenues of the City's business-type activities (see Table 2) decreased by \$18,478 (2.86 percent) and program expenses increased by \$53,845 (14.96 percent). The decrease in revenues is due primarily to a decrease in sewer access charges in the Sewer Fund. The increase in expenses is due to an increase in professional services in the Water Fund.

**CITY OF PEQUOT LAKES, MINNESOTA
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2018**

THE CITY'S FUNDS

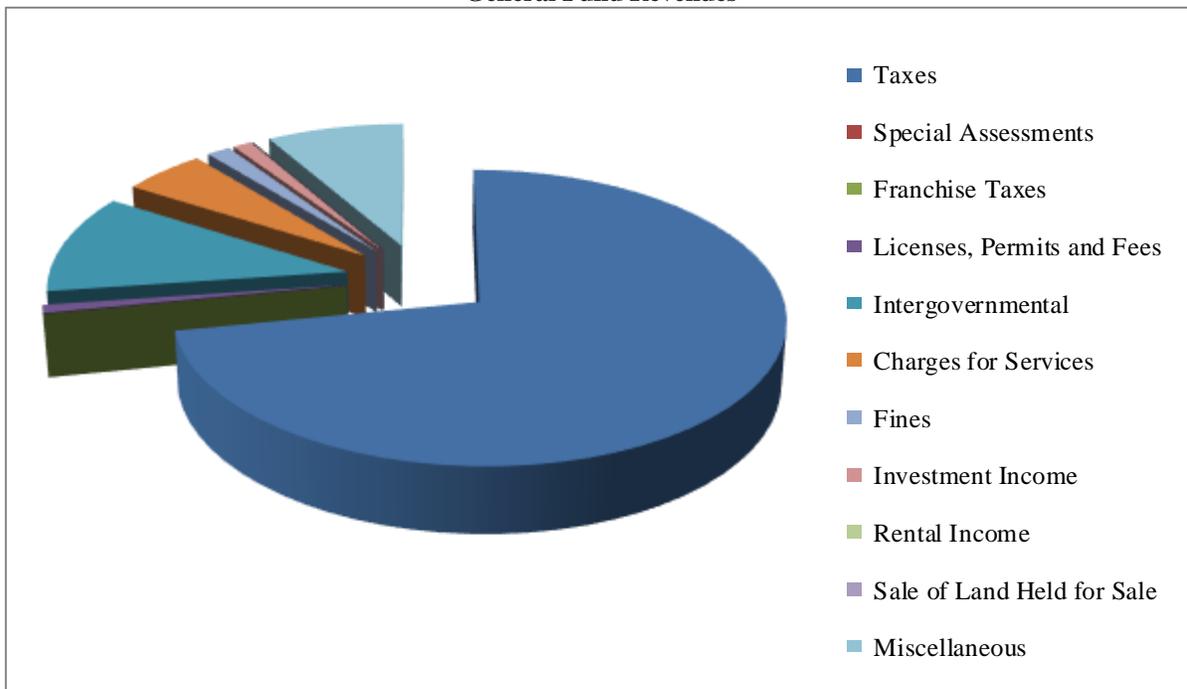
Governmental Funds

As the City completed the year, its governmental funds (as presented in the balance sheet on page sixteen) reported a combined fund balance of \$6,470,895. This is an increase of \$3,652,309 from the prior year. Operations were comparable to the prior year, with the exception of an increase in intergovernmental revenue from the capital contribution for future roadway maintenance and reconstruction received in the Highway 371 Project Fund. Financial information specific to the governmental funds is detailed in the following pages. Such information was derived from the fund financials. The following is a summary of the City's major governmental funds:

Major Fund	Fund Balance December 31,		Increase (Decrease)
	2018	2017	
General	\$ 570,590	\$ 1,441,827	\$ (871,237)

The fund balance of the General Fund decreased by \$871,237 compared to 2017. Overall, operations were generally consistent year-to-year, with the exception of an increase in intergovernmental and donation revenue, an increase in capital outlay and public safety expenditures, along with fewer expenditures incurred for parks and recreation and transfers out in the current year. Details of the General Fund's revenues and expenditures are displayed below:

General Fund Revenues



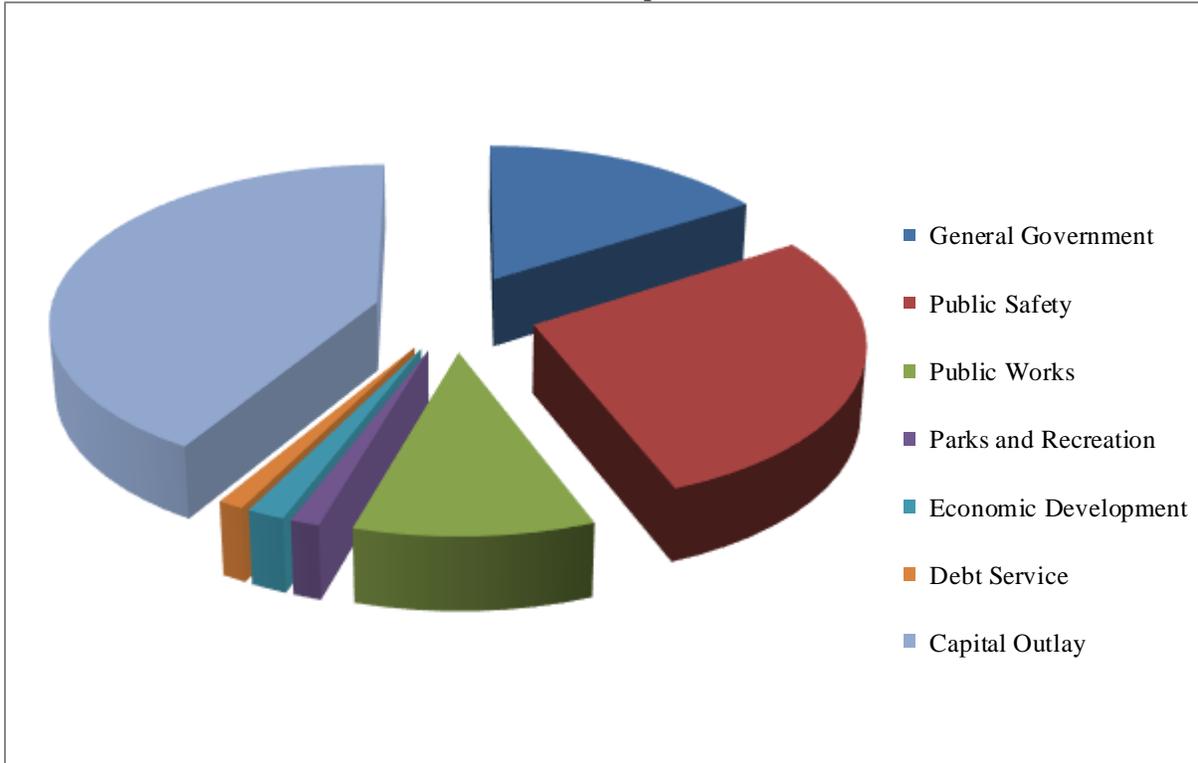
The City receives the majority of its funding in the General Fund in the form of taxes (71.90 percent), funding received from other governmental agencies (11.18 percent) and miscellaneous (8.34 percent). Overall, the City's General Fund revenues were comparable to the prior year.

**CITY OF PEQUOT LAKES, MINNESOTA
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2018**

THE CITY'S FUNDS (Continued)

Governmental Funds (Continued)

General Fund Expenditures



A significant portion of the City's General Fund expenditures were used for capital outlay (41.39 percent). Remaining expenditures are used primarily for public safety (28.18 percent), general government operations (15.95 percent), and public works (10.44 percent). Expenditures are comparable to the prior year, with the exception of changes discussed on the previous page.

Major Fund	Fund Balance December 31,		Increase (Decrease)
	2018	2017	
Fire Department Fund	\$ 124,244	\$ 108,445	\$ 15,799

The Fire Department fund balance increased primarily as a result of an increase in charges for services along with a decrease in capital outlay expenditures in the current year.

Major Fund	Fund Balance December 31,		Increase (Decrease)
	2018	2017	
Highway 371 Project Fund	\$ 5,311,231	\$ 782,468	\$ 4,528,763

The Highway 371 Project fund balance increased as a result of significant capital contributions received from the State of Minnesota and Crow Wing County.

**CITY OF PEQUOT LAKES, MINNESOTA
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2018**

THE CITY'S FUNDS (Continued)

General Fund Budgetary Highlights

The City's General Fund generated less revenue than budgeted of \$1,924,821, excluding transfers in from other funds. Expenditures were also less than those budgeted by \$5,319,784, excluding transfers to other funds. As previously discussed, such variances pertain primarily to differences between the manner in which debt issuance and capital outlay activities were budgeted, in comparison with the actual activity.

Proprietary Funds

As the City completed the year, its business-type activities reported a combined net position of \$3,744,155. This is an increase of \$201,098 from the prior year. The following is a summary of the City's major proprietary funds:

Major Fund	Net Position December 31,		Increase (Decrease)
	2018	2017	
Water	\$ 1,041,480	\$ 1,015,301	\$ 26,179
Sewer	\$ 2,702,675	\$ 2,527,756	\$ 174,919

The Water Fund and Sewer Fund net position increased due revenues exceeding expenses and the results of current year operations.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

At the end of 2018, the City had \$11,946,225 net investment in a broad range of capital assets, including machinery and equipment, buildings, improvements and infrastructure. This amount represents a net increase of \$1,840,774 (18.22 percent) from last year. More detailed information about the City's capital assets is presented in the notes to the financial statements, starting on page thirty-six.

**Table 4
Capital Assets Net of Depreciation**

	Governmental Activities		Business-Type Activities		Totals	
	2018	2017	2018	2017	2018	2017
Land	\$ 1,596,318	\$ 1,504,339	\$ 156,969	\$ 156,969	\$ 1,753,287	\$ 1,661,308
Construction In Progress	956,498	100,779	24,570	-	981,068	100,779
Buildings and Improvements	898,221	878,724	52,944	56,852	951,165	935,576
Machinery, Furniture and Equipment	1,574,926	1,465,795	1,303,657	1,252,401	2,878,583	2,718,196
Infrastructure	4,077,370	3,345,880	1,304,752	1,343,712	5,382,122	4,689,592
Total Capital Assets	\$ 9,103,333	\$ 7,295,517	\$ 2,842,892	\$ 2,809,934	\$ 11,946,225	\$ 10,105,451

**CITY OF PEQUOT LAKES, MINNESOTA
MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2018**

CAPITAL ASSET AND DEBT ADMINISTRATION (Continued)

Debt

At year-end, the City had \$1,516,452 in gross debt versus \$1,672,164 last year (a decrease of 9.31 percent), as shown in Table 5. See additional information regarding the current year issuances on page thirty-eight of the financial statements.

**Table 5
Outstanding Debt at Year-End**

	Governmental Activities		Business-Type Activities		Totals	
	2018	2017	2018	2017	2018	2017
Bonds Payable	\$ -	\$ -	\$ 911,600	\$ 971,738	\$ 911,600	\$ 971,738
Equipment Certificates	165,900	214,250	-	-	165,900	214,250
Loans Payable	273,537	293,650	-	-	273,537	293,650
Capital Leases	164,073	190,606	1,342	1,920	165,415	192,526
Totals	\$ 603,510	\$ 698,506	\$ 912,942	\$ 973,658	\$ 1,516,452	\$ 1,672,164

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

City has continued to work on the design of the Trailside Park Improvement project and plans to add amenities in 2019-2020. In 2018, the City completed the Maintenance Facility and Storage Shed. The City has also started the planning and design process of the Rasmussen Road Reconstruction Project in 2018 and plans to start construction in 2020.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have questions about this report or need additional financial information, contact City Hall at 4638 Main Street, Pequot Lakes, MN 56472 or by phone at (218) 568-5222.

BASIC FINANCIAL STATEMENTS

CITY OF PEQUOT LAKES, MINNESOTA
STATEMENT OF NET POSITION
DECEMBER 31, 2018

	Governmental Activities	Business-Type Activities	Total
ASSETS			
Cash, Cash Equivalents and Investments	\$ 6,496,041	\$ 1,872,910	\$ 8,368,951
Property Taxes Receivable	136,693	-	136,693
Assessments Receivable	19,765	1,766	21,531
Accounts Receivable	4,587	139,046	143,633
Interest Receivable	39	-	39
Due from Other Governments	487	-	487
Debt Reserve Restricted Cash	14,436	-	14,436
Land Held For Resale	46,982	-	46,982
Noncurrent Assets:			
Capital Assets not Being Depreciated	2,552,816	181,539	2,734,355
Capital Assets Being Depreciated (Net)	6,550,517	2,661,353	9,211,870
Net Pension Asset	483,953	-	483,953
TOTAL ASSETS	16,306,316	4,856,614	21,162,930
DEFERRED OUTFLOWS OF RESOURCES			
Pensions	612,929	5,572	618,501
LIABILITIES			
Accounts Payable	88,571	148,973	237,544
Accrued Salaries	29,725	1,402	31,127
Due to Other Governments	1,357	108	1,465
Accrued Interest	9,705	9,554	19,259
Other Liabilities	11,222	-	11,222
Noncurrent Liabilities:			
Long-term Debt, Due Within One Year	117,876	60,638	178,514
Long-term Debt, Due After One Year	485,634	852,304	1,337,938
Compensated Absences Due Within One Year	18,613	273	18,886
Compensated Absences Due After One Year	27,480	315	27,795
Net OPEB Liability	110,904	7,078	117,982
Net Pension Liability	613,091	29,068	642,159
TOTAL LIABILITIES	1,514,178	1,109,713	2,623,891
DEFERRED INFLOWS OF RESOURCES			
Pensions	913,804	8,318	922,122
NET POSITION			
Net Investment in Capital Assets	8,499,823	1,929,950	10,429,773
Restricted	126,453	-	126,453
Unrestricted	5,864,987	1,814,205	7,679,192
TOTAL NET POSITION	\$ 14,491,263	\$ 3,744,155	\$ 18,235,418

**CITY OF PEQUOT LAKES, MINNESOTA
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2018**

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Position		
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Primary Government		Total
					Governmental Activities	Business-Type Activities	
Governmental Activities:							
General Government	\$ 538,889	\$ 65,488	\$ 6,230	\$ -	\$ (467,171)	\$ -	\$ (467,171)
Public Safety	1,016,110	258,056	128,253	-	(629,801)	-	(629,801)
Public Works	594,661	374	14,801	5,581,322	5,001,836	-	5,001,836
Parks and Recreation	180,722	5,898	-	5,000	(169,824)	-	(169,824)
Economic Development	100,705	-	-	-	(100,705)	-	(100,705)
Debt Service	22,865	-	-	-	(22,865)	-	(22,865)
Total Governmental Activities	2,453,952	329,816	149,284	5,586,322	3,611,470	-	3,611,470
Business-Type Activities:							
Water	260,754	294,006	-	-	-	33,252	33,252
Sewer	152,977	298,778	-	-	-	145,801	145,801
Total Business-Type Activities	413,731	592,784	-	-	-	179,053	179,053
TOTALS	\$ 2,867,683	\$ 922,600	\$ 149,284	\$ 5,586,322	3,611,470	179,053	3,790,523
General Revenues (Expenses):							
Taxes					1,604,118	-	1,604,118
Intergovernmental					61,995	294	62,289
Investment Income					78,712	23,967	102,679
Miscellaneous					199,543	9,742	209,285
Gain (Loss) on Disposal of Assets					(33,774)	2,500	(31,274)
Total General Revenues (Expenses)					1,910,594	36,503	1,947,097
Transfers					21,198	(21,198)	-
Total General Revenues (Expenses) and Transfers					1,931,792	15,305	1,947,097
CHANGE IN NET POSITION					5,543,262	194,358	5,737,620
NET POSITION - BEGINNING OF YEAR					8,842,388	3,543,057	12,385,445
CHANGE IN ACCOUNTING PRINCIPLE					105,613	6,740	112,353
NET POSITION - END OF YEAR					\$ 14,491,263	\$ 3,744,155	\$ 18,235,418

**CITY OF PEQUOT LAKES, MINNESOTA
BALANCE SHEET
GOVERNMENTAL FUNDS
DECEMBER 31, 2018**

	General Fund	Fire Department	Highway 371 Project	Total Nonmajor Governmental Funds	Total Governmental Funds
ASSETS					
Cash, Cash Equivalents and Investments	\$ 1,550,261	\$ 118,012	\$ 4,402,451	\$ 425,317	\$ 6,496,041
Property Taxes Receivable	133,054	-	-	3,639	136,693
Assessments Receivable	19,765	-	-	-	19,765
Accounts Receivable	3,812	775	-	-	4,587
Due from Other Governments	487	-	-	-	487
Accrued Interest	39	-	-	-	39
Debt Reserve Restricted Cash	-	14,436	-	-	14,436
Land Held for Resale	-	-	-	46,982	46,982
Advances to Other Funds	-	-	908,780	-	908,780
	<u> </u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
TOTAL ASSETS	<u>\$ 1,707,418</u>	<u>\$ 133,223</u>	<u>\$ 5,311,231</u>	<u>\$ 475,938</u>	<u>\$ 7,627,810</u>
LIABILITIES					
Accounts Payable	\$ 71,092	\$ 8,979	\$ -	\$ 8,500	\$ 88,571
Accrued Salaries	29,725	-	-	-	29,725
Due to Other Governments	1,357	-	-	-	1,357
Other Liabilities	11,222	-	-	-	11,222
Advances from Other Funds	908,780	-	-	-	908,780
Total Liabilities	<u>1,022,176</u>	<u>8,979</u>	<u>-</u>	<u>8,500</u>	<u>1,039,655</u>
DEFERRED INFLOWS OF RESOURCES					
Unavailable Revenue:					
Property Taxes	94,887	-	-	2,608	97,495
Special Assessments	19,765	-	-	-	19,765
Total Deferred Inflows of Resources	<u>114,652</u>	<u>-</u>	<u>-</u>	<u>2,608</u>	<u>117,260</u>
FUND BALANCES					
Nonspendable	-	-	908,780	46,982	955,762
Restricted	63,887	14,436	-	50,115	128,438
Committed	317,801	109,808	4,402,451	367,733	5,197,793
Unassigned	188,902	-	-	-	188,902
Total Fund Balances	<u>570,590</u>	<u>124,244</u>	<u>5,311,231</u>	<u>464,830</u>	<u>6,470,895</u>
TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND FUND BALANCES	<u>\$ 1,707,418</u>	<u>\$ 133,223</u>	<u>\$ 5,311,231</u>	<u>\$ 475,938</u>	<u>\$ 7,627,810</u>

**CITY OF PEQUOT LAKES, MINNESOTA
RECONCILIATION OF THE BALANCE SHEET-GOVERNMENTAL FUNDS
TO THE STATEMENT OF NET POSITION
DECEMBER 31, 2018**

Total Fund Balance for Governmental Funds	\$	6,470,895
Amounts reported for governmental activities in the Statement of Net Position are different because:		
Capital assets (net of accumulated depreciation of \$5,567,350) used in governmental activities are not financial resources and, therefore, are not reported in the funds:		9,103,333
The net pension asset/liability and related deferred inflows/outflows of resources represent the allocation of pension obligations to the City. Such balances are not reported in the funds:		
Net Pension Asset	\$ 483,953	
Net Pension Liability	(613,091)	
Deferred Outflows - Pensions	612,929	
Deferred Inflows - Pensions	<u>(913,804)</u>	
		(430,013)
Other long-term assets are not available to pay for current-period expenditures and, therefore, are reported as unavailable in the funds:		
Taxes Receivable	97,495	
Special Assessments Receivable	<u>19,765</u>	
		117,260
Interest payable on long-term debt does not require current financial resources and, therefore, is not reported as a liability in the governmental funds Balance Sheet:		(9,705)
Long-term liabilities are not due and payable in the current period and, therefore, they are not reported in the governmental funds Balance Sheet:		
Compensated Absences	(46,093)	
Other Postemployment Benefit Liability	(110,904)	
Long-term Debt Due Within One Year	(117,876)	
Long-term Debt Due In More Than One Year	<u>(485,634)</u>	
		<u>(760,507)</u>
TOTAL NET POSITION OF GOVERNMENTAL ACTIVITIES	\$	<u>14,491,263</u>

CITY OF PEQUOT LAKES, MINNESOTA
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2018

	General Fund	Fire Department	Highway 371 Project	Total Nonmajor Governmental Funds	Total Governmental Funds
REVENUES					
Taxes	\$ 1,515,188	\$ -	\$ 93,170	\$ 43,120	\$ 1,651,478
Licenses, Permits and Fees	18,810	-	-	-	18,810
Intergovernmental	235,693	25,434	4,604,000	-	4,865,127
Charges for Services	107,597	206,770	-	1,600	315,967
Fines	30,373	-	-	-	30,373
Investment Income	23,951	2,409	46,886	5,466	78,712
Miscellaneous	175,647	30,491	-	1	206,139
TOTAL REVENUES	<u>2,107,259</u>	<u>265,104</u>	<u>4,744,056</u>	<u>50,187</u>	<u>7,166,606</u>
EXPENDITURES					
Current:					
General Government	474,942	-	-	299	475,241
Public Safety	839,233	150,005	-	257	989,495
Public Works	310,989	-	9,848	286	321,123
Parks and Recreation	37,979	-	-	-	37,979
Economic Development	48,966	-	-	51,739	100,705
Debt Service:					
Principal	26,533	29,213	-	39,250	94,996
Interest and Other Charges	7,027	16,176	-	1,491	24,694
Capital Outlay	1,232,827	64,852	205,445	-	1,503,124
TOTAL EXPENDITURES	<u>2,978,496</u>	<u>260,246</u>	<u>215,293</u>	<u>93,322</u>	<u>3,547,357</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	(871,237)	4,858	4,528,763	(43,135)	3,619,249
OTHER FINANCING SOURCES					
Proceeds from the Sale of Assets	-	10,941	-	921	11,862
Operating Transfers In	-	-	-	21,198	21,198
TOTAL OTHER FINANCING SOURCES	<u>-</u>	<u>10,941</u>	<u>-</u>	<u>22,119</u>	<u>33,060</u>
NET CHANGE IN FUND BALANCES	(871,237)	15,799	4,528,763	(21,016)	3,652,309
FUND BALANCE - BEGINNING	<u>1,441,827</u>	<u>108,445</u>	<u>782,468</u>	<u>485,846</u>	<u>2,818,586</u>
FUND BALANCE - ENDING	<u>\$ 570,590</u>	<u>\$ 124,244</u>	<u>\$ 5,311,231</u>	<u>\$ 464,830</u>	<u>\$ 6,470,895</u>

**CITY OF PEQUOT LAKES, MINNESOTA
RECONCILIATION OF CHANGES IN FUND BALANCE OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2018**

Net Change in Fund Balances - Total Governmental Funds \$ 3,652,309

Amounts reported for governmental activities in the Statement of Activities are different due to the following:

Governmental funds report capital outlays as expenditures while governmental activities report depreciation expense to allocate those expenditures over the life of the assets:

Capital Outlay Capitalized	\$ 1,380,336	
Transfer of Capital Assets from Other Governments	977,321	
Loss on Disposal	(45,635)	
Depreciation Expense	<u>(504,206)</u>	1,807,816

Revenues in Statement of Activities that do not provide current financial resources are not reported as revenues in the funds:

Change in Long-term Receivables	(45,855)
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Proceeds from the issuance of long-term debt is an other financing source in the governmental funds, while repayment of debt principal is an expenditure in the governmental funds. However, neither transaction has any effect on net position:

Debt Principal Payments	94,996
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Net change in accrued interest on bonds is not reported as expenditures in the funds: 1,829

Net pension asset/liability balances do not represent the impending use of current resources. Therefore, the change in this asset/liability and the related deferrals is not reported in the governmental funds: 57,981

Some expenses reported in the Statement of Activities do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds:

Change in Accrued Compensated Absences	2,318	
Change in Other Postemployment Benefits	<u>(28,132)</u>	<u>(25,814)</u>

CHANGE IN NET POSITION OF GOVERNMENTAL ACTIVITIES \$ 5,543,262

CITY OF PEQUOT LAKES, MINNESOTA
STATEMENT OF NET POSITION
PROPRIETARY FUNDS
DECEMBER 31, 2018

	Water Fund	Sewer Fund	Totals
ASSETS			
Current Assets			
Cash and Cash Equivalents	\$ 823,529	\$ 1,049,381	\$ 1,872,910
Assessments Receivable	883	883	1,766
Accounts Receivable	51,285	87,761	139,046
Total Current Assets	875,697	1,138,025	2,013,722
Noncurrent Assets			
Capital Assets Not Depreciated	24,570	156,969	181,539
Capital Assets Being Depreciated (Net)	1,153,969	1,507,384	2,661,353
Total Noncurrent Assets	1,178,539	1,664,353	2,842,892
TOTAL ASSETS	2,054,236	2,802,378	4,856,614
DEFERRED OUTFLOWS OF RESOURCES			
Pensions	2,786	2,786	5,572
LIABILITIES			
Current Liabilities			
Accounts Payable	70,436	78,537	148,973
Accrued Salaries	701	701	1,402
Due to Other Governments	54	54	108
Accrued Interest	9,554	-	9,554
Compensated Absences	137	136	273
Capital Lease Payable Due Within One Year	319	319	638
Bonds Due Within One Year	60,000	-	60,000
Total Current Liabilities	141,201	79,747	220,948
Noncurrent Liabilities			
Compensated Absences Due After One Year	157	158	315
Capital Lease Payable Due After One Year	352	352	704
Bonds Due After One Year	851,600	-	851,600
Net OPEB Liability	3,539	3,539	7,078
Net Pension Liability	14,534	14,534	29,068
Total Noncurrent Liabilities	870,182	18,583	888,765
TOTAL LIABILITIES	1,011,383	98,330	1,109,713
DEFERRED INFLOWS OF RESOURCES			
Pensions	4,159	4,159	8,318
NET POSITION			
Net Investment in Capital Assets	266,268	1,663,682	1,929,950
Unrestricted	775,212	1,038,993	1,814,205
TOTAL NET POSITION	\$ 1,041,480	\$ 2,702,675	\$ 3,744,155

CITY OF PEQUOT LAKES, MINNESOTA
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2018

	Water Fund	Sewer Fund	Totals
OPERATING REVENUES			
Charges for Services	\$ 285,341	\$ 298,740	\$ 584,081
OPERATING EXPENSES			
Personnel Services	26,640	26,640	53,280
Materials and Supplies	18,972	2,173	21,145
Repairs and Maintenance	9,055	4,213	13,268
Professional Services	89,921	33,483	123,404
Insurance	2,130	3,872	6,002
Utilities	14,400	18,032	32,432
Miscellaneous	11,576	5,462	17,038
Depreciation	64,703	59,102	123,805
TOTAL OPERATING EXPENSES	237,397	152,977	390,374
OPERATING INCOME	47,944	145,763	193,707
NONOPERATING REVENUES (EXPENSES)			
Special Assessments	414	-	414
Intergovernmental	147	147	294
Gain on Disposal of Capital Assets	-	2,500	2,500
Investment Income	10,608	13,359	23,967
Miscellaneous	8,251	9,780	18,031
Interest and Other Charges	(23,357)	-	(23,357)
NET NONOPERATING REVENUES (EXPENSES)	(3,937)	25,786	21,849
CHANGE IN NET POSITION PRIOR TO TRANSFERS	44,007	171,549	215,556
TRANSFERS			
Operating Transfers Out	(21,198)	-	(21,198)
CHANGE IN NET POSITION	22,809	171,549	194,358
NET POSITION - BEGINNING OF YEAR	1,015,301	2,527,756	3,543,057
CHANGE IN ACCOUNTING PRINCIPLE	3,370	3,370	6,740
NET POSITION - END OF YEAR	\$ 1,041,480	\$ 2,702,675	\$ 3,744,155

**CITY OF PEQUOT LAKES, MINNESOTA
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2018**

	<u>Water Fund</u>	<u>Sewer Fund</u>	<u>Totals</u>
CASH FLOWS FROM OPERATING ACTIVITIES			
Cash Received from Customers	\$ 289,181	\$ 305,607	\$ 594,788
Cash Paid to Suppliers	(110,241)	(52,097)	(162,338)
Cash Paid to Employees	<u>(24,435)</u>	<u>(24,435)</u>	<u>(48,870)</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	154,505	229,075	383,580
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES			
Special Assessments, Intergovernmental and Other Revenue	8,902	10,017	18,919
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES			
Purchases of Capital Assets	(56,397)	(97,866)	(154,263)
Payments on Debt Principal	(60,289)	(289)	(60,578)
Cash Paid for Interest	<u>(23,820)</u>	<u>-</u>	<u>(23,820)</u>
NET CASH USED BY CAPITAL AND RELATED FINANCING ACTIVITIES	(140,506)	(98,155)	(238,661)
CASH FLOW FROM INVESTING ACTIVITIES			
Investment Income	<u>10,608</u>	<u>13,359</u>	<u>23,967</u>
Net Change in Cash and Cash Equivalents	33,509	154,296	187,805
Cash and Cash Equivalents – Beginning of Year	<u>790,020</u>	<u>895,085</u>	<u>1,685,105</u>
Cash and Cash Equivalents – End of Year	<u>\$ 823,529</u>	<u>\$ 1,049,381</u>	<u>\$ 1,872,910</u>

CITY OF PEQUOT LAKES, MINNESOTA
STATEMENT OF CASH FLOWS (Continued)
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2018

	Water Fund	Sewer Fund	Totals
RECONCILIATION OF OPERATING INCOME TO			
NET CASH PROVIDED BY OPERATING ACTIVITIES			
Operating Income	\$ 47,944	\$ 145,763	\$ 193,707
Adjustments to Reconcile Operating Income to Net Cash Provided by Operating Activities:			
Depreciation	64,703	59,102	123,805
Change in Assets and Liabilities:			
Accounts Receivable	3,786	6,813	10,599
Accounts Payable	35,813	15,138	50,951
Accrued Salaries	(9)	(9)	(18)
Due to Other Governments	54	54	108
Deferred Outflows of Resources - Pensions	493	493	986
Net Pension Liability	1,440	1,440	2,880
Deferred Inflows of Resources - Pensions	381	381	762
Compensated Absences	(997)	(997)	(1,994)
Other Post Employment Benefits	897	897	1,794
NET CASH PROVIDED BY OPERATING ACTIVITIES	\$ 154,505	\$ 229,075	\$ 383,580
SCHEDULE OF NONCASH CAPITAL AND RELATED			
FINANCING ACTIVITIES			
Amortization of Current Year Bond Premium	\$ 138	\$ -	\$ 138
Transfer of Land Held for Sale to Governmental Funds	\$ (21,198)	\$ -	\$ (21,198)

CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the City of Pequot Lakes (the City), have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental units. GAAP includes all relevant Governmental Accounting Standards Board (GASB) pronouncements.

The City has a mayor-council form of government that is governed by an elected mayor and four-member council. The City provides the following services: water, sewer, public safety (police and fire), public works, parks and recreation, public improvements, planning and zoning and general administrative services.

1.A. FINANCIAL REPORTING ENTITY

The City's financial reporting entity is comprised of the primary governmental unit of the City of Pequot Lakes, Minnesota.

In determining the financial reporting entity, the City complies with the provisions of GASB Statement No. 14, *The Financial Reporting Entity*, and includes all component units of which the City appointed a voting majority of the units' board; the City is either able to impose its will on the unit or a financial benefit or burden relationship exists.

Blended Component Units

Blended component units are separate legal entities that meet the component unit criteria described above and whose governing body is the same or substantially the same as the City Council or the component unit provides services entirely to the City. These component units' funds are blended into those of the City's by appropriate activity type to compose the primary government presentation. Currently, the City has no blended component units.

Discretely Presented Component Units

Discretely presented component units are separate legal entities that meet the component unit criteria described above but do not meet the criteria for blending. Currently, the City has no discretely presented component units.

Related Organizations

The Pequot Lakes Fire Relief Association is organized as a non-profit organization by its members to provide benefits to such members in accordance with Minnesota Statutes. Its Board of Directors is appointed by the membership of the organization. The City has no significant influence over the management, budget or policies of the association. All funding is conducted in accordance with Minnesota Statutes, whereby state aids flow through the City to the Association.

1.B. BASIS OF PRESENTATION

Government-wide Financial Statements

The Statement of Net Position and Statement of Activities display information about the reporting government as a whole. They include all funds of the reporting entity except for fiduciary funds (of which the City has none). The statements distinguish between governmental and business-type activities. Governmental activities generally are financed through taxes, intergovernmental revenues, and other nonexchange revenues. Business-type activities are financed in whole or in part by fees charged to external parties for goods and services.

Fund Financial Statements

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

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

1.B. BASIS OF PRESENTATION (Continued)

Fund Financial Statements (Continued)

A fund is considered major if it is the primary operating fund of the City or meets the following criteria:

- Total assets and deferred outflows of resources, liabilities and deferred inflows of resources, revenues, or expenditures/expenses of that individual governmental or proprietary fund are at least 10 percent of the corresponding total for all funds of that category or type; and
- Total assets and deferred outflows of resources, liabilities and deferred inflows of resources, revenues, or expenditures/expenses of that individual governmental or proprietary fund are at least 5 percent of the corresponding total for all governmental and proprietary funds combined.

The City reports the following major governmental funds:

The *General Fund* is the primary operating fund of the City and is always classified as a major fund. It is used to account for all activities except those legally or administratively required to be accounted for in other funds.

The *Fire Department Fund* is a special revenue fund used to account for funds received by the City for fire department expenses. The City has elected to make this fund major in the current year.

The *Highway 371 Project Fund* is a capital projects fund used to account for financial resources to be used for the acquisition or construction of capital improvements on Highway 371 within the City.

The City reports the following major proprietary funds:

The *Proprietary Funds* are used to account for business-type activities provided to the general public. These activities are financed primarily by user charges and the measurement of financial activity focuses on net income measurement similar to the private sector. The City maintains Water and Sewer Proprietary Funds.

The City reports the following nonmajor fund types:

The *Special Revenue Funds* account for funds received by the City with a specific purpose.

The *Debt Service Funds* account for the accumulation of financial resources for the payment of interest and principal on general long-term debt of the City other than debt service payments made by proprietary funds. Tax Levies and special assessments are used for the payment of principal and interest on the City's indebtedness.

1.C. MEASUREMENT FOCUS AND BASIS OF ACCOUNTING

Measurement focus is a term used to describe "which" transactions are recorded within the various financial statements. Basis of accounting refers to "when" transactions are recorded regardless of the measurement focus applied.

Measurement Focus

On the government-wide Statement of Net Position and the Statement of Activities, both governmental and business-type activities are presented using the *economic resources* measurement focus as defined in the second bullet point on the following page.

CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

1.C. MEASUREMENT FOCUS AND BASIS OF ACCOUNTING (Continued)

Measurement Focus (Continued)

In the fund financial statements, the *current financial resources* measurement focus or the *economic resources* measurement focus is used as appropriate:

- All governmental funds utilize a *current financial resources* measurement focus. Only current financial assets and liabilities are generally included on their balance sheets. Their operating statements present sources and uses of available spendable financial resources during a given period. These funds use fund balance as their measure of available spendable financial resources at the end of the period.
- The government-wide financial statements and proprietary funds utilize an *economic resources* measurement focus. The accounting objectives of this measurement focus are the determination of operating income, changes in net position (or cost recovery), financial position and cash flows. All assets, deferred outflows, liabilities and deferred inflows (whether current or noncurrent) associated with their activities are reported. Proprietary fund equity is classified as net position.

Basis of Accounting

In the government-wide Statement of Net Position and Statement of Activities, both governmental and business-type activities are presented using the *accrual* basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or economic asset used. Revenues, expenses, gains, losses, assets, liabilities and deferred outflows/inflows resulting from exchange and exchange-like transactions are recognized when the exchange takes place.

In the fund financial statements, governmental funds are presented on the *modified accrual* basis of accounting. Under this modified accrual basis of accounting, revenues are recognized when “measurable and available.” Measurable means knowing or being able to reasonable estimate the amount. Available means collectible within the current period or within sixty days after year end. Expenditures (including capital outlay) are recorded when the related fund liability is incurred, except for general obligation bond principal and interest which are reported when due.

All proprietary funds utilize the accrual basis of accounting.

1.D. USE OF ESTIMATES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, deferred outflows of resources, liabilities, and deferred inflows of resources, and disclosure of contingent assets, liabilities, and deferred outflows/inflows of resources at the date of the financial statements. Estimates also affect reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

1.E. ASSETS, LIABILITIES, DEFERRED OUTFLOWS/INFLOWS OF RESOURCES AND EQUITY

Cash, Cash Equivalents and Investments

Cash balances are invested to the extent available in various securities as authorized by Minnesota Statutes. Investment earnings are recorded in the individual fund carrying the investment. Investments are stated at fair value.

Cash equivalents are considered to be short-term, highly-liquid investments that are readily convertible to cash and have original maturities of three months or less.

CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

1.E. ASSETS, LIABILITIES, DEFERRED OUTFLOWS/INFLOWS OF RESOURCES AND EQUITY (Continued)

Cash, Cash Equivalents, and Investments (Continued)

For the purpose of the proprietary fund Statement of Cash Flows, the City considers all cash and investments under the classification of current assets to be cash and cash equivalents. Cash and cash equivalents consist of checking and savings certificate accounts, cash on hand, and money market savings accounts.

See Note 3.A. for additional information related to Cash, Cash Equivalents and Investments.

Interfund Receivables and Payables

During the course of operations, transactions occur between individual funds that may result in amounts owed between funds. Those related to goods and services type transactions are classified as “due to and from other funds.” Short-term interfund loans are reported as “due to and from other funds.” Long-term interfund loans are reported as “advances from and to other funds.” Interfund receivables and payables between funds within governmental activities, as well as interfund receivables and payables between funds within business-type activities, are eliminated in the Statement of Net Position. See Note 3.D. for details of interfund transactions, including receivables and payables at year-end.

Receivables

In the government-wide statements, receivables consist of all revenues earned at year-end and not yet received. Allowances for uncollectible accounts receivable are based upon historical trends and the periodic aging of accounts receivable and not deemed necessary at year end. Major receivable balances for the governmental activities include taxes, special assessments and charges for services. Business-type activities report utility charges and assessments as their major receivables.

In the fund financial statements, material receivables in governmental funds include revenue accruals such as taxes, assessments, other intergovernmental revenues, fines and charges for services since they are usually both measurable and available. Revenues collectible but not available are deferred in the fund financial statements in accordance with modified accrual basis, but not deferred in the government-wide financial statements in accordance with the accrual basis. Interest and investment earnings are recorded when earned only if paid within 60 days since they would be considered both measurable and available. Proprietary fund material receivables consist of all revenues earned at year-end and not yet received. Utility accounts receivable and assessments compose the majority of proprietary fund receivables. Allowance for uncollectible accounts receivable are based upon historical trends and the periodic aging of accounts receivable. No allowances are deemed necessary at year end.

Capital Assets

The accounting treatment over property, plant and equipment (capital assets) depends on whether the assets are used in governmental or proprietary fund operations and whether they are reported in the government-wide or fund financial statements.

Capital assets, which include property, plant, equipment and infrastructure assets (e.g., roads, bridges, sidewalks and similar items) are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets are defined by the City as assets with an initial individual cost of more than \$2,500 and an estimated useful life in excess of one year.

The range of estimated useful lives by type of asset is as follows:

Buildings and Improvements	28-40 years
Infrastructure	10-40 years
Machinery, Furniture and Equipment	5-20 years

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

1.E. ASSETS, LIABILITIES, DEFERRED OUTFLOWS/INFLOWS OF RESOURCES AND EQUITY (Continued)

Capital Assets (Continued)

Government-wide Statements

In the government-wide financial statements, capital outlay expenditures are accounted for as capital assets. All capital assets are valued at historical cost or estimated historical cost if actual is unavailable, except for donated capital assets which are recorded at their estimated acquisition value at the date of donation.

Depreciation of all exhaustible capital assets is recorded as an allocated expense in the Statement of Activities, with accumulated depreciation reflected in the Statement of Net Position. Depreciation is provided over the assets' estimated useful lives using the straight-line method of depreciation.

Fund Financial Statements

In the fund financial statements, capital assets used in governmental fund operations are accounted for as capital outlay expenditures of the governmental fund upon acquisition. Capital assets used in proprietary fund operations are accounted for the same as in the government-wide statements.

Accounts Payable

Payables in the governmental and proprietary funds are composed almost entirely of payables to vendors.

Compensated Absences

Per the City's policy, employees earn vacation from 40 to 160 hours per year, depending on length of service to the City. Employees are permitted to carry over a maximum of 140 hours of vacation leave to the following year. Employees also earn sick leave of one day per month, with the maximum accumulation of 960 hours. All accumulated and unused vacation, and a portion of unused sick leave, is paid out upon retirement or resignation. Unused sick leave is paid out at termination for full-time employees as follows: 10 percent of total unused sick leave for five to nine years of service and 25 percent of unused sick leave if more than ten years of service. All paid time off and compensatory pay are accrued when incurred in the government-wide and proprietary fund financial statements.

A liability for these amounts is reported in governmental funds only if they have matured, for example, as the result of an employee's resignation or retirement. In the event a liability is recorded in the governmental funds, General Fund resources would be used to liquidate the compensated absences.

Long-Term Debt

The accounting treatment of long-term debt depends on whether the assets are used in governmental fund operations or proprietary fund operations and whether they are reported in the government-wide or fund financial statements.

All long-term debt to be repaid from governmental and business-type resources are reported as liabilities in the government-wide statements. The long-term debt consists primarily of bonds, certificates of indebtedness, loans payable and capital leases payable.

Long-term debt for governmental funds is not reported as liabilities in the fund financial statements. The debt proceeds are reported as other financing sources and payment of principal and interest are reported as expenditures. The accounting for proprietary funds is the same in the fund statements as it is in the government-wide statements.

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

1.E. ASSETS, LIABILITIES, DEFERRED OUTFLOWS/INFLOWS OF RESOURCES AND EQUITY (Continued)

Net Pension Asset/Liability

The net pension asset represents the Pequot Lakes Fire Relief Association's net pension asset as of the most recent valuation date. The net pension liability represents the City's allocation of their pro-rata share of the statewide pension plans net pension liability.

PERA

For purposes of measuring the net pension liability, deferred outflows/inflows of resources, and pension expense, information about the 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 end is June 30. For this purpose, plan contributions are recognized as of employer payroll paid dates and benefit payments and refunds are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Deferred Outflows/Inflows of Resources

In addition to assets, the Statements of Net Position reports a separate section for deferred outflows of resources. This element represents a consumption of net position that applies to future periods and, therefore, will not be recognized as an outflow of resources (expense) until that time. The City reports deferred outflows of resources in the government-wide and proprietary fund Statements of Net Position in relation to the activity of the pension funds in which City employees participate.

In addition to liabilities, the Statements of Net Position and Balance Sheet report a separate section for deferred inflows of resources. This element represents an acquisition of net position or fund balance that applies to future periods and, therefore, will not be recognized as an inflow of resources (revenue) until that time. The City reports unavailable revenues as deferred inflows of resources. Unavailable revenues consist of property taxes and special assessments. Accordingly, these amounts are deferred and recognized as inflows of resources in the period that they become available, in accordance with the modified accrual basis of accounting. In addition, the City reports deferred inflows of resources in the government-wide and proprietary fund Statements of Net Position in relation to the activity of pension funds in which City employees participate. Accordingly, such amounts are deferred and recognized as inflows of resources in the period that they become available.

See Note 4 for additional information pertaining to the deferred outflows and deferred inflows recorded to account for pension activities.

Equity Classifications

Government-wide Statements

Equity is classified as net position and displayed in three components:

Net Investment in Capital Assets – Consists of capital assets including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction or improvement of those assets.

Restricted – Consists of net position with constraints placed on the use either by 1) external groups such as creditors, grantors, contributors, or laws or regulations of other governments; or 2) law through constitutional provisions or enabling legislation.

Unrestricted – Remaining balance of net position that does not meet the definition of “restricted” or “net investment in capital assets.”

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

1.E. ASSETS, LIABILITIES, DEFERRED OUTFLOWS/INFLOWS OF RESOURCES AND EQUITY (Continued)

Equity Classifications (Continued)

Government-wide Statements (Continued)

It is the City's policy to consider restricted net position to its depletion before unrestricted net position is applied.

Fund Statements

Governmental Fund Financial Statements – In the fund financial statements, governmental funds report fund balances as either nonspendable, restricted, committed, assigned or unassigned. When the City incurs an expenditure for which it may use either restricted or unrestricted fund balances, it uses restricted fund balances first unless unrestricted fund balances will have to be returned because they were not used. When the City incurs an expenditure for purposes for which amounts in any unrestricted fund balance classification could be used, it uses fund balances in the following order: Committed, assigned, unassigned.

Nonspendable – Includes amounts that cannot be spent because they are either not in spendable form, or legally or contractually required to be maintained intact. The nonspendable fund balances at December 31, 2018 consist of land held for resale and advances made to other funds.

Restricted – That portion of fund balance which is not available for appropriation or which has been legally segregated for a specific purpose.

Committed – Amounts that can only be used for specific purposes pursuant to constraints imposed by formal action of the City Council, which is the highest level of decision making authority. Committed amounts cannot be used for any other purpose unless the City Council modifies or rescinds the commitment by resolution.

Assigned – Amounts that are constrained by the City's intent to be used for specific purposes, but are neither restricted nor committed. The authority to assign fund balance has not been formally delegated by the City Council.

Unassigned – This classification represents fund balance that has not been assigned to other funds and that has not been restricted, committed or assigned to specific purposes within the General Fund. At the end of each year, it is the City's policy that up to 50 percent of the following year's general fund budgeted expenditures will be set aside in the General Fund's fund balance for cash flow purposes.

See Note 3.E. for additional disclosures.

Proprietary Fund Financial Statements – Proprietary fund equity is classified the same as in the government-wide statements, as described above.

1.F. REVENUES, EXPENDITURES AND EXPENSES

Property Tax

Under State law, municipalities are limited in their ability to levy a property tax. The City levies its property tax for the subsequent year during the month of December. Crow Wing County is the collecting agency for the levy and remits the collections to the City. In the fund financial statements, property taxes are recorded as revenue in the period levied to the extent they are collected within 60 days of year-end.

CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

1.F. REVENUES, EXPENDITURES AND EXPENSES (Continued)

Property Tax (Continued)

November 30th is the last day the City can certify a tax levy to the County for collection the following year. The County creates the tax list for all taxable property in the City and applies the applicable tax rate to the tax capacity of individual properties to arrive at the actual tax for each property. The County also collects all special assessments, except for certain prepayments paid directly to the City. The County collects all taxes and assessments, except as noted above. The County mails copies of all real estate and personal property tax statements. Each year, property owners are required to pay one half of their real estate taxes by May 15 and the balance by October 15. Penalties and interest are assessed to property owners who do not pay their property taxes and special assessments by the due dates.

Delinquent taxes receivable include the past six years' uncollected taxes. Delinquent taxes have been offset by deferred inflows of resources for taxes not received within 60 days after year end in the fund financial statements.

Operating Revenues and Expenses

Operating revenues and expenses for proprietary funds are those that result from providing services and producing and delivering goods and/or services. It also includes all revenue and expenses not related to capital and noncapital financing or investing activities.

Expenditures/Expenses

In the government-wide financial statements, expenses are classified by function for both governmental and business-type activities.

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

Governmental Funds - By Character	Current (further classified by Function)
	Debt Service
	Capital Outlay
Proprietary Fund - By Operating and Nonoperating	

In the fund financial statements, governmental funds report expenditures of financial resources. Proprietary funds report expenses relating to use of economic resources.

Interfund Transfers

Permanent reallocation of resources between funds of the reporting entity are classified as interfund transfers. For the purpose of the Statement of Activities, all interfund transfers between individual governmental funds, as well as all interfund transfers between individual proprietary funds, have been eliminated. See additional information at Note 3.D.

1.G. RECENTLY ISSUED ACCOUNTING STANDARD

Effective December 31, 2018, the City adopted GASB Statement No. 75, *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 for the City's Postemployment Benefit Plan.

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 2 STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

2.A. FUND ACCOUNTING REQUIREMENTS AND DEPOSITS AND INVESTMENTS LAWS AND REGULATIONS

By its nature as a local government unit, the City is subject to various Federal, State, and local laws and contractual regulations. The City complies with all State and local laws and regulations requiring the use of separate funds.

In accordance with State law, all uninsured deposits of municipal funds in financial institutions must be secured with acceptable collateral valued at market value. Minnesota Statutes require that all deposits with financial institutions be collateralized in an amount equal to 110% of deposits in excess of FDIC or FSLIC insurance (100% if collateral pledged is irrevocable standby letters of credit issued by the Federal Home Loan Bank). The City complies with such laws.

2.B. BUDGETARY INFORMATION

Annual budgets are adopted on a basis consistent with accounting principles generally accepted in the United States of America for the General Fund and major special revenue funds. All annual appropriations lapse at fiscal year-end. The City does not use encumbrance accounting.

Each year, the City Administrator submits a proposed operating budget to the City Council for the following year. Public hearings are conducted to allow for taxpayer comments, and the proposed budget is then reviewed and approved by the Council.

The appropriated budget is prepared by fund, function and department. The City's management may make transfers of appropriations between departments within any fund, however transfers of appropriations between departments require the approval of the Council. The legal level of budgetary control (i.e., the level at which expenditures may not legally exceed appropriations) is the department level. Budgeted amounts are as originally adopted, or as amended by the Council. See original and final General Fund and Fire Department Fund budgets presented as Required Supplementary Information.

NOTE 3 DETAIL NOTES ON TRANSACTION CLASSES/ACCOUNTS

The following notes present detail information to support the amounts reported in the basic financial statements for its various assets, liabilities, deferred outflows/inflows if resources, equity, revenues and expenditures/expenses.

3.A. CASH, CASH EQUIVALENTS AND INVESTMENTS

Deposits

In accordance with applicable Minnesota Statutes, the City maintains deposits at depository banks authorized by the City Council. Minnesota Statutes require that all City deposits be protected by insurance, surety bond, or collateral. The market value of collateral pledged must equal 110 percent of the deposits not covered by insurance or bonds (100% if collateral pledged is irrevocable standby letters of credit issued by the Federal Home Loan Bank). The City complies with such laws.

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 3 DETAIL NOTES ON TRANSACTION CLASSES/ACCOUNTS (Continued)

3.A. CASH, CASH EQUIVALENTS AND INVESTMENTS (Continued)

Deposits (Continued)

Authorized collateral in lieu of a corporate surety bond includes:

- United States government Treasury bills, Treasury notes, Treasury bonds;
- Issues of United States government agencies and instrumentalities as quoted by a recognized industry quotation service available to the government entity;
- A general obligation of a state or local government, with taxing powers, rated “A” or better;
- A revenue obligation of a state or local government, with taxing powers, rated “AA” or better;
- Unrated general obligation securities of a local government, with taxing powers, pledged as collateral against funds deposited by that same local government entity;
- Irrevocable standby letter of credit issued by a Federal Home Loan Bank accompanied by written evidence that the Federal Home Loan Bank’s public debt is rated “AA” or better by Moody’s or Standard and Poor’s; or
- Time deposits insured by any federal agency.

Minnesota Statutes require that 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. The selection should be approved by the City Council.

At December 31, 2018, the City’s deposits, including certificates of deposit, were not exposed to custodial credit risk. The City’s deposits were sufficiently covered by federal depository insurance or by collateral held by the government’s agent in the government’s name.

Investments

The City may also invest idle funds as authorized by Minnesota Statutes as follows: direct obligations guaranteed by the United States or its agencies; shares of investment companies registered under the Federal Investment Company Act of 1940 that received the highest credit rating, are rated in one of the two highest rating categories by a statistical rating agency, and all of the investments have a final maturity of 13 months or less; general obligations rated “A” or better; revenue obligations rated “AA” or better; general obligations of the Minnesota Housing Finance Agency rated “A” or better; bankers’ acceptances of United States banks eligible for purchase by the Federal Reserve System; commercial paper issued by United States corporations or their Canadian subsidiaries, rated of the highest quality category by at least two nationally recognized rating agencies, and maturing in 270 days or less; Guaranteed Investment Contracts guaranteed by a United States commercial bank, domestic branch of a foreign bank, or a United States insurance company, and with a credit quality in one of the top two highest categories; repurchase or reverse purchase agreements and securities lending agreements with financial institutions qualified as a “depository” by the government entity, with banks that are members of the Federal Reserve System with capitalization exceeding \$10,000,000, a primary reporting dealer in U.S. government securities to the Federal Reserve Bank of New York, or certain Minnesota securities broker-dealers. The City does not have any investment policies that would further limit investment choices.

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 3 DETAIL NOTES ON TRANSACTION CLASSES/ACCOUNTS (Continued)

3.A. CASH, CASH EQUIVALENTS AND INVESTMENTS (Continued)

Investments (Continued)

Investment balances at December 31, 2018 are as follows:

<u>Deposit/Investment</u>	<u>Interest Rates</u>	<u>Maturity</u>	<u>Fair Value</u>	<u>S & P's Rating</u>	<u>Moody's Rating</u>	<u>Percent of Total</u>
Money Market Funds	2.22	N/A	\$ 32,951	N/R	N/R	2.05
U.S. Treasury Notes	2.39	< 1 year	25,011	N/R	AAA	1.56
	2.46 - 2.51	1 - 5 years	174,508	N/R	AAA	10.88
	2.54	6 - 10 years	74,862	N/R	AAA	4.67
Federal Home Loan Mortgage Corporation Med Term Notes	2.43	< 1 year	30,092	AA+	AAA	1.88
	2.51 - 2.59	1 - 5 years	114,423	AA+	AAA	7.13
Municipal Bonds	2.97	< 1 year	50,000	AA	AA3	3.12
	2.61 - 3.42	1 - 5 years	527,962	N/R - AA+	N/R - AA3	32.92
	3.00 - 3.76	6 - 10 years	<u>574,132</u>	N/R - AAA	N/R - AAA	<u>35.79</u>
Totals			<u>\$ 1,603,941</u>			<u>100.00</u>

The investments of the City are subject to the following risks:

- Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Ratings are provided by various credit rating agencies and where applicable, indicate associated credit risk as indicated in the table above. Minnesota Statutes limit the City's investments.
- Custodial credit risk is the risk that in the event of a failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The City does not have a formal investment policy to address custodial credit risk but typically limits its exposure by purchasing insured or registered investments.
- Concentration Risk is the risk associated with investing a significant portion of the City's investments (considered 5 percent or more) in the investments of a single issuer, excluding U.S. guaranteed investments (such as treasuries), investment pools and mutual funds. The City has no formal policy limiting the amounts that may be invested in any one issuer. At December 31, 2018, the City's concentration of credit risk is shown in the table above.

**CITY OF PEQUOT LAKES, MINNESOTA
 NOTES TO THE BASIC FINANCIAL STATEMENTS
 DECEMBER 31, 2018**

NOTE 3 DETAIL NOTES ON TRANSACTION CLASSES/ACCOUNTS (Continued)

3.A. CASH, CASH EQUIVALENTS AND INVESTMENTS (Continued)

Investments (Continued)

- Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment and is disclosed above by presenting maturity information. The City’s investment policy requires the City to diversify its investment portfolio to insure that capital losses are avoided. The policy also states the City’s investment portfolio will remain sufficiently liquid to meet all operating costs that may be reasonably anticipated.

The City categorizes its fair value measurements within the fair value hierarchy established by accounting principles generally accepted in the United States of America. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs.

The City has the following recurring fair value measurements as of December 31, 2018:

- U.S. Treasury Notes of \$274,381, Federal Home Loan Mortgage Corporation Med Term Notes of \$144,515 and Municipal Bonds of \$1,152,094 are valued by using significant other observable inputs (level 2).

Deposits and Investments Summary

A reconciliation of cash, cash equivalents, and investments as shown on the Statement of Net Position for the City follows:

Carrying Amount of Deposits	\$	1,158,389
Money Market Funds		5,621,057
Investments (See Investments Section)		<u>1,603,941</u>
Total	\$	<u>8,383,387</u>
Government-wide Cash, Cash Equivalents and Investments	\$	8,368,951
Debt Reserve Restricted Cash		<u>14,436</u>
Total	\$	<u>8,383,387</u>

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 3 DETAIL NOTES ON TRANSACTION CLASSES/ACCOUNTS (Continued)

3.B. CAPITAL ASSETS

Capital asset activity for the year ended December 31, 2018 is as follows:

	<u>Balance at 01/01/18</u>	<u>Additions</u>	<u>Disposals</u>	<u>Transfers</u>	<u>Balance at 12/31/18</u>
Governmental Activities:					
Capital Assets not Being					
Depreciated					
Land	\$ 1,504,339	\$ 91,979	\$ -	\$ -	\$ 1,596,318
Construction In Progress	<u>100,779</u>	<u>899,555</u>	<u>(43,836)</u>	<u>-</u>	<u>956,498</u>
Total Capital Assets not Being					
Depreciated	1,605,118	991,534	(43,836)	-	2,552,816
Capital Assets Being					
Depreciated					
Buildings and Improvements	1,579,950	78,872	(2,963)	-	1,655,859
Machinery, Furniture and					
Equipment	3,127,559	316,167	(92,299)	-	3,351,427
Infrastructure	<u>6,139,497</u>	<u>971,084</u>	<u>-</u>	<u>-</u>	<u>7,110,581</u>
Total Capital Assets Being					
Depreciated	10,847,006	1,366,123	(95,262)	-	12,117,867
Less: Accumulated Depreciation					
Buildings and Improvements	(701,226)	(57,576)	1,164	-	(757,638)
Machinery, Furniture and					
Equipment	(1,661,764)	(207,036)	92,299	-	(1,776,501)
Infrastructure	<u>(2,793,617)</u>	<u>(239,594)</u>	<u>-</u>	<u>-</u>	<u>(3,033,211)</u>
Total Accumulated					
Depreciation	<u>(5,156,607)</u>	<u>(504,206)</u>	<u>93,463</u>	<u>-</u>	<u>(5,567,350)</u>
Total Capital Assets Being					
Depreciated, Net	<u>5,690,399</u>	<u>861,917</u>	<u>(1,799)</u>	<u>-</u>	<u>6,550,517</u>
Capital Assets, Net	<u>\$ 7,295,517</u>	<u>\$ 1,853,451</u>	<u>\$ (45,635)</u>	<u>\$ -</u>	<u>\$ 9,103,333</u>

Depreciation is charged to governmental activities as follows:

General Government	\$ 68,509
Public Safety	131,817
Public Works	283,925
Parks and Recreation	<u>19,955</u>
Total Depreciation Expense	<u>\$ 504,206</u>

CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018

NOTE 3 DETAIL NOTES ON TRANSACTION CLASSES/ACCOUNTS (Continued)

3.B. CAPITAL ASSETS (Continued)

	Balance at 01/01/18	Additions	Disposals	Transfers	Balance at 12/31/18
Business-Type Activities:					
Capital Assets not Being					
Depreciated					
Land	\$ 156,969	\$ -	\$ -	\$ -	\$ 156,969
Construction In Progress	-	24,570	-	-	24,570
Total Capital Assets not Being					
Depreciated	156,969	24,570	-	-	181,539
Capital Assets Being					
Depreciated					
Buildings and Improvements	1,125,329	-	-	-	1,125,329
Machinery and Equipment	3,198,056	132,193	-	-	3,330,249
Infrastructure	1,512,530	-	-	-	1,512,530
Total Capital Assets Being					
Depreciated	5,835,915	132,193	-	-	5,968,108
Less: Accumulated Depreciation					
Buildings and Improvements	(1,068,477)	(3,908)	-	-	(1,072,385)
Machinery and Equipment	(1,945,655)	(80,937)	-	-	(2,026,592)
Infrastructure	(168,818)	(38,960)	-	-	(207,778)
Total Accumulated					
Depreciation	(3,182,950)	(123,805)	-	-	(3,306,755)
Total Capital Assets Being					
Depreciated, Net	2,652,965	8,388	-	-	2,661,353
Capital Assets, Net	\$ 2,809,934	\$ 32,958	\$ -	\$ -	\$ 2,842,892

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 3 DETAIL NOTES ON TRANSACTION CLASSES/ACCOUNTS (Continued)

3.C. NONCURRENT LIABILITIES

The City's long-term debt is segregated between the amounts to be repaid from governmental activities and amounts to be repaid from business-type activities.

Debt Detail

As of December 31, 2018, the long-term debt of the financial reporting entity consists of the following:

Governmental Activities

General Obligation Certificates					
Issue Date	Original Amount	Annual Principal Payment	Interest Rate(s)	Maturity Date	Remaining Amount
01/14	\$ 193,000	\$37,000 - \$40,000	2.50%	02/19	\$ 40,000
02/17	135,000	\$9,100 - \$32,900	2.99%	08/22	125,900
					165,900

Capital Leases					
Issue Date	Original Amount	Annual Principal Payment	Interest Rate(s)	Maturity Date	Remaining Amount
02/04	\$ 1,097,442	\$34,583	4.00%	03/24	\$ 162,058
03/14	9,866	\$2,796	14.67%	03/18	-
10/15	4,544	\$1,116	10.00%	12/20	2,015
					164,073

Loans Payable					
Issue Date	Original Amount	Annual Principal Payment	Interest Rate(s)	Maturity Date	Remaining Amount
02/14	\$ 350,000	\$18,141 - \$29,322	3.50%	02/19	\$ 273,537
		Total Governmental Activities Long-Term Debt			603,510
		Due Within One Year			117,876
		Due After One Year			\$ 485,634

CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018

NOTE 3 DETAIL NOTES ON TRANSACTION CLASSES/ACCOUNTS (Continued)

3.C. NONCURRENT LIABILITIES (Continued)

Debt Detail (Continued)

Business-Type Activities

General Obligation Bonds					
Issue Date	Original Amount	Annual Principal Payment	Interest Rate(s)	Maturity Date	Remaining Amount
02/13	\$ 1,270,000	\$55,000 - \$85,000	0.60 - 3.10%	08/31	\$ 910,000
Capital Leases					
Issue Date	Original Amount	Annual Principal Payment	Interest Rate(s)	Maturity Date	Remaining Amount
10/15	3,029	\$744	10.00%	12/20	\$ 1,342
Total Business-Type Long-Term Debt					911,342
Due Within One Year					60,638
Due After One Year					<u>\$ 850,704</u>

All bonds are direct obligations of the City and pledge the full faith and credit of the City.

Changes in Noncurrent Liabilities

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

Type of Debt	Balance 01/01/18	Additions	Deductions	Balance 12/31/18	Amounts Due Within One Year
<i>Governmental Activities:</i>					
General Obligation Certificates	\$ 214,250	\$ -	\$ (48,350)	\$ 165,900	\$ 70,100
Capital Leases	190,606	-	(26,533)	164,073	26,959
Loans Payable	293,650	-	(20,113)	273,537	20,817
Compensated Absences	48,411	58,961	(61,279)	46,093	18,613
Total	<u>\$ 746,917</u>	<u>\$ 58,961</u>	<u>\$ (156,275)</u>	<u>\$ 649,603</u>	<u>\$ 136,489</u>
<i>Business-Type Activities:</i>					
General Obligation Bonds	\$ 970,000	\$ -	\$ (60,000)	\$ 910,000	\$ 60,000
Unamortized Bond Premium	1,738	-	(138)	1,600	-
Capital Leases	1,920	-	(578)	1,342	638
Compensated Absences	2,582	4,923	(6,917)	588	273
Total	<u>\$ 976,240</u>	<u>\$ 4,923</u>	<u>\$ (67,633)</u>	<u>\$ 913,530</u>	<u>\$ 60,911</u>

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 3 DETAIL NOTES ON TRANSACTION CLASSES/ACCOUNTS (Continued)

3.C. NONCURRENT LIABILITIES (Continued)

Changes in Noncurrent Liabilities (Continued)

Governmental activity debt is typically funded through Debt Service Funds. Business-type activity debt is typically funded through the Water and Sewer Funds. Compensated absences are funded through the funds to which the respective employees' wages are allocated.

At December 31, 2018, capital assets acquired with capital leases include the City Hall building with an original cost of \$1,056,200, a copier with an original cost of \$9,866 and a postage machine with an original cost of \$7,575. There was accumulated depreciation of \$549,961 on the City Hall building, \$9,866 on the copier lease and \$4,923 on the postage machine lease as of December 31, 2018.

Annual Debt Service Requirements

At December 31, 2018, the estimated annual debt service requirements to maturity, including principal and interest, are as follows:

Years Ending December 31,	Governmental Activities					
	Capital Leases			Loans		
	Principal	Interest	Total	Principal	Interest	Total
2019	\$ 26,959	\$ 6,167	\$ 33,126	\$ 20,817	\$ 9,574	\$ 30,391
2020	28,117	5,041	33,158	21,546	8,845	30,391
2021	28,162	3,847	32,009	22,300	8,091	30,391
2022	29,310	2,700	32,010	23,080	7,311	30,391
2023	30,504	1,506	32,010	23,888	6,503	30,391
2024-2028	21,021	318	21,339	132,584	19,372	151,956
2029	-	-	-	29,322	1,025	30,347
Totals	<u>\$ 164,073</u>	<u>\$ 19,579</u>	<u>\$ 183,652</u>	<u>\$ 273,537</u>	<u>\$ 60,721</u>	<u>\$ 334,258</u>

Years Ending December 31,	Governmental Activities		
	General Obligation Certificates		
	Principal	Interest	Total
2019	\$ 70,100	\$ 4,264	\$ 74,364
2020	31,000	2,864	33,864
2021	31,900	1,938	33,838
2022	32,900	984	33,884
Totals	<u>\$ 165,900</u>	<u>\$ 10,050</u>	<u>\$ 175,950</u>

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 3 DETAIL NOTES ON TRANSACTION CLASSES/ACCOUNTS (Continued)

3.C. NONCURRENT LIABILITIES (Continued)

Annual Debt Service Requirements (Continued)

Years Ending December 31,	Business-Type Activities					
	General Obligation Bonds			Capital Leases		
	Principal	Interest	Total	Principal	Interest	Total
2019	\$ 60,000	\$ 22,540	\$ 82,540	\$ 638	\$ 106	\$ 744
2020	60,000	21,640	81,640	704	60	764
2021	60,000	20,620	80,620	-	-	-
2022	65,000	19,460	84,460	-	-	-
2023	65,000	18,160	83,160	-	-	-
2024-2028	355,000	64,863	419,863	-	-	-
2029-2031	245,000	11,547	256,547	-	-	-
Totals	<u>\$ 910,000</u>	<u>\$ 178,830</u>	<u>\$ 1,088,830</u>	<u>\$ 1,342</u>	<u>\$ 166</u>	<u>\$ 1,508</u>

Interest and other fiscal charges total \$45,859 in the Statement of Activities (included in Debt Service and Water lines). Interest and other fiscal charges total \$24,694 for the Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Funds (included in the line Interest and Other Charges) and \$23,357 in the Statement of Revenues, Expenses and Changes in Net Position – Proprietary Funds (included in the line Interest and Other Charges).

3.D. INTERFUND TRANSACTIONS AND BALANCES

Operating transfers consist of the following for the year ended December 31, 2018:

Major Funds	Transfers Out	Transfers In	
		Nonmajor Funds Governmental	Totals
Water	<u>\$ 21,198</u>	<u>\$ 21,198</u>	<u>\$ 21,198</u>

Transfers are used to (a) move revenues from the fund that statute or budget requires to collect them to the fund that statute or budget require to expend them and to (b) use unrestricted revenues collected in the General Fund to finance various programs accounted for in other funds in accordance with budgetary authorizations.

The interfund balances are as follows:

Long-Term Advances			
Advances To	Advances From	Amount	Reason
General	Highway 371 Project	\$ 908,780	Finance capital improvements

Interfund balances are to be repaid as cash flows become available.

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 3 DETAIL NOTES ON TRANSACTION CLASSES/ACCOUNTS (Continued)

3.E. FUND EQUITY

At December 31, 2018, governmental fund equity consists of the following:

Major Governmental Funds

General Fund	
Restricted for Park Dedication	\$ 30,166
Restricted by Donor - Splash Park	15,000
Restricted for Forfeiture	18,721
Committed for Library	158,467
Committed for Water Tower	3,263
Committed for Capital Outlay	156,071
Unassigned	<u>188,902</u>
Total General Fund Balance	<u>\$ 570,590</u>
Fire Department Fund	
Restricted for Debt Reserves	\$ 14,436
Committed for Fire Department	61,123
Committed for Capital Outlay	<u>48,685</u>
Total Fire Department Fund Balance	<u>\$ 124,244</u>
Highway 371 Project Fund	
Nonspendable - Advance to Other Funds	\$ 908,780
Committed for Highway 371 Project	<u>4,402,451</u>
Total Highway 371 Project Fund Balance	<u>\$ 5,311,231</u>

Nonmajor Governmental Funds

Nonmajor Governmental Funds	
Nonspendable - Land Held for Resale	\$ 46,982
Restricted for Debt Service	50,115
Committed for Business Park	299,418
Committed for Cemetery Perpetual Care	<u>68,315</u>
Total Nonmajor Governmental Funds Balance	<u>\$ 464,830</u>

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 4 OTHER NOTES

4.A. EMPLOYEE DEFINED BENEFIT PENSION PLANS – STATEWIDE

Plan Description

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

General Employees Retirement Plan

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

Public Employees Police and Fire Plan

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

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. 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.

General Employees Plan Benefits

General Employee Plan Benefits are based on a member's highest average salary for any five successive years of allowable service, age and years of credit at termination of service. Two methods are used to compute benefits for PERA's Coordinated Plan members. Members hired prior to July 1, 1989 receive the higher of Method 1 or Method 2 formulas. Only Method 2 is used for members hired after June 30, 1989. Under Method 1, the accrual rate for Coordinated Plan members is 1.20 percent of average salary for each of the first ten years of service and 1.70 percent of average salary for each additional year. Under Method 2, the accrual rate for Coordinated Plan members is 1.70 percent of average salary for all years of service. For members hired prior to July 1, 1989, a full annuity is available when age plus years of service equal 90 and normal retirement age is 65. For members hired on or after July 1, 1989, normal retirement age is the age for unreduced Social Security benefits capped at 66.

Benefit increases are provided to benefit recipients each January. Increases are related to the funding ratio of the plan. If the General Employees Plan is at least 90 percent funded for two consecutive years, benefit recipients are given a 2.5 percent increase.

If the plan has not exceeded 90 percent funded, or have fallen below 80 percent, benefit recipients are given a one percent increase. A benefit recipient who has been receiving a benefit for at least 12 full months as of June 30, will receive a full increase. Members receiving benefits for at least one month but less than 12 full months as of June 30, will receive a pro rata increase.

Police and Fire Plan Benefits

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

**CITY OF PEQUOT LAKES, MINNESOTA
 NOTES TO THE BASIC FINANCIAL STATEMENTS
 DECEMBER 31, 2018**

NOTE 4 OTHER NOTES (Continued)

4.A. EMPLOYEE DEFINED BENEFIT PENSION PLANS – STATEWIDE (Continued)

Benefits Provided (Continued)

Police and Fire Plan Benefits (Continued)

Benefit increases are provided to benefit recipients each January. Police and Fire Plan benefit recipients receive a future annual 1.0 percent increase. An annual adjustment will equal 2.5 percent any time the plan exceeds a 90.0 percent funded ratio for two consecutive years. If the adjustment is increased to 2.5 percent and the funded ratio falls below 80.0 percent for one year or 85.0 percent for two consecutive years, the post-retirement benefit increase will be lowered to one percent. A benefit recipient who has been receiving a benefit for at least twelve full months as of June 30 will receive a full increase. Members receiving benefits for at least one month but less than twelve full months as of June 30 will receive a pro rata increase. For retirements after May 31, 2014, the first increase will be delayed two years.

Contributions

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

General Employees Fund Contributions

Coordinated Plan members were required to contribute 6.5 percent of their annual covered salary in fiscal year 2018 and the City was required to contribute 7.50 percent for Coordinated Plan members. The City’s contributions to the General Employees Fund for the year ended December 31, 2018 total \$27,572. The City’s contributions were equal to the required contributions as set by State Statute.

Police and Fire Fund Contributions

Plan members were required to contribute 10.8 percent of their annual covered salary and the City was required to contribute 16.20 percent of pay for members in fiscal year 2018. The City’s contributions to the Police and Fire Fund for the year ended December 31, 2018 total \$54,743. The City’s contributions were equal to the required contributions as set by State Statute.

Pension Costs

General Employees Fund Pension Costs

At December 31, 2018, the City reported a liability of \$310,665 for its proportionate share of the General Employees Fund’s net pension liability. The City’s net pension liability reflected a reduction due to the State of Minnesota’s contribution of \$16 million to the fund in 2018. The State of Minnesota is considered a non-employer contributing entity and the state’s contribution meets the definition of a special funding situation. The State of Minnesota’s proportionate share of the net pension liability associated with the City totaled \$10,219. The net pension liability was measured as of June 30, 2018 and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The City’s proportionate share of the net pension liability was based on the City’s contributions received by PERA during the measurement period for employer payroll paid dates from July 1, 2017 through June 30, 2018, relative to the total employer contributions received from all of PERA’s participating employers. At June 30, 2018, the City’s proportionate share was 0.0056 percent which was an increase of 0.0002 percent from its proportionate share measured as of June 30, 2017.

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

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 4 OTHER NOTES (Continued)

4.A. EMPLOYEE DEFINED BENEFIT PENSION PLANS – STATEWIDE (Continued)

Pension Costs (Continued)

General Employees Fund Pension Costs (Continued)

For the year ended December 31, 2018, the City recognized pension expense of \$21,209 for its proportionate share of the General Employees Plan’s pension expense. In addition, the City recognized an additional \$2,383 as pension expense (and grant revenue) for its proportionate share of the State of Minnesota’s contribution of \$16 million to the General Employees Fund.

At December 31, 2018, the City reported its proportionate share of the General Employees Plan’s deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences Between Expected and Actual Economic Experience	\$ 7,942	\$ 8,899
Changes in Actuarial Assumption	29,147	34,053
Difference Between Projected and Actual Investment Earnings	-	30,828
Changes in Proportionate Share	9,576	15,129
Contributions Paid to PERA Subsequent to the Measurement Date	13,358	-
Total City Deferred Outflows/Inflows	\$ 60,023	\$ 88,909

A total of \$13,358 reported as deferred outflows of resources related to pensions resulting from the City contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2019. Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended December 31,	Pension Expense
2019	\$ 819
2020	\$ (15,106)
2021	\$ (21,474)
2022	\$ (6,483)

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 4 OTHER NOTES (Continued)

4.A. EMPLOYEE DEFINED BENEFIT PENSION PLANS – STATEWIDE (Continued)

Pension Costs (Continued)

Police and Fire Fund Pension Costs

At December 31, 2018, the City reported a liability of \$331,494 for its proportionate share of the Police and Fire Fund’s net pension liability. The net pension liability was measured as of June 30, 2018 and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The City’s proportionate share of the net pension liability was based on the City’s contributions received by PERA during the measurement period for employer payroll paid dates from July 1, 2017 through June 30, 2018, relative to the total employer contributions received from all of PERA’s participating employers. At June 30, 2018 the City’s proportionate share was 0.0311 percent which was a decrease of 0.0009 percent from its proportionate share measured as of June 30, 2017. The City also recognized \$2,799 for the year ended December 31, 2018 as pension revenue and an offsetting reduction of net pension liability for its proportionate share of the State of Minnesota’s on-behalf contributions to the Police and Fire Fund. Legislation passed in 2013 required the State of Minnesota to begin contributing \$9 million to the Police and Fire Fund each year, starting in fiscal year 2014.

For the year ended December 31, 2018, the City recognized pension expense of \$28,002 for its proportionate share of the Police and Fire Plan’s pension expense.

At December 31, 2018 the City reported its proportionate share of the Police and Fire Plan’s deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences Between Expected and Actual Economic Experience	\$ 13,685	\$ 86,292
Changes in Actuarial Assumption	455,125	501,803
Difference Between Projected and Actual Investment Earnings	-	66,976
Changes in Proportionate Share	4,472	43,406
Contributions Paid to PERA Subsequent to the Measurement Date	27,787	-
Total City Deferred Outflows/Inflows	\$ 501,069	\$ 698,477

A total of \$27,787 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, 2019. Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

Year ended December 31,	Pension Expense
2019	\$ 6,509
2020	\$ (27,740)
2021	\$ (56,091)
2022	\$ (144,756)
2023	\$ (3,117)

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 4 OTHER NOTES (Continued)

4.A. EMPLOYEE DEFINED BENEFIT PENSION PLANS – STATEWIDE (Continued)

Actuarial Assumptions

The total pension liability in the June 30, 2018 actuarial valuation was determined using an individual entry-age normal actuarial cost method and the following actuarial assumptions:

<u>Assumptions</u>	<u>Rates</u>
Inflation	2.50% per year
Active Member Payroll Growth	3.25% per year
Investment Rate of Return	7.50%

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

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

The following changes in actuarial assumptions occurred in 2018:

General Employees Fund

- The mortality projection scale was changed from MP-2015 to MP-2017.
- The assumed post-retirement benefit increase was changed from 1.0 percent per year through 2044 and 2.50 percent per year thereafter to 1.25 percent per year.

Police and Fire Fund

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

The State Board of Investment, which manages the investments of PERA, prepares an analysis of the reasonableness on a regular basis of the long-term expected rate of return using a building-block method in which best-estimate ranges of expected future rates of return are developed for each major asset class. These ranges are combined to produce an expected long-term rate of return by weighting the expected future rates of return by the target asset allocation percentages. The target allocation and best estimates of geometric 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	36%	5.10%
International Stocks	17%	5.30%
Bonds (Fixed Income)	20%	0.75%
Alternative Assets (Private Markets)	25%	5.90%
Cash	2%	0.00%

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 4 OTHER NOTES (Continued)

4.A. EMPLOYEE DEFINED BENEFIT PENSION PLANS – STATEWIDE (Continued)

Discount Rate

The discount rate used to measure the total pension liability in 2018 was 7.5 percent. The projection of cash flows used to determine the discount rate assumed that contributions from plan members and employers will be made at rates set in Minnesota Statutes. Based on these assumptions, the fiduciary net position of the General Employees Fund and the Police and Fire Fund were projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Pension Liability Sensitivity

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

	<u>1% Decrease in Discount Rate (6.5%)</u>		<u>Discount Rate (7.5%)</u>		<u>1% Increase in Discount Rate (8.5%)</u>
Proportionate share of the General Employees Fund					
Net Pension Liability	\$ 504,870	\$	310,665	\$	150,354
Proportionate share of the Police and Fire Fund					
Net Pension Liability	\$ 710,744	\$	331,494	\$	17,870

Pension Plan Fiduciary Net Position

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

4.B. PUBLIC EMPLOYEES DEFINED CONTRIBUTION PLAN – STATEWIDE

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

Plan benefits depend solely on amounts contributed to the plan plus investment earnings, less administrative expenses. *Minnesota Statutes*, Chapter 353D.03, 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 five percent 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 contributions 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 shares in one or more of the seven accounts of the Minnesota Supplemental Investment Fund. For administering the plan, PERA receives two percent of employer contributions and twenty-five hundredths of one percent (0.25 percent) of the assets in each member's account annually.

**CITY OF PEQUOT LAKES, MINNESOTA
 NOTES TO THE BASIC FINANCIAL STATEMENTS
 DECEMBER 31, 2018**

NOTE 4 OTHER NOTES (Continued)

4.B. DEFINED CONTRIBUTION PENSION PLAN – STATEWIDE (Continued)

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

Contribution Amount		Percentage of Covered Payroll		Required
Employee	Employer	Employee	Employer	Rate
\$ 418	\$ 418	5.0%	5.0%	5.0%

4.C. DEFINED BENEFIT PENSION PLANS – FIRE RELIEF ASSOCIATION

Plan Description

Firefighters of the City of Pequot Lakes are members of the Pequot Lakes Firefighters Relief Association. The Association is the administrator of a single-employer defined benefit pension plan available to firefighters. The plan operates under the provisions of *Minnesota Statutes* Chapters 69 and 424A, along with the Association’s bylaws.

Benefits Provided

After the age of 50 and upon retirement, each member who has served as an active firefighter in the Association is eligible for varying levels of pension benefits, dependent upon the individual’s years of service. In addition, members or their beneficiaries may qualify for death or disability benefits.

Contributions

Minnesota Statute Chapter 424A.092 specifies minimum contributions required on an annual basis. The minimum support rates from the municipality and state aid are determined in the amount required to meet the normal cost plus amortizing any existing prior year service costs over a 10-year period. The City’s contributions to the Association for the year ended December 31, 2018, total \$57,410, of which \$36,527 was funded via contributions from participating local governments.

Pension Costs

At December 31, 2018, the City of Pequot Lakes reported a net pension asset of \$483,953 for the Fire Relief Association’s plan. The net pension asset was measured as of December 31, 2017, as determined by an actuarial valuation as of that date.

For the year ended December 31, 2018, the City recognized pension expense of \$16,818 for the Association. The City also recognized \$51,257 for the year ended December 31, 2018, as pension expense (and grant revenue) for State of Minnesota’s contributions to the Association during the measurement period.

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 4 OTHER NOTES (Continued)

4.C. DEFINED BENEFIT PENSION PLANS – FIRE RELIEF ASSOCIATION (Continued)

Pension Costs (Continued)

The following table presents the changes in net pension asset during the year.

	<u>Total Pension Liability</u>	<u>Plan Fiduciary Net Position</u>	<u>Net Pension Liability (Asset)</u>
Beginning Balance 1/1/17	\$ 1,117,731	\$ 1,587,722	\$ (469,991)
Changes for the Year			
Service Cost	50,980	-	50,980
Interest on Pension Liability	43,638	-	43,638
Plan Changes	103,240	-	103,240
Projected Investment Earnings	-	62,311	(62,311)
Contributions (Employer)	-	54,033	(54,033)
Contributions (State)	-	51,257	(51,257)
Asset (Gain)/Loss	-	53,867	(53,867)
Benefit Payments	(155,524)	(155,524)	-
Administrative Fee	-	(9,648)	9,648
Net Changes	<u>42,334</u>	<u>56,296</u>	<u>(13,962)</u>
Balance End of Year 12/31/17	<u>\$ 1,160,065</u>	<u>\$ 1,644,018</u>	<u>\$ (483,953)</u>

At December 31, 2018, the City of Pequot Lakes reported deferred outflows/inflows of resources related to the pension from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Differences Between Expected and Actual Economic Experience	\$ -	\$ 47,227
Changes in Actuarial Assumptions	-	51,450
Difference Between Projected and Actual Investment Earnings	-	36,061
Contributions Paid Subsequent to the Measurement Date	<u>57,410</u>	<u>-</u>
Total City Deferred Outflows/Inflows	<u>\$ 57,410</u>	<u>\$ 134,738</u>

A total of \$57,410 reported as deferred outflows of resources related to the pension resulting from City contributions subsequent to the measurement date will be recognized as an addition to the net pension asset in the year ended December 31, 2019.

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 4 OTHER NOTES (Continued)

4.C. DEFINED BENEFIT PENSION PLANS – FIRE RELIEF ASSOCIATION (Continued)

Pension Costs (Continued)

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

Year ended December 31,	Pension Expense
2019	\$ (19,010)
2020	\$ (15,182)
2021	\$ (23,987)
2022	\$ (21,737)
2023	\$ (10,964)
2024-2027	\$ (43,858)

Actuarial Assumptions

The total pension asset at December 31, 2017, was determined using the entry age normal actuarial cost method and the following actuarial assumptions:

Assumptions	Rates
Investment Rate of Return (Discount)	4.00%
Expected Long-Term Rate of Return	4.00%
20-Year Municipal Bond Yield	3.50%
Salary Increases	2.50%
Cost of Living Increases	0.00%

There were no changes to actuarial assumptions during 2017.

Pension Liability Sensitivity

The following presents the City’s net pension asset for the Fire Relief Association’s plan, calculated using the discount rate disclosed in the preceding paragraph, as well as what the City’s net pension asset would be if it were calculated using a discount rate 1% lower or 1% higher than the current discount rate:

	1% Decrease in Discount Rate (3.0%)	Discount Rate (4.0%)	1% Increase in Discount Rate (5.0%)
Net Pension Asset	\$ 451,882	\$ 483,953	\$ 514,904

**CITY OF PEQUOT LAKES, MINNESOTA
 NOTES TO THE BASIC FINANCIAL STATEMENTS
 DECEMBER 31, 2018**

NOTE 4 OTHER NOTES (Continued)

4.C. DEFINED BENEFIT PENSION PLANS – FIRE RELIEF ASSOCIATION (Continued)

Plan Investments

Asset Allocation

The long-term expected rate of return on pension plan investments is 4.00%. The target allocation and best estimates of arithmetic real rates of return for each major asset class of the Association’s pension fund investments are summarized in the following table:

<u>Asset Class</u>	<u>Portfolio Weight</u>	<u>Long-Term Expected Real Rate of Return</u>
Cash	49%	2.25%
Fixed Income	23%	3.30%
Equities	28%	7.50%
Other	0%	N/A

Description of significant investment policy changes during the year

The Fire Relief Association made no significant changes to their investment policy during 2017.

Pension Plan Fiduciary Net Position

Detailed information about the pension plan’s net position is available in a separately-issued financial report that includes financial statements and required supplementary information. That report may be obtained by contacting the City Hall at 4638 Main Street, Pequot Lakes, MN 56472.

4.D. POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS

Plan Description

The City administers a single-employer defined benefit medical plan (the Plan), through which the City provides postemployment benefits to eligible retirees and their spouses. As of the most recent actuarial valuation date, there are 14 active employees electing coverage. The Plan does not issue a publicly available financial report.

Benefits Provided

The City offers continuing group health insurance coverage after retirement for qualifying City employees. Police and certain other City employees who retire from active service may continue their single or family coverage, at their expense, through the City plan if they retire after reaching the age of 50 or 55 with at least 3 to 10 years of uninterrupted service in the City. Additionally, Police and certain other City personnel who retire from active service with 15 years of uninterrupted service in the City are eligible for direct subsidies in varying dollar amounts for up to 3 years or until medicare eligibility. Benefits and eligibility provisions have been established through negotiations between the City and the union representing the City’s employees.

The City is legally required to include any retirees for who it provides health insurance coverage in the same insurance pool as its active employees until the retiree reaches Medicare eligibility, regardless of whether the premiums are paid by the City or the retiree. Consequently, participating retirees are considered to receive a secondary benefit known as an “implicit rate subsidy.” This benefit arises from the assumption that the retiree is receiving a more favorable premium rate that they would otherwise be able to obtain if purchasing insurance on their own, due to being included in the same pool with the City’s younger and statistically healthier active employees.

**CITY OF PEQUOT LAKES, MINNESOTA
 NOTES TO THE BASIC FINANCIAL STATEMENTS
 DECEMBER 31, 2018**

NOTE 4 OTHER NOTES (Continued)

4.D. POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS (Continued)

Contributions

The City has historically funded these liabilities on a pay-as-you-go basis, in the amounts contractually required to satisfy the benefit terms discussed above. For the year ended December 31, 2018, the City did not contribute to the Plan.

Net OPEB Liabilities, OPEB Expense, and Deferred Outflows/Inflows of Resources

At December 31, 2018, the City reported a net OPEB liability of \$117,982 for the City’s plan. The net OPEB liability was measured as of December 31, 2017, as determined by an actuarial valuation as of that date.

For the year ended December 31, 2018, the City recognized OPEB expense of \$30,527. At December 31, 2018, There were no deferred inflows or outflows of resources related to the Plan that will be recognized by the City as OPEB expense in the forthcoming years.

Changes in Net OPEB Liability

The following table summarizes changes in the net OPEB liability for the year ended December 31, 2018:

Changes in Total OPEB Liability (TOL)	
Balance at January 1st	\$ 88,055
Service Cost	26,748
Interest Cost	3,778
Benefit Payments	<u>(599)</u>
Balance at December 31st	<u>\$ 117,982</u>

**CITY OF PEQUOT LAKES, MINNESOTA
 NOTES TO THE BASIC FINANCIAL STATEMENTS
 DECEMBER 31, 2018**

NOTE 4 OTHER NOTES (Continued)

4.D. POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS (Continued)

Actuarial Assumptions

The following is a summary of pertinent actuarial assumptions and methods utilized, applied to all periods included in the measurement, unless otherwise specified:

Key Methods and Assumptions Used in Valuation of Total OPEB Liability	
<u>Actuarial Information:</u>	
Valuation Date	January 01, 2018
Measurement Date	January 01, 2018
Actuarial Cost Method	Entry Age Normal, level percentage of pay
Actuarial Assets	None
Amortization of Deferred Resource Flows	Average of expected remaining service on a closed basis for differences between expected and actual experience and assumption changes
<u>Actuarial Assumptions:</u>	
Discount Rate	3.30%
20-Year Municipal Bond Yield	3.30%
Inflation	2.50%
Salary Increases	3.00%
Medical Trend Rate	6.50% as of January 1, 2018 grading to 5.00% over 6 years
Dental Trend Rate	N/A

Mortality rates were based on the RP-2014 mortality tables and then projected beyond the valuation date using scale MP-2017.

Significant changes in assumptions, benefit terms, and other inputs since the prior measurement date include:

- The years of service required to be eligible for a benefit (implicit rate subsidy) was increased from three years to five years.
- The City contribution for union employees changed to 85% of the premium. Also, union employees are now on the same medical plan as other city employees rather than the Teamsters Local 346 plan.
- The mortality table was updated from RP-2014 White Collar Mortality Tables with MP-2014 Generational Improvement Scale (with Blue Collar adjustment for Police and Fire Personnel) to the RP-2014 White Collar Mortality Tables with MP-2017 Generational Improvement Scale (with Blue Collar adjustment for Police and Fire Personnel).
- The retirement and withdrawal tables for all employees were updated.
- The discount rate was changed from 4.00% to 3.30%.
- The actuarial cost method was changed from projected unit credit to entry age as prescribed by GASB 75.

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 4 OTHER NOTES (Continued)

4.D. POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS (Continued)

Net OPEB Liability Sensitivity

The following presents the net OPEB liability, calculated using the discount rate disclosed in the preceding section, as well as what the City’s net OPEB liability would be if it were calculated using a discount rate one percentage point lower or one percentage point higher than the current discount rate:

Sensitivity of Net OPEB Liability at Current Single Discount Rate		
	Rates	Amounts
1% Increase in Discount Rate	4.30%	\$105,980
Current Discount Rate	3.30%	\$117,982
1% Decrease in Discount Rate	2.30%	\$131,170

The following presents the net OPEB liability, calculated using the healthcare cost trend rates disclosed in the preceding section, as well as what the City’s net OPEB liability would be if it were calculated using healthcare cost trend rates that are one percentage point lower or one percentage point higher than the current healthcare cost trend rates:

Sensitivity of Net OPEB Liability at Current Healthcare Cost Trend Rate	
	Amounts
1% Increase in Healthcare Trend Rates	\$140,499
Current Healthcare Trend Rates	\$117,983
1% Decrease in Healthcare Trend Rates	\$99,445

4.E. RISK MANAGEMENT

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. To manage these risks, the City purchases commercial insurance. The City retains risk for the deductible portions of the insurance. The amounts of these deductibles are considered immaterial to the financial statements. There were no significant reductions in insurance from the previous year settlements in excess of insurance for any of the past three years.

Liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities, if any, include an amount for claims that have been incurred but not reported. The City’s management is not aware of any incurred but no reported claims.

4.F. TAX ABATEMENTS

The City executed a tax abatement agreement with a local business during November 2009, as authorized under the provisions of Minnesota Statutes 469.1812 and 469.1815, for the purpose of enhancing the City’s tax base and creating employment opportunities within the City. Under the terms of the agreement, the Developer was required to construct a grocery store, commercial facility, potential gas island, and associated parking. Assuming these and other requirements defined by the abatement agreement are satisfied, all real estate taxes generated by the improvements and collected by the City shall be used to reimburse the Developer for costs incurred. Such reimbursements are scheduled to occur for real estate taxes payable in 2012 through 2024, but shall not exceed the maximum of \$350,000 (plus 4% interest). For the year ended December 31, 2018, taxes abated by the City under this agreement total \$16,389.

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2018**

NOTE 4 OTHER NOTES (Continued)

4.G. CHANGE IN ACCOUNTING PRINCIPLE

During the year ended December 31, 2018, the City determined adjustments to beginning government-wide and proprietary fund net position were necessary to conform to the financial statement presentation prescribed under the newly adopted standard previously discussed in Note 1.G. Adjustments were made to revise the balance of the net OPEB liability at the beginning of the year, as determined by an actuary in accordance with the newly applied standards. The following tables depict the impact of the change in accounting principle on government-wide and proprietary fund beginning net position:

	Governmental Activities	Business-Type Activities
Beginning Net Position	\$ 8,842,388	\$ 3,543,057
Remove: Prior Year Net OPEB Liability at 1/1/18	188,385	12,024
Add: Revised Net OPEB Liability at 1/1/18	(82,772)	(5,284)
Beginning Net Position Balance, as Restated	\$ 8,948,001	\$ 3,549,797
	Water Fund	Sewer Fund
Beginning Net Position	\$ 1,015,301	\$ 2,527,756
Remove: Prior Year Net OPEB Liability at 1/1/18	6,012	6,012
Add: Revised Net OPEB Liability at 1/1/18	(2,642)	(2,642)
Beginning Net Position Balance, as Restated	\$ 1,018,671	\$ 2,531,126

4.H. COMMITMENTS

During the year, the City entered into various contracts for construction services. At December 31, 2018, remaining commitments total \$84,102.

**REQUIRED SUPPLEMENTARY
INFORMATION**

**CITY OF PEQUOT LAKES, MINNESOTA
BUDGETARY COMPARISON SCHEDULE - GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2018**

	Budget Amounts- Original and Final	Actual Amounts	Variance with Final Budget Over (Under)
RESOURCES (INFLOWS):			
Taxes	\$ 1,517,365	\$ 1,515,188	\$ (2,177)
Licenses, Permits, and Fees	15,710	18,810	3,100
Intergovernmental	113,835	235,693	121,858
Charges for Services	102,470	107,597	5,127
Fines	17,000	30,373	13,373
Investment Income	16,000	23,951	7,951
Miscellaneous	289,700	175,647	(114,053)
Bond Proceeds	1,960,000	-	(1,960,000)
Transfers In	15,000	-	(15,000)
AMOUNTS AVAILABLE	4,047,080	2,107,259	(1,939,821)
CHARGES TO APPROPRIATIONS (OUTFLOWS):			
Current:			
General Government	498,690	474,942	(23,748)
Public Safety	703,970	839,233	135,263
Public Works	385,140	310,989	(74,151)
Parks and Recreation	45,110	37,979	(7,131)
Economic Development	32,605	48,966	16,361
Debt Service:			
Principal	24,990	26,533	1,543
Interest and Other Charges	7,030	7,027	(3)
Capital Outlay	6,600,745	1,232,827	(5,367,918)
Transfers Out	15,000	-	(15,000)
TOTAL CHARGES	8,313,280	2,978,496	(5,334,784)
BUDGETARY CHANGE IN FUND BALANCE	\$ (4,266,200)	(871,237)	\$ 3,394,963
FUND BALANCE - BEGINNING		1,441,827	
FUND BALANCE - ENDING		\$ 570,590	

**CITY OF PEQUOT LAKES, MINNESOTA
 BUDGETARY COMPARISON SCHEDULE - FIRE DEPARTMENT FUND
 FOR THE YEAR ENDED DECEMBER 31, 2018**

	Budget Amounts- Original and Final	Actual Amounts	Variance with Final Budget Over (Under)
RESOURCES (INFLOWS):			
Intergovernmental	\$ 8,000	\$ 25,434	\$ 17,434
Charges for Services	206,000	206,770	770
Investment Income	2,500	2,409	(91)
Miscellaneous	700	30,491	29,791
Proceeds from the Sale of Assets	-	10,941	10,941
Transfers In	31,500	-	(31,500)
AMOUNTS AVAILABLE	248,700	276,045	27,345
CHARGES TO APPROPRIATIONS (OUTFLOWS):			
Current:			
Public Safety	134,190	150,005	15,815
Debt Service:			
Principal	45,720	29,213	(16,507)
Interest and Other Charges	16,180	16,176	(4)
Capital Outlay	50,650	64,852	14,202
Transfers Out	31,500	-	(31,500)
TOTAL CHARGES	278,240	260,246	(17,994)
BUDGETARY CHANGE IN FUND BALANCE	\$ (29,540)	15,799	\$ 45,339
FUND BALANCE - BEGINNING		108,445	
FUND BALANCE - ENDING		\$ 124,244	

**CITY OF PEQUOT LAKES, MINNESOTA
SCHEDULE OF CITY'S PROPORTIONATE
SHARE OF THE NET PENSION LIABILITY
LAST TEN YEARS (Presented Prospectively)**

For the Measurement Year Ended June 30,	City's Proportion of the Net Pension Liability (Asset)	City's Proportionate Share of the Net Pension Liability (Asset) (a)	State's Proportionate Share of the Net Pension Liability Associated with the City (b)	City's Proportionate Share of the Net Pension Liability Associated with the City (a+b)	City's Covered Payroll (c)	City's Proportionate Share of the Net Pension Liability (Asset) as a Percentage of its Covered Payroll ((a+b)/c)	Plan Fiduciary Net Position as a Percentage of the Total Pension Liability
<i>General Employees Retirement Fund Pension Plan</i>							
2018	0.0056%	\$ 310,665	\$ 10,219	\$ 320,884	\$ 373,795	85.8%	79.5%
2017	0.0054%	\$ 344,732	\$ 33,241	\$ 377,973	\$ 348,587	108.4%	75.9%
2016	0.0055%	\$ 446,573	\$ 2,970	\$ 449,543	\$ 342,732	131.2%	68.9%
2015	0.0063%	\$ 326,499	\$ -	\$ 326,499	\$ 369,980	88.2%	78.2%
<i>Public Employees Police and Fire Fund Pension Plan</i>							
2018	0.0311%	\$ 331,494	\$ -	\$ 331,494	\$ 327,432	101.2%	88.8%
2017	0.0320%	\$ 432,038	\$ -	\$ 432,038	\$ 326,444	132.3%	85.4%
2016	0.0330%	\$ 1,324,347	\$ -	\$ 1,324,347	\$ 318,651	415.6%	63.9%
2015	0.0340%	\$ 386,320	\$ -	\$ 386,320	\$ 311,104	124.2%	86.6%

Note: The schedule is provided prospectively with the City's fiscal year ended December 31, 2015 and is intended to show a ten year trend. Additional years will be reported as they become available.

**CITY OF PEQUOT LAKES, MINNESOTA
SCHEDULE OF CITY PENSION CONTRIBUTIONS
LAST TEN YEARS (Presented Prospectively)**

For the Calendar Year Ended December 31,	Statutorily Required Contribution	Contributions in Relation to the Statutorily Required Contribution	Contribution Deficiency (Excess)	City's Covered Payroll	Contributions as a Percentage of Covered Payroll
<i>General Employees Retirement Fund Pension Plan</i>					
2018	\$ 27,572	\$ 27,572	\$ -	\$ 367,622	7.5%
2017	\$ 27,434	\$ 27,434	\$ -	\$ 365,787	7.5%
2016	\$ 24,792	\$ 24,792	\$ -	\$ 330,560	7.5%
2015	\$ 27,566	\$ 27,566	\$ -	\$ 367,547	7.5%
2014	\$ 25,559	\$ 25,559	\$ -	\$ 352,531	7.3%
<i>Public Employees Police and Fire Fund Pension Plan</i>					
2018	\$ 54,743	\$ 54,743	\$ -	\$ 337,920	16.2%
2017	\$ 51,998	\$ 51,998	\$ -	\$ 320,975	16.2%
2016	\$ 52,387	\$ 52,387	\$ -	\$ 323,378	16.2%
2015	\$ 50,492	\$ 50,492	\$ -	\$ 311,680	16.2%
2014	\$ 47,017	\$ 47,017	\$ -	\$ 307,297	15.3%
<i>Pequot Lakes Firefighters Relief Association Pension Plan</i>					
2018	\$ -	\$ -	\$ -	N/A	N/A
2017	\$ -	\$ -	\$ -	N/A	N/A
2016	\$ -	\$ -	\$ -	N/A	N/A
2015	\$ -	\$ -	\$ -	N/A	N/A
2014	\$ -	\$ -	\$ -	N/A	N/A

Note: The schedule is provided prospectively with the City's fiscal year ended December 31, 2014 and is intended to show a ten year trend. Additional years will be reported as they become available.

CITY OF PEQUOT LAKES, MINNESOTA
SCHEDULE OF CHANGES IN NET PENSION LIABILITY (ASSET)
FIRE RELIEF ASSOCIATION
LAST TEN YEARS (Presented Prospectively)

	2017	2016	2015	2014
Changes in Total Pension Liability (TPL)				
Balance at January 1st	\$ 1,117,731	\$ 1,087,207	\$ 1,009,761	\$ 1,002,635
Service Cost	50,980	51,471	52,224	48,196
Interest on the TPL	43,638	45,547	38,947	36,930
Assumption Changes	-	(62,883)	-	-
Plan Changes	103,240	54,111	58,442	-
Actuarial Experience (Gains)/Losses	-	(57,722)	-	-
Benefit Payments	(155,524)	-	(72,167)	(78,000)
Balance at December 31st	<u>\$ 1,160,065</u>	<u>\$ 1,117,731</u>	<u>\$ 1,087,207</u>	<u>\$ 1,009,761</u>
Plan Fiduciary Net Position (PFNP)				
Balance at January 1st	\$ 1,587,722	\$ 1,423,957	\$ 1,392,053	\$ 1,308,978
Fire State Aid	51,257	49,001	48,895	48,390
Municipal Contributions	54,033	51,310	48,305	46,629
Projected Investment Income	62,311	58,832	12,056	71,726
Gain or Loss	53,867	11,247	-	-
Total Additions	<u>221,468</u>	<u>170,390</u>	<u>109,256</u>	<u>166,745</u>
Benefit Payments	(155,524)	-	(72,167)	(78,000)
Administrative Expenses	(9,648)	(6,625)	(5,185)	(5,670)
Total Reductions	<u>(165,172)</u>	<u>(6,625)</u>	<u>(77,352)</u>	<u>(83,670)</u>
Balance at December 31st	<u>\$ 1,644,018</u>	<u>\$ 1,587,722</u>	<u>\$ 1,423,957</u>	<u>\$ 1,392,053</u>
Net Pension Liability (Asset) - December 31st	<u>\$ (483,953)</u>	<u>\$ (469,991)</u>	<u>\$ (336,750)</u>	<u>\$ (382,292)</u>
Plan Fiduciary Net Position as a Percentage of Total Pension Liability	142%	142%	131%	138%

Note: The schedule is provided prospectively with the City's fiscal year ended December 31, 2015 (December 31, 2014 measurement date) and is intended to show a ten year trend. Additional years will be reported as they become available.

CITY OF PEQUOT LAKES, MINNESOTA
SCHEDULE OF CHANGES IN CITY'S NET OPEB LIABILITY
LAST TEN YEARS (Presented Prospectively)

	2017
Changes in Total OPEB Liability (TOL)	
Balance at January 1st	\$ 88,055
Service Cost	26,748
Interest on the TPL	3,778
Benefit Payments	(599)
Net OPEB Liability - December 31st	\$ 117,982
Covered Payroll	\$ 680,619
Net OPEB Liability / Covered Payroll	17.3%

Note: The schedule is provided prospectively beginning with the City's fiscal year ended December 31, 2018 (December 30, 2017 measurement period) and is intended to show a ten year trend. Additional years will be reported as they become available.

CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
DECEMBER 31, 2018

NOTE 1 PUBLIC EMPLOYEES RETIREMENT PLAN – GENERAL EMPLOYEES FUND

2018 Changes

Changes in Actuarial Assumptions

- The mortality projection scale was changed from MP-2015 to MP-2017.
- The assumed benefit increase was changed from 1.00 percent per year through 2044 and 2.50 percent per year thereafter to 1.25 percent per year.

2017 Changes

Changes in Plan Provisions

- The State's special funding contribution increased from \$6 million to \$16 million.

Changes in Actuarial Assumptions

- The Combined Service Annuity (CSA) loads were changed from 0.8 percent for active members and 60 percent for vested and non-vested deferred members. The revised CSA loads are now 0.0 percent for active member liability, 15.00 percent for vested deferred member liability and 3.00 percent for non-vested deferred member liability.
- The assumed post-retirement benefit increase rate was changed from 1.00 percent per year for all years to 1.00 percent per year through 2044 and 2.50 percent per year thereafter.

2016 Changes

Changes in Actuarial Assumptions

- The assumed post-retirement benefit increase rate was changed from 1.00 percent per year through 2035 and 2.50 percent per year thereafter to 1.00 percent per year for all years.
- The assumed investment return was changed from 7.90 percent to 7.50 percent. The single discount rate was changed from 7.90 percent to 7.50 percent.
- Other assumptions were changed pursuant to the experience study dated June 30, 2015. The assumed future salary increases, payroll growth, and inflation were decreased by 0.25 percent to 3.25 percent for payroll growth and 2.50 percent for inflation.

2015 Changes

Changes in Plan Provisions

- On January 1, 2015 the Minneapolis Employees Retirement Fund was merged into the General Employees Fund, which increased the total pension liability by \$1.1 billion and increased the fiduciary plan net position by \$892 million. Upon consolidation, state and employer contributions were revised; the State's contribution of \$6 million, which meets the special funding situation definition, is due September 2015.

Changes in Actuarial Assumptions

- The assumed post-retirement benefit increase rate was changed from 1.00 percent per year through 2030 and 2.50 percent per year thereafter to 1.00 percent per year through 2035 and 2.50 percent per year thereafter.

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
DECEMBER 31, 2018**

NOTE 2 DEFINED BENEFIT PENSION PLAN – POLICE AND FIRE FUND

2018 Changes

Changes in Actuarial Assumptions

- The mortality projection scale was changed from MP-2016 to MP-2017.

2017 Changes

Changes in Actuarial Assumptions

- Assumed salary increases were changed as recommended in the June 30, 2016 experience study. The net effect is proposed rates that average 0.34 percent lower than the previous rates.
- Assumed rates of retirement were changed, resulting in fewer retirements.
- The Combined Service Annuity (CSA) load was 30.0 percent for vested and non-vested deferred members. The CSA has been changed to 33.0 percent for vested members and 2.0 percent for non-vested members.
- The base mortality table for healthy annuitants was changed from the RP-2000 fully generational table to the RP-2014 fully generational table (with a base year of 2006), with male rates adjusted by a factor of 0.96. The mortality improvement scale was changed from Scale AA to Scale MP-2016. The base mortality table for disabled annuitants was changed from the RP-2000 disabled mortality table to the mortality tables assumed for healthy retirees.
- Assumed termination rates were decreased to 3.0 percent for the first three years of service. Rates beyond the select period of three years were adjusted, resulting in more expected terminations overall.
- Assumed percentage of married female members was decreased from 65.0 percent to 60.0 percent.
- Assumed age difference was changed from separate assumptions for male members (wives assumed to be three years younger) and female members (husbands assumed to be four years older) to the assumption that males are two years older than females.
- The assumed percentage of female members electing Joint and Survivor annuities was increased.
- The assumed post-retirement benefit increase rate was changed from 1.0 percent for all years to 1.0 percent per year through 2064 and 2.5 percent thereafter.
- The Single Discount Rate was changed from 5.60 percent per annum to 7.50 percent per annum.

2016 Changes

Changes in Actuarial Assumptions

- The assumed post-retirement benefit increase rate was changed from 1.00 percent per year through 2037 and 2.50 percent thereafter to 1.00 percent per year for all future years.
- The assumed investment return was changed from 7.90 percent to 7.50 percent. The single discount rate changed from 7.90 percent to 5.60 percent.
- The assumed future salary increases, payroll growth, and inflation were decreased by 0.25 percent to 3.25 percent for payroll growth and 2.50 percent for inflation.

2015 Changes

Changes in Plan Provisions

- The post-retirement benefit increase to be paid after attainment of the 90 percent funding threshold was changed, from inflation up to 2.50 percent, to a fixed rate of 2.50 percent.

Changes in Actuarial Assumptions

- The assumed post-retirement benefit increase rate was changed from 1.00 percent per year through 2030 and 2.50 percent per year thereafter to 1.00 percent per year through 2037 and 2.50 percent per year thereafter.

**CITY OF PEQUOT LAKES, MINNESOTA
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
DECEMBER 31, 2018**

NOTE 3 DEFINED BENEFIT PENSION PLAN – FIRE RELIEF ASSOCIATION

2017 Changes

Changes in Plan Provisions

- The benefit level changed from \$3,900 to \$4,250.

2016 Changes

Changes in Plan Provisions

- The benefit level changed from \$3,700 to \$3,900.

Changes in Actuarial Assumptions

- The retirement age changed from Age 50 to an age-based schedule.

2015 Changes

Changes in Actuarial Assumptions

- There were no significant changes made to actuarial assumptions during 2015.

NOTE 4 OTHER POSTEMPLOYMENT BENEFIT PLAN

2017 Changes

Changes in Plan Provisions

- The years of service required to be eligible for a benefit (implicit rate subsidy) was increased from three years to five years.
- The city contribution for union employees changed to 85% of the premium. Also, union employees are now on the same medical plan as other city employees rather than the Teamsters Local 346 plan.

Changes in Actuarial Assumptions

- The mortality table was updated from RP-2014 White Collar Mortality Tables with MP-2014 Generational Improvement Scale (with Blue Collar adjustment for Police and Fire Personnel) to the RP-2014 White Collar Mortality Tables with MP-2017 Generational Improvement Scale (with Blue Collar adjustment for Police and Fire Personnel).
- The retirement and withdrawal tables for all employees were updated.
- The discount rate was changed from 4.00% to 3.30%.

Method Changes

- The actuarial cost method was changed from projected unit credit to entry age as prescribed by GASB 75.

**SUPPLEMENTARY
INFORMATION**

**CITY OF PEQUOT LAKES, MINNESOTA
COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS
DECEMBER 31, 2018**

	Cemetery Perpetual Care	Business Park	2014 Equipment Certificates	2010 Equipment Certificates	Total Nonmajor Funds
ASSETS					
Cash, Cash Equivalents and Investments	\$ 68,315	\$ 307,918	\$ 49,035	\$ 49	\$ 425,317
Property Taxes Receivable	-	-	3,522	117	3,639
Land Held for Resale	-	46,982	-	-	46,982
TOTAL ASSETS	<u>\$ 68,315</u>	<u>\$ 354,900</u>	<u>\$ 52,557</u>	<u>\$ 166</u>	<u>\$ 475,938</u>
LIABILITIES					
Accounts Payable	\$ -	\$ 8,500	\$ -	\$ -	\$ 8,500
DEFERRED INFLOWS OF RESOURCES					
Unavailable Revenue:					
Property Taxes	-	-	2,491	117	2,608
FUND BALANCES					
Nonspendable	-	46,982	-	-	46,982
Restricted	-	-	50,066	49	50,115
Committed	68,315	299,418	-	-	367,733
Total Fund Balances	<u>68,315</u>	<u>346,400</u>	<u>50,066</u>	<u>49</u>	<u>464,830</u>
TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND FUND BALANCES	<u>\$ 68,315</u>	<u>\$ 354,900</u>	<u>\$ 52,557</u>	<u>\$ 166</u>	<u>\$ 475,938</u>

CITY OF PEQUOT LAKES, MINNESOTA
COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
NONMAJOR GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2018

	Cemetery Perpetual Care	Business Park	2014 Equipment Certificates	2010 Equipment Certificates	Total Nonmajor Funds
REVENUES					
Taxes	\$ -	\$ -	\$ 43,039	\$ 81	\$ 43,120
Charges for Services	1,600	-	-	-	1,600
Investment Income	869	4,143	454	-	5,466
Miscellaneous	1	-	-	-	1
TOTAL REVENUES	<u>2,470</u>	<u>4,143</u>	<u>43,493</u>	<u>81</u>	<u>50,187</u>
EXPENDITURES					
Current:					
General Government	299	-	-	-	299
Public Safety	-	-	-	257	257
Public Works	-	-	286	-	286
Economic Development	-	51,739	-	-	51,739
Debt Service:					
Principal	-	-	39,250	-	39,250
Interest and Other Charges	-	-	1,491	-	1,491
TOTAL EXPENDITURES	<u>299</u>	<u>51,739</u>	<u>41,027</u>	<u>257</u>	<u>93,322</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	2,171	(47,596)	2,466	(176)	(43,135)
OTHER FINANCING SOURCES					
Proceeds from the Sale of Assets	-	921	-	-	921
Operating Transfers In	-	21,198	-	-	21,198
TOTAL OTHER FINANCING SOURCES	<u>-</u>	<u>22,119</u>	<u>-</u>	<u>-</u>	<u>22,119</u>
NET CHANGE IN FUND BALANCES	2,171	(25,477)	2,466	(176)	(21,016)
FUND BALANCES - BEGINNING	<u>66,144</u>	<u>371,877</u>	<u>47,600</u>	<u>225</u>	<u>485,846</u>
FUND BALANCES - ENDING	<u>\$ 68,315</u>	<u>\$ 346,400</u>	<u>\$ 50,066</u>	<u>\$ 49</u>	<u>\$ 464,830</u>

**CITY OF PEQUOT LAKES, MINNESOTA
SCHEDULE OF INDEBTEDNESS
FOR THE YEAR ENDED DECEMBER 31, 2018
(UNAUDITED)**

	Issue Date	Interest Rates	Maturity Date	Initial Authorized Issue	Outstanding Balance 01/01/18	Issued	Paid	Outstanding Balance 12/31/18	Principal Due in 2019
GOVERNMENTAL ACTIVITIES									
G.O. Equipment Certificate, Series 2014A	1/17/2014	2.50%	2/1/2019	\$ 193,000	\$ 79,250	\$ -	\$ 39,250	\$ 40,000	\$ 40,000
G.O. Equipment Certificate, Series 2017A	2/15/2017	2.99%	8/1/2022	135,000	135,000	-	9,100	125,900	30,100
Community Facility Loan - Fire Truck	2/1/2014	3.50%	2/1/2019	350,000	293,650	-	20,113	273,537	20,817
City Hall Building Capital Lease	2/27/2004	4.00%	3/1/2024	1,097,442	187,042	-	24,984	162,058	26,001
Copier Machine Capital Lease	3/1/2014	14.67%	3/31/2018	9,866	683	-	683	-	-
Postage Machine Capital Lease	10/6/2015	10.00%	12/31/2020	4,544	2,881	-	866	2,015	958
TOTAL GOVERNMENTAL ACTIVITY DEBT				1,789,852	698,506	-	94,996	603,510	117,876
BUSINESS-TYPE ACTIVITIES									
G.O. Utility Refunding Bonds, Series 2012A	2/12/2013	0.60-3.10%	8/20/2031	1,270,000	970,000	-	60,000	910,000	60,000
Postage Machine Capital Lease	10/6/2015	10.00%	12/31/2020	3,029	1,920	-	578	1,342	638
TOTAL BUSINESS-TYPE ACTIVITY DEBT				1,273,029	971,920	-	60,578	911,342	60,638
TOTAL INDEBTEDNESS				<u>\$ 3,062,881</u>	<u>\$ 1,670,426</u>	<u>\$ -</u>	<u>\$ 155,574</u>	<u>\$ 1,514,852</u>	<u>\$ 178,514</u>

OTHER REQUIRED REPORTS

**INDEPENDENT AUDITORS' REPORT ON INTERNAL
CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE
AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL
STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

May 28, 2019

Honorable Mayor and City Council
City of Pequot Lakes, Minnesota

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Pequot Lakes, Minnesota (the City) as of and for the year ended December 31, 2018, and the related notes to the financial statements, which collectively comprise the City of Pequot Lakes' basic financial statements, and have issued our report thereon dated May 28, 2019.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City of Pequot Lakes' 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 have not been identified. However, as described in the accompanying *Schedule of Findings and Responses*, we identified certain deficiencies in internal control that we consider to be a material weakness and significant deficiency.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. We consider the following deficiency described in the accompanying *Schedule of Findings and Responses* to be a material weakness: 2006-002.

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the following deficiency described in the accompanying *Schedule of Findings and Responses* to be a significant deficiency: 2006-001.

Compliance and Other Matters

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

City's Response to Findings

The City of Pequot Lakes' response to the findings identified in our audit is described in the accompanying *Schedule of Findings and Responses* and *Corrective Action Plans*. The City's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the City'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.

SCHLENNER WENNER & CO.

St. Cloud, Minnesota

**INDEPENDENT AUDITORS' REPORT ON
MINNESOTA LEGAL COMPLIANCE**

May 28, 2019

Honorable Mayor and City Council
City of Pequot Lakes, Minnesota

We have audited, in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of the City of Pequot Lakes, Minnesota (the City) as of and for the year ended December 31, 2018, and the related notes to the financial statements, and have issued our report thereon dated May 28, 2019.

The *Minnesota Legal Compliance Audit Guide for Cities*, promulgated by the State Auditor pursuant to Minnesota Statute Section 6.65, contains seven categories of compliance to be tested: deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, contracting and bidding, tax increment financing and miscellaneous provisions. 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 the following findings described in the accompanying *Schedule of Findings and Responses*: 2018-001 and 2018-002.

However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the City's noncompliance with the above referenced provisions.

This report is intended solely for the information and use of those charged with governance and management of the City of Pequot Lakes, Minnesota and the State Auditor and is not intended to be, and should not be, used by anyone other than these specified parties.

SCHLENNER WENNER & CO.
St. Cloud, Minnesota

**CITY OF PEQUOT LAKES, MINNESOTA
SCHEDULE OF FINDINGS AND RESPONSES
DECEMBER 31, 2018**

FINANCIAL STATEMENT FINDINGS (Continued)

Finding 2006-002 Financial Statement Preparation (Continued)

*Views of Responsible
Officials And Planned
Corrective Action:*

The City will continue to have Schlenner Wenner & Co. prepare the financial statements and assist with year-end adjustments as necessary, but will review the cost/benefit of preparing financial statements internally on an annual basis. See corresponding Corrective Action Plan.

LEGAL COMPLIANCE FINDINGS

Finding 2018-001 Withholding Affidavit for Contractors

Condition: The City failed to obtain certification from contractors that a Withholding Affidavit for Contractors was submitted to the Department of Revenue.

Criteria: Under Minnesota Statute 270C.66, the City is required to obtain certification from contractors that a Withholding Affidavit for Contractors was submitted to the Department of Revenue prior to making final payment to each contractor.

Cause: The City failed to obtain certification before making final payments to a contractor.

Effect: The failure to obtain such certification resulted in the City's noncompliance with Minnesota Statutes.

Recommendation: We recommend management require future contractors to provide documentation that a Withholding Affidavit for Contractors was submitted to the Department of Revenue prior to the City making final payment on a contract.

*Views of Responsible
Officials And Planned
Corrective Action:*

Management agrees with the recommendation. See corresponding Corrective Action Plan.

Finding 2018-002 Late Fire Relief Association Payment

Condition: The City failed to remit Fire State Aid dollars to the Pequot Lakes Fire Relief Association within the 30 day window prescribed by Minnesota Statutes.

Criteria: On an annual basis, the City collects Fire State Aid from the State of Minnesota, which is earmarked for the Pequot Lakes Fire Relief Association. Under Minnesota Statute 69.031, subdivision 5, the City must transmit these funds (along with any supplement Fire State Aid received) to the relief association within 30 days of being received by City.

Cause: The City failed to remit the funds to the relief association within the prescribed time frame.

Effect: The failure to pay within the prescribed time frame resulted in the City's noncompliance with Minnesota Statutes.

Recommendation: We recommend management closely monitor the receipt of future Fire State Aid and ensure the timely disbursement of these funds to the fire relief association within 30 days of receipt.

**CITY OF PEQUOT LAKES, MINNESOTA
SCHEDULE OF FINDINGS AND RESPONSES
DECEMBER 31, 2018**

LEGAL COMPLIANCE FINDINGS (Continued)

Finding 2018-002 Late Fire Relief Association Payment (Continued)

*Views of Responsible
Officials And Planned
Corrective Actions:*

Management agrees with the recommendation. See corresponding Corrective Action Plan.

**CITY OF PEQUOT LAKES, MINNESOTA
CORRECTIVE ACTION PLANS
DECEMBER 31, 2018**

FINANCIAL STATEMENT FINDINGS

Finding 2006-001 Limited Segregation of Duties

1. Explanation of Disagreement with Audit Finding
There is no disagreement with the audit finding.
2. Actions Planned in Response to Finding
The City will review current procedures and implement additional controls where possible.
3. Official Responsible
Nancy Malecha, City Administrator, is the official responsible for ensuring corrective action.
4. Planned Completion Date
The Corrective Action Plan will be reviewed on an ongoing basis with no anticipated completion date.
5. Plan to Monitor Completion
The City Council will be monitoring this Corrective Action Plan.

Finding 2006-002 Financial Statement Preparation

1. Explanation of Disagreement with Audit Finding
There is no disagreement with the audit finding.
2. Actions Planned in Response to Finding
The City will continue to have the auditor prepare the financial statements and assist with certain adjustments, and management will document their annual review of this information. The City will revisit this decision on an annual basis.
3. Official Responsible
Nancy Malecha, City Administrator, is the official responsible for ensuring corrective action.
4. Planned Completion Date
The Corrective Action Plan will be reviewed on an ongoing basis with no anticipated completion date.
5. Plan to Monitor Completion
The City Council will be monitoring this Corrective Action Plan.

**CITY OF PEQUOT LAKES, MINNESOTA
CORRECTIVE ACTION PLANS
DECEMBER 31, 2018**

LEGAL COMPLIANCE FINDINGS

Finding 2018-001 Withholding Affidavit for Contractors

1. Explanation of Disagreement with Audit Finding
There is no disagreement with the audit finding.
2. Actions Planned in Response to Finding
The City will require future contractors to provide documentation that a Withholding Affidavit for Contractors was submitted to the Department of Revenue prior to the City making final payment on a contract.
3. Official Responsible
Nancy Malecha, City Administrator, is the official responsible for ensuring corrective action.
4. Planned Completion Date
The planned completion date is December 31, 2019.
5. Plan to Monitor Completion
The City Council will be monitoring this Corrective Action Plan.

Finding 2018-002 Late Fire Relief Association Payment

1. Explanation of Disagreement with Audit Finding
There is no disagreement with the audit finding.
2. Actions Planned in Response to Finding
The City will closely monitor the timing of future Fire State Aid receipts, and ensures the timely disbursement of these funds to the fire relief association within the prescribed time frame.
3. Official Responsible
Nancy Malecha, City Administrator, is the official responsible for ensuring corrective action.
4. Planned Completion Date
The planned completion date is December 31, 2019.
5. Plan to Monitor Completion
The City Council will be monitoring this Corrective Action Plan.