

FINANCIAL STATEMENTS AND INDEPENDENT AUDITOR'S REPORT

FOR THE YEAR ENDED DECEMBER 31, 2011

CITY OF STURGIS



Ketel Thorstenson, LLP

Certified Public Accountants/Business & Personal Consultants

810 Quincy Street • Rapid City, SD 57701 • www.ktllp.com

CITY OF STURGIS

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Ketel Thorstenson, LLP

Certified Public Accountants/Business & Personal Consultants

810 Quincy Street
P.O. Box 3140, Rapid City, South Dakota 57709
Telephone (605) 342-5630 • e-mail: ktllp@ktllp.com

INDEPENDENT AUDITOR'S REPORT

City Council
City of Sturgis
Sturgis, South Dakota

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 STURGIS** (the City), Meade County, South Dakota, as of and for the year ended December 31, 2011, which collectively comprise the City's basic financial statements as listed in the Table of Contents. These financial statements are the responsibility of the City's management. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our 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 as of December 31, 2011, and the respective changes in financial position and cash flows, where applicable, for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated September 19, 2012, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards, and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 11, and the required supplementary budgetary information on pages 40 through 44 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 regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We 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.

City Council

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's financial statements as a whole. The combining nonmajor fund financial statements and schedule of rally activities on pages 45 through 47 are presented for purposes of additional analysis and are not a required part of the financial statements. The schedule of expenditures of federal awards on page 52 is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is also not a required part of the basic financial statements of the City. The combining nonmajor fund financial statements, schedule of expenditures of federal awards, and schedule of rally activities are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements taken as a whole.



KETEL THORSTENSON, LLP
Certified Public Accountants

September 19, 2012

CITY OF STURGIS

MANAGEMENT'S DISCUSSION AND ANALYSIS DECEMBER 31, 2011

This section of the City of Sturgis' annual financial report presents our discussion and analysis of the City's financial performance during the fiscal year ended on December 31, 2011. Please read it in conjunction with the City's financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

- During the year, the City's revenues generated from charges for services, taxes and other revenues of the governmental programs were \$199,914 more than the \$8,398,107 governmental program expenditures. This does not take into account any transfers in/out. The overall change in net assets, transfers included, in governmental activities increased three percent compared to last year.
- In the City's business-type activities, expenses exceeded revenues by \$148,364, which includes transfers and any activity due to the disposal of fixed assets. The decrease is due to significant capital grants not received in 2011 that had been received in the prior year.

OVERVIEW OF THE FINANCIAL STATEMENTS

The financial report is presented in a format consistent with the presentation requirements of the Governmental Accounting Standards Board (GASB) Statement 34.

This annual report consists of three parts – management's discussion and analysis (this section), the basic financial statements (including related notes), and required supplementary information. The basic financial statements include two kinds of statements that present different views of the City:

- The first two statements are government-wide financial statements that provide both long-term and short-term information about the City's overall financial status.
- The remaining statements are fund financial statements that focus on individual parts of the City government, reporting the City's operations in more detail than the government-wide statements.
 - The governmental funds statements tell how general government services like public safety were financed in the short-term, as well as what remains for future spending.
 - Proprietary fund statements offer short-term and long-term financial information about the activities that the City operates like businesses. The City has five proprietary funds – the Liquor Fund, Water Fund, Wastewater Fund, Sanitation Fund and Ambulance Fund.

The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of required supplementary information that further explains and supports the information in the financial statements. In addition to the required elements, we have included a section with combining statements that provide details about our non-major governmental funds, each of which are added together and presented in a single column in the basic financial statements.

CITY OF STURGIS

**MANAGEMENT’S DISCUSSION AND ANALYSIS (CONTINUED)
DECEMBER 31, 2011**

OVERVIEW OF THE FINANCIAL STATEMENTS (CONTINUED)

Figure A-1 summarizes the major features of the City’s financial statements, including the portion of the City government they cover and the types of information they contain. The remainder of the overview section of the management’s discussion and analysis explains the structure and contents of each of the statements.

Figure A-1

	Government-wide Statements	Fund Statements	
		Governmental Funds	Proprietary Funds
Scope	Entire City government (except fiduciary funds and the fiduciary component units)	The activities of the City that are not proprietary or fiduciary, such as finance office, police, fire and parks	Activities the City operates similar to private businesses, such as the water and sewer systems
Required Financial Statements	Statement of Net Assets and Statement of Activities	Balance Sheet and Statement of Revenues, Expenditures, and Changes in Fund Balances	Balance Sheet; Statement of Revenues, Expenses, and Changes in Net Assets; and Statement of Cash Flows
Accounting Basis and Measurement Focus	Accrual accounting and economic resources focus	Modified accrual accounting and current financial resources focus	Accrual accounting and economic resources focus
Type of Asset/Liability Information	All assets and liabilities, both financial and capital, and short-term and long-term	Only assets expected to be used up and liabilities that come due during the year or soon thereafter, no capital assets included	All assets and liabilities, both financial and capital, and short-term and long-term
Type of Inflow/Outflow Information	All revenues and expenses during year, regardless of when cash is received or paid	Revenues for which cash is received during or soon after the end of the year; expenditures when goods or services have been received and payment is due during the year or soon thereafter	All revenues and expenses during year, regardless of when cash is received or paid

Government-wide Statements

The government-wide statements report information about the City as a whole using accounting methods similar to those used by private-sector companies. The statement of net assets includes all of the government’s assets and liabilities. All of the current year’s revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

CITY OF STURGIS

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED) DECEMBER 31, 2011

OVERVIEW OF THE FINANCIAL STATEMENTS (CONCLUDED)

Government-wide Statements (Continued)

The two government-wide statements report the City's net assets and how they have changed. Net assets – the difference between the City's assets and liabilities – is one way to measure the City's financial health or position.

- Increases or decreases in the City's net assets are an indicator of whether its financial health is improving or deteriorating, respectively.
- To assess the overall health of the City you need to consider additional non-financial factors such as changes in the City's property tax base and changes in the sales tax revenue base.

The government-wide financial statements of the City are reported in two categories:

- **Governmental Activities** -- This category includes most of the City's basic services, such as police, fire, public works, parks department and general administration. Property taxes, sales taxes, charges for services, state and federal grants, and interest earnings finance most of these activities.
- **Business-type Activities** -- The City charges a fee to customers to help cover the costs of certain services it provides. The City's liquor, water, wastewater, sanitation, and ambulance funds are included here.

Fund Financial Statements

The fund financial statements provide more detailed information about the City's most significant funds – not the City as a whole. Funds are accounting devices that the City uses to keep track of specific sources of funding and spending for particular purposes. State law requires some of the funds. The City Council establishes other funds to control and manage money for particular purposes or to show that it is properly using certain taxes and grants.

The City has two kinds of funds:

- **Governmental Funds** – Most of the City's basic services are included in the governmental funds, which focus on (1) how cash and other financial assets that can readily be converted to cash flow in and out and (2) the balances left at the year-end that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that 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. Because this information does not encompass the additional long-term focus of the government-wide statements, we provide additional information at the bottom of the governmental funds' statements, or on the subsequent page, that explains the relationship (or differences) between them.
- **Proprietary Funds** – Services for which the City charges customers a fee are generally reported in proprietary funds. Proprietary funds, like the government-wide statements, provide both short-term and long-term financial information. The City's enterprise funds are the same as its business-type activities, but provide more detail and additional information, such as cash flows.

CITY OF STURGIS

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
DECEMBER 31, 2011**

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

Net Assets

The City's combined net assets increased one percent between fiscal year 2010 and 2011. (See Table A-1).

Table A-1 Summarized Statement of Net Assets						
	Governmental Activities		Business-Type Activities		Total	
	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>
Current and Other Assets	\$ 5,166,440	\$ 5,455,579	\$ 2,216,229	\$ 1,858,977	\$ 7,382,669	\$ 7,314,556
Capital Assets	33,550,581	33,715,061	18,219,729	17,769,328	51,770,310	51,484,389
Total Assets	\$ 38,717,021	\$39,170,640	\$ 20,435,958	\$19,628,305	\$ 59,152,979	\$58,798,945
Long-Term Debt	\$ 5,776,740	\$ 6,184,990	\$ 3,882,866	\$ 3,478,286	\$ 9,659,606	\$ 9,663,276
Other Liabilities	368,769	756,582	366,126	325,309	734,895	1,081,891
Total Liabilities	6,145,509	6,941,572	4,248,992	3,803,595	10,394,501	10,745,167
<i>Net Assets:</i>						
Invested in Capital Assets, Net of Related Debt	27,969,580	27,704,060	14,404,377	14,085,496	42,373,957	41,789,556
Restricted	3,583,942	3,323,038	4,098	-	3,588,040	3,323,038
Unrestricted	1,017,990	1,201,970	1,778,491	1,739,214	2,796,481	2,941,184
Total Net Assets	\$ 32,571,512	\$32,229,068	\$ 16,186,966	\$15,824,710	\$ 48,758,478	\$48,053,778
Beginning Net Assets (Note 11)	31,718,448	29,639,828	16,335,330	15,208,480	48,053,778	44,848,308
Increase in Net Assets	\$ 853,064	\$ 2,589,240	\$ (148,364)	\$ 616,230	\$ 704,700	\$ 3,205,470
Percentage of Increase in Net Assets	3%	9%	-1%	4%	1%	7%

The Statement of Net Assets reports all financial and capital resources. The statement presents the assets and liabilities in order of relative liquidity. The liabilities with average maturities greater than one year are reported in two components – the amount due within one year and the amount due in more than one year. The difference between the City's assets and liabilities is its net assets.

Changes in Net Assets

The City's revenues totaled \$14,498,244 (See Table A-2). Well over half of the City's revenue comes from charges for services and taxes, with 51 cents of every dollar raised coming from charges for services (primarily liquor and water operations) and 39 cents of every dollar raised coming from some type of tax (See Figure A-2). Of the City's total revenue, 6 percent comes from state and federal grants for capital purposes, and the rest comes from operating grants, contributions, state shared revenue, interest and miscellaneous.

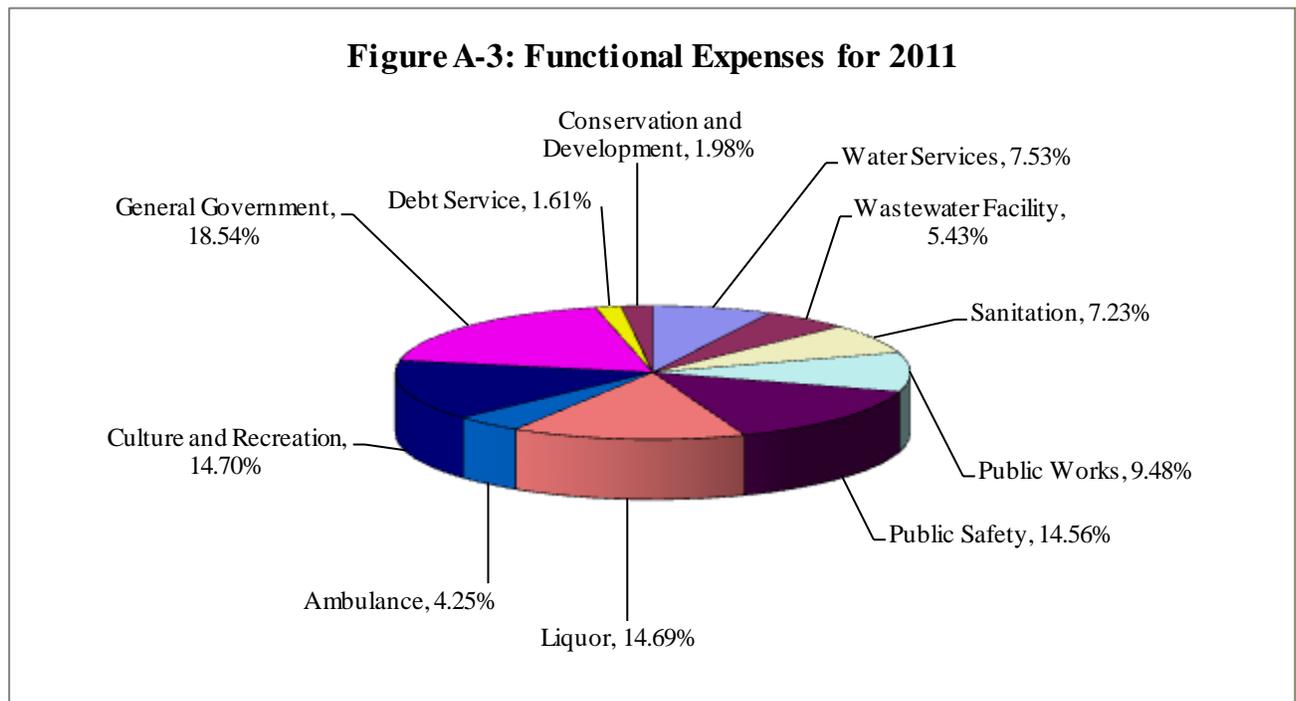
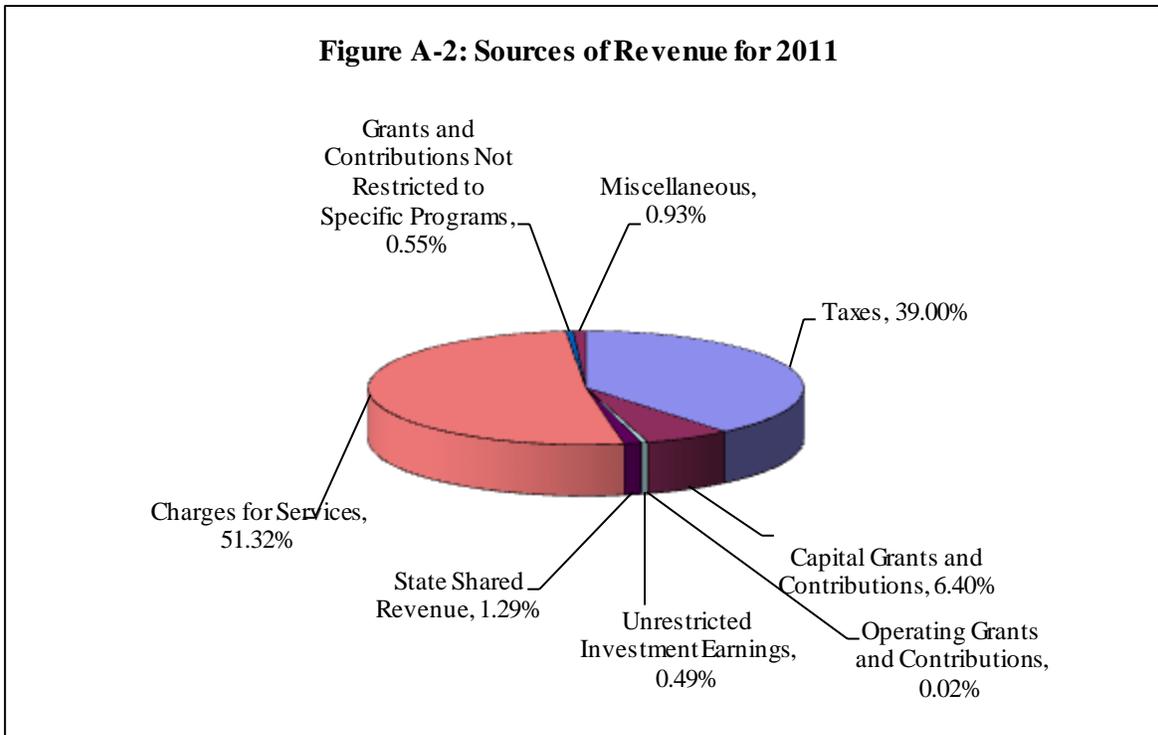
CITY OF STURGIS

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
DECEMBER 31, 2011**

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONTINUED)

Changes in Net Assets (Continued)

The total cost of all programs and services was \$13,793,544 (See Table A-2). The City's expenses cover a range of services, including road maintenance, parks and recreation services and sewer system services. (See Figure A-3).



CITY OF STURGIS

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
DECEMBER 31, 2011**

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONTINUED)

Changes in Net Assets (Conclude-d)

Table A-2 and the narrative that follows consider the operations of the governmental and business - type activities.

Table A-2						
Changes in Net Assets						
	Governmental Activities		Business - Type Activities		Total	
	2011	2010	2011	2010	2011	2010
Revenues						
Program Revenues						
Charges for Services	\$ 1,633,261	\$ 2,228,269	\$ 5,806,484	\$ 4,707,829	\$ 7,439,745	\$ 6,936,098
Operating Grants and Contributions	2,282	100,421	-	-	2,282	100,421
Capital Grants and Contributions	882,891	2,307,828	44,276	463,919	927,167	2,771,747
General Revenues						
Taxes	5,654,893	6,091,079	-	-	5,654,893	6,091,079
State Shared Revenue	187,344	191,065	-	-	187,344	191,065
Grants and Contributions not Program Specific	80,625	27,651	-	-	80,625	27,651
Unrestricted Investment Earnings	49,049	89,064	21,435	22,184	70,484	111,248
Miscellaneous	107,676	99,124	28,028	3,268	135,704	102,392
Total Revenues	8,598,021	11,134,501	5,900,223	5,197,200	14,498,244	16,331,701
Expenses						
General Government	2,557,890	2,376,696	-	-	2,557,890	2,376,696
Public Safety	2,008,909	1,939,302	-	-	2,008,909	1,939,302
Public Works	1,307,224	844,737	-	-	1,307,224	844,737
Health and Welfare	365	498,609	-	-	365	498,609
Culture and Recreation	2,028,141	1,907,030	-	-	2,028,141	1,907,030
Conservation and Development	273,546	456,918	-	-	273,546	456,918
Debt Service	222,032	551,916	-	-	222,032	551,916
Liquor	-	-	2,026,433	1,753,787	2,026,433	1,753,787
Water Services	-	-	1,038,152	1,181,895	1,038,152	1,181,895
Wastewater Services	-	-	748,589	803,488	748,589	803,488
Sanitation Services	-	-	996,604	811,853	996,604	811,853
Ambulance	-	-	585,659	-	585,659	-
Total Expenses	8,398,107	8,575,208	5,395,437	4,551,023	13,793,544	13,126,231
Excess Before Transfers	199,914	2,559,293	504,786	646,177	704,700	3,205,470
Transfers	653,150	584,916	(653,150)	(584,916)	-	-
Increase (Decrease) in Net Assets	853,064	3,144,209	(148,364)	61,261	704,700	3,205,470
Ending Net Assets (Note 11)	\$ 32,571,512	\$ 31,718,448	\$ 16,186,966	\$ 16,335,330	\$ 48,758,478	\$ 48,053,778

CITY OF STURGIS

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED) DECEMBER 31, 2011

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONCLUDED)

Governmental Activities

Total revenues of the governmental activities for the City decreased by 23 percent compared to the prior year, while total expenses decreased by two percent. The primary reason for the decrease of revenue is that the City had more capital grants and contributions to fund projects in the prior year.

Business-Type Activities

Operating revenues of the City's business-type activities increased by approximately 14 percent compared to the prior year, while total expenses increased approximately 19 percent. The overall increase in revenues and expenses is due to the Ambulance and Special Sanitation Funds becoming enterprise funds in the current year.

FINANCIAL ANALYSIS OF THE CITY'S FUNDS

The financial analysis of the City's funds mirror those highlighted in the analysis of governmental and business-type activities presented above. The City maintains governmental fund types - General, Special Revenue Funds (including the Capital Improvement Fund), Debt Service Funds (including the Revolving Loan Fund), Capital Projects Funds and Permanent Funds. The City also maintains five business type funds - Liquor, Water, Wastewater, Sanitation and Ambulance Funds.

BUDGETARY HIGHLIGHTS

Over the course of the year, the City Council revised the City budget two times. These amendments fall into two categories:

- Move contingency money to funds to prevent budget overruns
- Supplemental appropriations to increase the budget to prevent budget overruns

The Capital Improvement Fund budget had one unfavorable variance totaling \$16,574 within the airport function. Supplemental appropriations should have been made to cover the additional expenses for the airport construction.

CITY OF STURGIS

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
DECEMBER 31, 2011**

CAPITAL ASSET ADMINISTRATION

By the end of 2011, the City had invested \$51,770,310 in a broad range of capital assets, including, land, buildings, and various machinery and equipment. (See Table A-3). This amount represents a net increase (including additions and deductions) of \$285,921.

Table A-3 Capital Assets (net of depreciation)				
	Governmental Activities (Note 11)		Business-type Activities (Note 11)	
	2011	2010	2011	2010
Land	\$ 2,184,497	\$ 2,184,497	\$ 826,108	\$ 741,941
Construction Work in Progress	106,575	2,589,424	602,476	633,223
Buildings	9,142,763	9,415,693	1,814,199	1,056,649
Improvements Other Than Buildings	20,607,499	17,946,009	13,780,761	14,120,139
Machinery and Equipment	1,509,247	1,579,438	1,196,185	1,217,376
Total Capital Assets	\$ 33,550,581	\$ 33,715,061	\$ 18,219,729	\$ 17,769,328

LONG-TERM DEBT

At year-end, the City had \$9,659,606 in Sales Tax Revenue Bonds, General Obligation Bonds and other long-term obligations. This is a decrease of \$3,670 as shown on Table A-4 below.

Table A-4 Outstanding Debt and Obligations				
	Governmental Activities		Business-type Activities	
	2011	2010	2011	2010
Compensated Absences	\$ 195,739	\$ 173,989	\$ 67,514	\$ 60,702
Tax Increment Financing Obligations	406,001	406,001	-	-
Sales Tax Revenue Bonds	5,175,000	5,605,000	1,895,352	1,207,584
General Obligation Bonds	-	-	1,920,000	2,210,000
Total Outstanding Debt and Obligations	\$ 5,776,740	\$ 6,184,990	\$ 3,882,866	\$ 3,478,286

During the current year, the City obtained interim financing for the Drinking Water Project. The City made scheduled payments throughout the year on its debt balances.

CITY OF STURGIS

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONCLUDED) DECEMBER 31, 2011

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The City's current economic position has remained consistent and strong, with the foundations of the area's economy continuing to show resilience despite the nation's current economic turbulence. There was a moderate increase in total property valuation of \$8,457,943 or 2.5%. The City did not request an increase in the total property tax collection in 2011. With a growth factor of 0.48%, the City was able to reduce the total City mill levy.

The second largest portion of revenue within the general fund is retail sales tax. In 2011, the City experienced a decline of 2.5% compared to 2010. This decline was largely due to reduced tourist traffic during the annual Motorcycle Rally. This is a typical pattern as significant anniversaries draw additional visitors, as was experienced in 2010.

The adopted 2012 general fund expenditures budget is largely flat, increasing by only \$16,335. In order to fund additional labor costs, the City has reduced other operating expenses.

The majority of the City's business-type activities (liquor, water, wastewater, and ambulance) are anticipated to have similar results in 2012 as compared to 2011. The sanitation fund is likely to end 2012 better than 2011 due to changes in Rally-related income.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the City's finances and to demonstrate the City's accountability for the money it receives. If you have questions about this report or need additional information, contact the City of Sturgis' Finance Office, 1040 2nd Street, Suite 103, Sturgis, SD 57785.

CITY OF STURGIS

STATEMENT OF NET ASSETS
DECEMBER 31, 2011

	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTAL
Assets			
Cash and Cash Equivalents (Note 2)	\$ 3,340,776	\$ 1,596,985	\$ 4,937,761
Restricted Cash in Banks	-	4,098	4,098
Receivables, Net	621,504	280,988	902,492
Notes Receivable (Note 10)	312,951	50,000	362,951
Internal Balances (Note 6)	(35,000)	35,000	-
Inventories	1,051	235,810	236,861
Deferred Charges	137,205	-	137,205
Other Assets	26,344	13,348	39,692
Restricted Assets:			
Cash with Fiscal Agent (Note 5)	625,765	-	625,765
Deposits (Note 9)	135,844	-	135,844
Capital Assets (Note 4)			
Land and Construction Work in Progress	2,291,072	1,428,584	3,719,656
Other Capital Assets, Net of Depreciation	31,259,509	16,791,145	48,050,654
Total Assets	\$ 38,717,021	\$ 20,435,958	\$ 59,152,979
Liabilities			
Accounts Payable	\$ 211,913	\$ 169,447	\$ 381,360
Other Current Liabilities	156,856	196,679	353,535
Noncurrent Liabilities (Note 5):			
Due Within One Year	682,034	433,029	1,115,063
Due in More Than One Year	5,094,706	3,449,837	8,544,543
Total Liabilities	6,145,509	4,248,992	10,394,501
Net Assets			
Invested in Capital Assets, Net of Related Debt	27,969,580	14,404,377	42,373,957
Restricted for:			
Capital Outlay	1,025,180	-	1,025,180
Debt Service	635,461	4,098	639,559
SDPAA (Note 9)	135,844	-	135,844
Revolving Loans	998,027	-	998,027
BID Tax	96,081	-	96,081
Library Purposes	213,244	-	213,244
Permanently Restricted Purposes:			
Expendable	102,570	-	102,570
Nonexpendable	377,535	-	377,535
Unrestricted	1,017,990	1,778,491	2,796,481
Total Net Assets	32,571,512	16,186,966	48,758,478
Total Liabilities and Net Assets	\$ 38,717,021	\$ 20,435,958	\$ 59,152,979

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2011

	----- Program Revenues -----				Net (Expense) Revenue and ----- Changes in Net Assets -----		
	Expenses	Charges for Services	Operating	Capital	Governmental Activities	Business-Type Activities	Total
			Grants and Contributions	Grants and Contributions			
Functions/Programs							
Primary Government							
Governmental Activities:							
General Government	\$ 2,557,890	\$ 1,257,126	\$ -	\$ -	\$ (1,300,764)	\$ -	\$ (1,300,764)
Public Safety	2,008,909	44,867	-	-	(1,964,042)	-	(1,964,042)
Public Works	1,307,224	30,480	2,282	873,460	(401,002)	-	(401,002)
Health and Welfare	365	634	-	-	269	-	269
Culture and Recreation	2,028,141	300,154	-	9,431	(1,718,556)	-	(1,718,556)
Conservation and Development	273,546	-	-	-	(273,546)	-	(273,546)
Interest on Long-Term Debt	222,032	-	-	-	(222,032)	-	(222,032)
Total Governmental Activities	8,398,107	1,633,261	2,282	882,891	(5,879,673)	-	(5,879,673)
Business-Type Activities:							
Liquor	2,026,433	2,067,314	-	-	-	40,881	40,881
Water	1,038,152	1,158,857	-	-	-	120,705	120,705
Wastewater	748,589	949,175	-	-	-	200,586	200,586
Sanitation	996,604	1,017,862	-	44,276	-	65,534	65,534
Ambulance	585,659	613,276	-	-	-	27,617	27,617
Total Business-Type Activities	5,395,437	5,806,484	-	44,276	-	455,323	455,323
Total Primary Government	\$ 13,793,544	\$ 7,439,745	\$ 2,282	\$ 927,167	(5,879,673)	455,323	(5,424,350)
General Revenues:							
Taxes:							
Property Taxes					2,716,185	-	2,716,185
Sales Taxes					2,938,708	-	2,938,708
State Shared Revenue					187,344	-	187,344
Grants and Contributions Not Restricted							
to Specific Programs					80,625	-	80,625
Unrestricted Investment Earnings					49,049	21,435	70,484
Miscellaneous Revenue					107,676	28,028	135,704
Transfers					653,150	(653,150)	-
Total General Revenues and Transfers					6,732,737	(603,687)	6,129,050
Change in Net Assets					853,064	(148,364)	704,700
Net Assets, Beginning (Note 11)					31,718,448	16,335,330	48,053,778
Net Assets, Ending					\$ 32,571,512	\$ 16,186,966	\$ 48,758,478

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

BALANCE SHEET - GOVERNMENTAL FUNDS
DECEMBER 31, 2011

	<u>General Fund</u>	<u>Capital Improvement Fund</u>	<u>Revolving Loan Fund</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Assets					
101 Cash	\$ 10,650	\$ -	\$ -	\$ -	\$ 10,650
104 Interest Bearing Accounts	647,671	882,434	996,137	376,349	2,902,591
105 Savings Certificates	-	-	-	427,535	427,535
106 Restricted Cash with Fiscal Agent (Note 5)	-	625,765	-	-	625,765
108 Property Taxes Receivable	229,425	-	-	-	229,425
108 Sales Tax Receivable	86,804	86,804	-	13,302	186,910
115 Accounts Receivable	46,738	100,562	1,890	-	149,190
116 Estimated Uncollectible Accounts Receivable	(10,000)	-	-	-	(10,000)
121 Special Assessments Receivable	4,640	26,451	-	-	31,091
128 Notes Receivable (Note 10)	-	-	312,951	-	312,951
132 Due from Federal/State Government	34,888	-	-	-	34,888
142 Inventory of Supplies Purchased for Resale	1,051	-	-	-	1,051
154.1 Restricted Deposits	135,844	-	-	-	135,844
155 Prepaid Expense	26,344	-	-	-	26,344
Total Assets	\$ 1,214,055	\$ 1,722,016	\$ 1,310,978	\$ 817,186	\$ 5,064,235
Liabilities and Fund Balances					
<i>Liabilities</i>					
202 Accounts Payable	\$ 122,840	\$ 71,071	\$ -	\$ 18,002	\$ 211,913
216 Accrued Wages Payable	90,272	-	-	-	90,272
217 Accrued Taxes Payable	1,355	-	-	58	1,413
224 Deferred Revenue	179,427	26,452	-	-	205,879
236 Advance from Other Funds (Note 6)	35,000	-	-	-	35,000
Total Liabilities	428,894	97,523	-	18,060	544,477
<i>Fund Balances</i>					
263.01 Nonspendable - Inventory	1,051	-	-	-	1,051
263.02 Nonspendable - Prepaid Expenses	26,344	-	-	-	26,344
263.05 Nonspendable - Notes Receivable	-	-	312,951	-	312,951
263.49 Nonspendable - SDPAA Reserve (Note 9)	135,844	-	-	-	135,844
263.51 Nonspendable - Perpetual Care Cemetary	-	-	-	50,000	50,000
263.99 Nonspendable - Library Trust	-	-	-	327,535	327,535
264.01 Restricted - Debt Service	-	625,765	-	9,696	635,461
264.03 Restricted - Perpetual Care Cemetary	-	-	-	102,570	102,570
264.04 Restricted - BID Tax	-	-	-	96,081	96,081
264.05 Restricted - Library Purposes	-	-	-	213,244	213,244
264.97 Restricted - Revolving Loan	-	-	998,027	-	998,027
264.02 Restricted - Capital Projects	-	998,728	-	-	998,728
265.97 Committed - Brick Fund	38,469	-	-	-	38,469
266.01 Assigned - Subsequent Year's Budget	297,092	-	-	-	297,092
267 Unassigned	286,361	-	-	-	286,361
Total Fund Balances	785,161	1,624,493	1,310,978	799,126	4,519,758
Total Liabilities and Fund Balances	\$ 1,214,055	\$ 1,722,016	\$ 1,310,978	\$ 817,186	\$ 5,064,235

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

**RECONCILIATION OF GOVERNMENTAL FUNDS BALANCE SHEET
TO GOVERNMENT-WIDE STATEMENT OF NET ASSETS
DECEMBER 31, 2011**

Total Fund Balances - Governmental Funds \$ 4,519,758

Amounts reported for governmental activities in the Statement
of Net Assets are different because:

Capital assets used in governmental activities are not current financial
resources and therefore are not reported in the funds. 33,550,581

Long-term liabilities, including bonds payable, tax increment financing
obligations, and compensated absences are not due and payable in the
current period and therefore not reported in the funds. (5,776,740)

Accrued interest on long-term debt is not due and payable in the current period
and therefore is not reported in the funds. (65,171)

Assets such as delinquent taxes receivable and special assessments are not
available to pay for current period expenditures and therefore are deferred in
the funds. 205,879

Discount on bonds and bond costs are capitalized on the Statement of
Activities as deferred charges and amortized over the life of the refunded
bonds. These costs were expensed in the governmental funds. 137,205

Total Net Assets - Governmental Funds **\$ 32,571,512**

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2011**

	General Fund	Capital Improvement Fund	Revolving Loan Fund	Other Governmental Funds	Total Governmental Funds
Revenue					
<i>Taxes:</i>					
311	General Property Taxes	\$ 2,570,812	\$ -	\$ -	\$ 2,668,611
313	General Sales and Use Taxes	1,339,150	1,339,150	-	2,938,708
315	Amusement Taxes	924	-	-	924
319	Penalties and Interest on Delinquent Taxes	15,104	-	-	15,104
320	Licenses and Permits	397,835	-	-	397,835
<i>Intergovernmental Revenue:</i>					
331	Federal Grants	11,713	650,605	-	662,318
334	State Grants	-	220,841	-	220,841
335.01	Bank Franchise Tax	2,329	-	-	2,329
335.03	Liquor Tax Reversion	29,536	-	-	29,536
335.04	Motor Vehicle Licenses	53,712	-	-	53,712
335.08	Local Government Highway and Bridge Fund	101,767	-	-	101,767
338.02	County Highway and Bridge Reserve Tax	5,855	-	-	5,855
338.04	Port of Entry	14,373	-	-	14,373
338.99	Other	9,478	-	-	9,478
<i>Charges for Goods and Services:</i>					
341	General Government	859,291	-	-	859,291
342	Public Safety	40,957	-	-	40,957
343	Highways and Streets	774	-	-	774
345	Health	634	-	-	634
346	Culture and Recreation	300,154	-	-	300,154
349	Other	43,637	-	-	43,637
<i>Fines and Forfeits:</i>					
351	Court Fines and Costs	3,910	-	-	3,910
<i>Miscellaneous Revenue:</i>					
361	Earnings on Deposits and Investments	3,813	12,160	16,644	49,049
362	Rentals	8,111	-	-	8,111
363	Special Assessments	1,867	12,133	-	14,000
367	Contributions and Donations	64,114	-	16,511	80,625
369	Other	860	-	14,853	15,713
Total Revenue		5,880,710	2,234,889	16,644	406,003
		8,538,246			

CITY OF STURGIS

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES (CONTINUED)
 GOVERNMENTAL FUNDS
 FOR THE YEAR ENDED DECEMBER 31, 2011

	<u>General Fund</u>	<u>Capital Improvement Fund</u>	<u>Revolving Loan Fund</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Expenditures					
<i>General Government:</i>					
411	199,989	-	-	-	199,989
414	976,707	-	-	-	976,707
419	1,157,027	15,072	-	-	1,172,099
<i>Public Safety:</i>					
421	1,731,541	-	-	-	1,731,541
422	149,473	20,832	-	-	170,305
<i>Public Works:</i>					
431	613,225	70,218	-	-	683,443
435	43,781	-	-	-	43,781
437	81,455	-	-	-	81,455
<i>Health and Welfare:</i>					
441	365	-	-	-	365
<i>Culture and Recreation:</i>					
451	747,572	14,986	-	-	762,558
452	571,434	48,503	-	-	619,937
455	356,496	-	-	33,396	389,892
456	24,246	-	-	-	24,246
460	-	-	-	273,546	273,546
470	-	616,050	-	118,596	734,646
485	49,667	810,314	-	-	859,981
Total Expenditures	6,702,978	1,595,975	-	425,538	8,724,491
Excess of Revenue Over (Under) Expenditures	(822,268)	638,914	16,644	(19,535)	(186,245)
Other Financing Sources (Uses)					
391.1	665,150	-	-	-	665,150
391.4	40,215	-	-	-	40,215
511	(12,000)	-	-	-	(12,000)
Total Other Financing Sources	693,365	-	-	-	693,365
Net Change in Fund Balance	(128,903)	638,914	16,644	(19,535)	507,120
Fund Balance, December 31, 2010 (Note 11)	914,064	985,579	1,294,334	818,661	4,012,638
Fund Balance, December 31, 2011	\$ 785,161	\$ 1,624,493	\$ 1,310,978	\$ 799,126	\$ 4,519,758

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

RECONCILIATION OF GOVERNMENTAL FUNDS STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES TO GOVERNMENT-WIDE STATEMENT OF ACTIVITIES FOR THE YEAR ENDED DECEMBER 31, 2011

Net change in fund balances - total government funds \$ 507,120

Amounts reported for governmental activities in the Statement of Activities are different because:

Governmental funds report capital outlays as expenditures. However, in the Statement of Activities the cost of those assets is allocated over their estimated lives and reported as depreciation expense. This is the amount by which depreciation exceeded capital outlays in the current period. (164,480)

Governmental funds report property taxes and special assessments as revenue when funds become available, but the Statement of Activities includes the property tax and special assessments as revenue when earned. 19,560

Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the Statement of Net Assets. 430,000

Debt issuance costs are deferred in the government wide statements and amortized over the term of the related debt. 20,498

Accrued interest on long-term debt is not due and payable in the current period and therefore is not reported in the funds. The amount represents the change in accrued interest during the current period. 62,116

Governmental funds do not reflect the change in accrued leave, but the Statement of Activities reflects the change in accrued leave through expenditures. (21,750)

Change in Net Assets of Governmental Activities \$ 853,064

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

**BALANCE SHEET
PROPRIETARY FUNDS
DECEMBER 31, 2011**

Assets	Liquor Fund	Water Fund	Wastewater Fund	Sanitation Fund	Ambulance Fund	Total Proprietary Funds
Current Assets						
101 Cash	\$ 9,776	\$ 768,824	\$ 320,083	\$ 107,778	\$ 390,524	\$ 1,596,985
107 Restricted Cash in Banks	4,098	-	-	-	-	4,098
115 Accounts Receivable, Net	27,995	85,055	81,051	70,963	15,924	280,988
128 Notes Receivable (Note 10)	-	-	50,000	-	-	50,000
131 Due from Liquor Fund (Note 6)	-	299,290	-	-	-	299,290
142 Inventory of Supplies for Resale	235,810	-	-	-	-	235,810
155 Prepaid Expenses	1,914	2,768	2,115	3,125	3,426	13,348
Total Current Assets	279,593	1,155,937	453,249	181,866	409,874	2,480,519
Noncurrent Asset						
131 Advance to Other Fund (Note 6)	-	-	-	35,000	-	35,000
Capital Assets (Note 4)						
160 Land	6,500	1,800	733,641	84,167	-	826,108
162 Buildings	826,042	181,183	445,257	310,994	359,809	2,123,285
163 Accumulated Depreciation - Buildings	(25,032)	(44,418)	(134,157)	(52,107)	(53,372)	(309,086)
164 Improvements Other Than Buildings	-	10,139,737	10,129,936	22,789	-	20,292,462
165 Accumulated Depreciation - Improvements Other Than Buildings	-	(3,746,292)	(2,750,782)	(14,627)	-	(6,511,701)
166 Machinery and Equipment	46,433	604,089	658,107	2,108,087	486,262	3,902,978
167 Accumulated Depreciation - Machinery and Equipment	(20,987)	(491,927)	(486,605)	(1,467,251)	(240,023)	(2,706,793)
168 Construction Work in Progress	-	602,476	-	-	-	602,476
Total Noncurrent Assets	832,956	7,246,648	8,595,397	1,027,052	552,676	18,254,729
Total Assets	\$ 1,112,549	\$ 8,402,585	\$ 9,048,646	\$ 1,208,918	\$ 962,550	\$ 20,735,248

Liabilities and Net Assets	Liquor Fund	Water Fund	Wastewater Fund	Sanitation Fund	Ambulance Fund	Total Proprietary Funds
Current Liabilities						
202 Accounts Payable	\$ 21,088	\$ 56,643	\$ 32,636	\$ 53,344	\$ 5,736	\$ 169,447
208 Due to Water Fund (Note 6)	299,290	-	-	-	-	299,290
215 Accrued Interest Payable	6,023	-	4,467	-	-	10,490
216 Accrued Wages	3,527	9,292	7,340	8,336	10,421	38,916
217 Accrued Taxes Payable	12,394	46	-	3,223	-	15,663
220 Customer Deposits	450	131,160	-	-	-	131,610
226 Bonds Payable - Current (Note 5)	8,870	82,684	273,961	-	-	365,515
233 Accrued Leave Payable (Note 5)	1,595	29,574	19,494	16,851	-	67,514
Total Current Liabilities	353,237	309,399	337,898	81,754	16,157	1,098,445
Long-Term Liabilities (Note 5)						
231 Bonds Payable	780,931	946,525	1,722,381	-	-	3,449,837
Total Liabilities	1,134,168	1,255,924	2,060,279	81,754	16,157	4,548,282
Net Assets						
253.1 Invested in Capital Assets, Net of Related Debt	43,155	6,217,439	6,599,055	992,052	552,676	14,404,377
253.21 Net Assets Restricted for Revenue Bond Debt Service	4,098	-	-	-	-	4,098
253.9 Unrestricted Net Assets	(68,872)	929,222	389,312	135,112	393,717	1,778,491
Total Net Assets	(21,619)	7,146,661	6,988,367	1,127,164	946,393	16,186,966
Total Liabilities and Net Assets	\$ 1,112,549	\$ 8,402,585	\$ 9,048,646	\$ 1,208,918	\$ 962,550	\$ 20,735,248

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
 PROPRIETARY FUNDS
 FOR THE YEAR ENDED DECEMBER 31, 2011**

	<u>Liquor Fund</u>	<u>Water Fund</u>	<u>Wastewater Fund</u>	<u>Sanitation Fund</u>	<u>Ambulance Fund</u>	<u>Total Proprietary Funds</u>
Total Operating Revenue						
380 Charges for Goods and Services	\$ 2,067,314	\$ 1,158,857	\$ 949,175	\$ 1,017,862	\$ 613,276	\$ 5,806,484
Operating Expenses						
410 Personal Services	155,648	449,924	309,967	360,372	413,369	1,689,280
420 Other Current Expense	182,611	337,958	135,474	489,604	116,468	1,262,115
426.2 Materials (Cost of Goods Sold)	1,632,241	-	-	-	-	1,632,241
457 Depreciation	30,128	235,456	247,542	146,628	55,822	715,576
Total Operating Expenses	2,000,628	1,023,338	692,983	996,604	585,659	5,299,212
Operating Income	66,686	135,519	256,192	21,258	27,617	507,272
Nonoperating Income (Expense)						
330 State Grants	-	-	-	44,276	-	44,276
361 Earnings on Deposits and Investments	11,479	5,134	2,136	899	1,787	21,435
369 Other	-	29,963	-	1,161	1,677	32,801
442 Interest Expense	(25,805)	(14,814)	(55,606)	-	-	(96,225)
Total Nonoperating Income (Expense)	(14,326)	20,283	(53,470)	46,336	3,464	2,287
Income Before Transfers and Loss on Sale of Property	52,360	155,802	202,722	67,594	31,081	509,559
391.1 Transfers In (Note 7)	-	-	-	12,000	-	12,000
391.03 Loss Sale of Property	(4,773)	-	-	-	-	(4,773)
511 Transfers Out (Note 7)	(190,810)	-	(250,697)	(223,643)	-	(665,150)
Transfers and Loss on Sale of Property	(195,583)	-	(250,697)	(211,643)	-	(657,923)
Net Income (Loss)	(143,223)	155,802	(47,975)	(144,049)	31,081	(148,364)
Net Assets, December 31, 2010 (Note 11)	121,604	6,990,859	7,036,342	1,271,213	915,312	16,335,330
Net Assets, December 31, 2011	\$ (21,619)	\$ 7,146,661	\$ 6,988,367	\$ 1,127,164	\$ 946,393	\$16,186,966

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

**STATEMENT OF CASH FLOWS
 PROPRIETARY FUNDS
 FOR THE YEAR ENDED DECEMBER 31, 2011**

	Liquor Fund	Water Fund	Wastewater Fund
Cash Flows from Operating Activities			
Receipts from Customers	\$ 2,064,831	\$ 1,159,376	\$ 948,974
Payments to Suppliers	(1,967,802)	(334,928)	(136,774)
Payments to Employees	(155,305)	(446,544)	(307,110)
Net Cash Flows Provided by (Used in) Operating Activities	(58,276)	377,904	505,090
Cash Flows from Noncapital Financing Activities			
Transfers In	-	-	-
Transfers Out	(190,810)	-	(250,697)
Internal Activity - Receipts from (Payments to) Other Funds	33,042	(33,042)	-
Cash Receipts from Notes Receivable	-	-	12,500
Net Cash Flows Used in Noncapital Financing Activities	(157,768)	(33,042)	(238,197)
Cash Flows from Capital and Related Financing Activities			
Purchases of Capital Assets	(192,819)	(693,182)	(27,438)
Proceeds from Sale of Asset	2,630	-	-
State Grants	-	-	-
Proceeds from Capital Debt	449,609	307,377	-
Principal Paid on Debt	(21,199)	(68,844)	(269,175)
Interest Paid	(19,782)	(14,814)	(55,606)
Other Receipts	-	29,963	-
Net Cash Flows Provided by (Used in) Capital and Related Financing Activities	218,439	(439,500)	(352,219)
Cash Flows Provided by Investing Activities			
Cash Received From Interest	11,479	5,134	2,136
Increase (Decrease) in Cash and Cash Equivalents	13,874	(89,504)	(83,190)
Cash and Cash Equivalents, January 1, 2011	-	858,328	403,273
Cash and Cash Equivalents, December 31, 2011	\$ 13,874	\$ 768,824	\$ 320,083
Reconciliation of Operating Income to Net Cash Provided by Operating Activities			
Operating Income	\$ 66,686	\$ 135,519	\$ 256,192
<i>Adjustments to Reconcile Operating Income to Net Cash Flows Provided by (Used in) Operating Activities:</i>			
Depreciation Expense	30,128	235,456	247,542
Change in Assets and Liabilities:			
Accounts Receivable	(2,783)	(5,006)	(201)
Inventory of Supplies	(69,105)	-	-
Prepaid Expenses and Deposits	(555)	945	(2,115)
Accounts Payable	(84,430)	2,074	815
Accrued Wages	5	(1,431)	536
Accrued Taxes Payable	1,140	11	-
Customer Deposits	300	5,525	-
Accrued Leave Payable	338	4,811	2,321
Net Cash Flows Provided by (Used in) Operating Activities	\$ (58,276)	\$ 377,904	\$ 505,090
Noncash Capital and Related Financing Activities			
Loss on Disposal of Equipment	4,773	-	-
Purchase of Fixed Assets Included in Accounts Payable	-	33,708	25,902

The accompanying notes are an integral part of the financial statements.

Sanitation Fund	Ambulance Fund	Total Proprietary Funds
\$ 999,603	\$ 632,866	\$ 5,805,650
(479,384)	(115,997)	(3,034,885)
(360,477)	(408,060)	(1,677,496)
<u>159,742</u>	<u>108,809</u>	<u>1,093,269</u>
12,000	-	12,000
(223,643)	-	(665,150)
25,000	-	25,000
-	-	12,500
<u>(186,643)</u>	<u>-</u>	<u>(615,650)</u>
(122,701)	(53,529)	(1,089,669)
-	-	2,630
44,276	-	44,276
-	-	756,986
-	-	(359,218)
-	-	(90,202)
1,161	1,677	32,801
<u>(77,264)</u>	<u>(51,852)</u>	<u>(702,396)</u>
899	1,787	21,435
(103,266)	58,744	(203,342)
211,044	331,780	1,804,425
\$ 107,778	\$ 390,524	\$ 1,601,083
\$ 21,258	\$ 27,617	\$ 507,272
146,628	55,822	715,576
(18,259)	-	(6,659)
-	19,590	(69,105)
-	-	(69,105)
392	(808)	(2,141)
10,263	1,279	(69,999)
553	5,309	4,972
(435)	-	716
-	-	5,825
(658)	-	6,812
<u>\$ 159,742</u>	<u>\$ 108,809</u>	<u>\$ 1,093,269</u>
-	-	4,773
24,101	-	83,711

CITY OF STURGIS

**STATEMENT OF FIDUCIARY NET ASSETS
DECEMBER 31, 2011**

	Agency Fund
Assets	
Interest Bearing Accounts	\$ 42,542
Total Assets	\$ 42,542
Liabilities	
Amounts Held for Others	\$ 42,542
Total Liabilities	\$ 42,542

The accompanying notes are an integral part of the financial statements.

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2011

(1) Summary of Significant Accounting Policies

a. Reporting Entity

The reporting entity of the City of Sturgis (the City), consists of the primary government (which includes all of the funds, organizations, institutions, agencies, departments, and offices that make up the legal entity, plus those funds for which the primary government has a fiduciary responsibility; those organizations for which the primary government is financially accountable; and other organizations for which the nature and significance of their relationship with the primary government are such that their exclusion would cause the financial reporting entity's financial statements to be misleading or incomplete).

b. Basis of Presentation

Government-wide Financial Statements:

The Statement of Net Assets and Statement of Activities display information about the reporting entity as a whole. They include all funds of the reporting entity except for fiduciary funds. The statements distinguish between governmental and business-type activities. Governmental activities generally are financed through taxes, intergovernmental revenues, and other non-exchange revenues. Business-type activities are financed in whole or in part by fees charged to external parties for goods or services.

The Statement of Activities presents a comparison between direct expenses and program revenues for each segment of the business-type activities of the City and for each function of the City's governmental activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function. Program revenues include (a) charges paid by recipients of goods and services offered by the programs and (b) grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues.

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, liabilities, fund equity, revenues, and expenditures/expenses. Funds are organized into three major categories: governmental, proprietary, and fiduciary. An emphasis is placed on major funds within the governmental and proprietary categories. A fund is considered major if it is the primary operating fund of the City or it meets the following criteria:

1. Total assets, liabilities, revenues, or expenditures/expenses of the individual governmental or enterprise fund are at least 10 percent of the corresponding total for all funds of that category or type, and
2. Total assets, liabilities, revenues, or expenditures/expenses of the individual governmental or enterprise fund are at least 5 percent of the corresponding total for all governmental and enterprise funds combined, or
3. Management has elected to classify one or more governmental or enterprise funds as major for consistency in reporting from year to year, or because of public interest in the fund's operations.

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2011

(1) Summary of Significant Accounting Policies (Continued)

b. Basis of Presentation (Continued)

The major funds of the City financial reporting entity are described below:

Governmental Funds:

General Fund - the general fund is the general operating fund of the City. It is used to account for all financial resources except those required to be accounted for in another fund. The general fund is always considered to be a major fund.

Special Revenue Funds - special revenue funds are used to account for the proceeds of specific revenue sources (other than trusts for individuals, private organizations, or other governments or for major capital projects) that are legally restricted to expenditures for specified purposes.

Capital Improvement Fund - 50 percent of the tax levied under Title 20 Tax, Chapter 20.01 Municipal Sales and Service Tax, and Use Tax shall be used only for capital improvements, land acquisition, debt reduction, and the purchase of machinery and equipment. This is a major fund.

Revolving Loan Fund - to account for federal grants and other municipal monies used for financing improvements. The fund may be used both to pay the portion of the cost of an improvement and to advance the portion of such costs to business which are to be repaid over a period of years. This is a major fund.

Debt Service Funds - debt service funds are used to account for the accumulation of resources for, and the payment of, general long-term debt principal, interest, and related costs. There are no major debt service funds.

Capital Projects Funds - capital projects funds are used to account for financial resources to be used for the acquisition or construction of major capital facilities (other than those financed by proprietary funds or trust funds for individuals, private organizations, or other governments). There are no major capital projects funds.

Permanent Funds - permanent funds are used to report resources that are legally restricted to the extent that only earnings, and not principal, may be used for purposes that support the City's programs - that is for the benefit of the City and its citizenry. There are no major permanent funds.

Proprietary Funds:

Enterprise Funds - enterprise funds are used to account for operations (a) that are financed and operated in a manner similar to private business enterprises, where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

The enterprise funds and business-type activities do not apply any FASB Statements and Interpretations issued after November 30, 1989.

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2011

(1) Summary of Significant Accounting Policies (Continued)

b. Basis of Presentation (Concluded)

Proprietary Funds (Continued):

Proprietary Funds include:

Liquor Fund - financed primarily by the sale of liquor; this fund accounts for construction and operation of the City liquor store. This is a major fund.

Water Fund - financed primarily by user charges; this fund accounts for the construction and operation of the City waterworks system and related facilities (SDCL 9-47-1). This is a major fund.

Wastewater Fund - financed primarily by user charges; this fund accounts for the construction and operation of the City sanitary sewer system and related facilities (SDCL 9-48-2). This is a major fund.

Sanitation Fund - financed primarily by user charges; this fund accounts for the construction and operation of the City rubble site and collection and disposal of solid waste and includes activity from the Special Sanitation Fund. This is a major fund.

Ambulance Fund - financed primarily by user charges; this new enterprise fund in 2011 accounts for construction and operation of the City ambulance service. This is a major fund. (See note 11).

Fiduciary Funds:

Fiduciary funds consist of the following sub-category and are never considered to be major funds:

Agency Funds - agency funds are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations. Agency funds are used to account for the accumulation and distribution of property tax revenues and various pass through funds. This fund includes special assessment activities.

c. Measurement Focus and Basis of Accounting

Measurement focus is a term used to describe how transactions are recorded within the various financial statements. Basis of accounting refers to when revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements, regardless of the measurement focus.

Measurement Focus:

Government-wide Financial Statements:

In the government-wide Statement of Net Assets and Statement of Activities, both governmental and business-type activities are presented using the economic resources measurement focus, applied on the accrual basis of accounting.

Non-exchange transactions, in which the City gives (or receives) value without directly receiving (or giving) equal value in exchange, include property taxes, grants, entitlements and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenues from grants, entitlements and donations are recognized in the year in which all eligibility requirements have been satisfied.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2011**

(1) Summary of Significant Accounting Policies (Continued)

c. Measurement Focus and Basis of Accounting (Continued)

Measurement Focus (Continued):

Fund Financial Statements:

In the fund financial statements, the current financial resources measurement focus and the modified accrual basis of accounting are applied to governmental funds, while the economic resources measurement focus and the accrual basis of accounting are applied to the proprietary and fiduciary funds.

Basis of Accounting:

Government-wide Financial Statements:

In the Government-wide Statement of Net Assets and Statement of Activities, governmental and business-type activities are presented using the accrual basis of accounting. Under the accrual basis of accounting, revenues and related assets are recorded when earned (usually when the right to receive cash vests); and, expenses and related liabilities are recorded when an obligation is incurred (usually when the obligation to pay cash in the future vests).

Fund Financial Statements:

All governmental fund types are accounted for using the modified accrual basis of accounting. Their revenues, including property taxes, are recognized when they become measurable and available. Available means resources are collected or to be collected soon enough after the end of the fiscal year that they can be used to pay the bills of the current period. The accrual period for the City does not exceed one bill-paying cycle, and for the City, the length of that cycle is 60 days. The revenues which are accrued at December 31, 2011 are sales tax revenues and intergovernmental revenue.

Under the modified accrual basis of accounting, receivables may be measurable, but not available. Available means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Reported deferred revenues are those where asset recognition criteria have been met, but for which revenue recognition criteria have not been met.

Expenditures are generally recognized when the related fund liability is incurred. Exceptions to this general rule include principal and interest on general long-term debt, which are recognized when due.

All proprietary funds and fiduciary funds are accounted for using the accrual basis of accounting. Their revenues are recognized when they are earned, and their expenses are recognized when they are incurred.

d. Interfund Eliminations and Reclassifications

Government-wide Financial Statements:

In the process of aggregating data for the government-wide financial statements, some amounts reported as interfund activity and balances in the fund financial statements have been eliminated or reclassified, as follows:

In order to minimize the grossing-up effect on assets and liabilities within the governmental and business-type activities columns of the primary government, amounts reported as interfund receivables and payables have been eliminated in the governmental and business-type activities columns, except for the net, residual amounts due between governmental and business-type activities, which are presented as Internal Balances.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2011**

(1) Summary of Significant Accounting Policies (Continued)

d. Interfund Eliminations and Reclassifications (Continued)

Fund Financial Statements:

Noncurrent portions of long-term interfund receivables (reported in Advance to asset accounts) are equally offset by a nonspendable fund balance account which indicates that they do not constitute available spendable resources since they are not a component of net current assets. Current portions of interfund receivables (reported in Due from asset accounts) are considered available spendable resources.

e. Capital Assets

Capital assets include land, buildings, machinery and equipment, and all other tangible or intangible assets that are used in operations and that have initial useful lives extending beyond a single reporting period. Infrastructure assets are long-lived capital assets that normally are stationary in nature and can be preserved for a significantly greater number of years than most capital assets.

The accounting treatment over capital assets 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.

Government-wide Financial Statements:

Capital assets are recorded at historical cost, or estimated cost, where actual cost could not be determined. Donated capital assets are valued at their estimated fair value on the date donated. Reported cost values include ancillary charges necessary to place the asset into its intended location and condition for use. Subsequent to initial capitalization, improvements or betterments that are significant and which extend the useful life of a capital asset are also capitalized.

For governmental activities capital assets, construction-period interest is not capitalized, in accordance with USGAAP; while for capital assets used in business-type activities; construction-period interest is capitalized in accordance with USGAAP.

Infrastructure assets used in general government operations, consisting of certain improvements other than buildings, including roads, bridges, sidewalks, drainage systems, and lighting systems, acquired prior to January 1, 2004, were not required to be capitalized by the City. Infrastructure assets acquired since January 1, 2004, are recorded at cost, and classified as "Improvements Other than Buildings."

Depreciation of all exhaustible capital assets is recorded as an allocated expense in the Government-wide Statement of Activities. Accumulated depreciation is reported on the Government-wide Statement of Net Assets and on each proprietary fund's Statement of Net Assets/Balance Sheet.

Capitalization thresholds (the dollar values above which asset acquisitions are added to the capital asset accounts), depreciation methods, and estimated useful lives of capital assets reported in the government-wide statements and proprietary funds are as follows:

	<u>Capitalization Threshold</u>	<u>Depreciation Method</u>	<u>Estimated Useful Life</u>
Land	\$ -0-	----N/A-----	----N/A-----
Improvements Other Than Buildings	\$ 15,000	Straight-line	10-50 years
Buildings	\$ 15,000	Straight-line	10-50 years
Machinery and Equipment	\$ 10,000	Straight-line	5-40 years

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2011

(1) Summary of Significant Accounting Policies (Continued)

e. Capital Assets (Continued)

Land is an inexhaustible capital asset and is not depreciated.

Fund Financial Statements:

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

f. Long-Term Liabilities

The accounting treatment of long-term liabilities 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 liabilities to be repaid from governmental and business-type resources are reported as liabilities in the government-wide statements. The long-term liabilities primarily consist of general obligation bonds, revenue bonds, tax increment financing, and compensated absences.

In the fund financial statements, debt proceeds are reported as revenues (other financing sources), while payments of principal and interest are reported as expenditures when they become due. The accounting for proprietary fund long-term debt is on the accrual basis, the same in the fund statements as in the government-wide statements.

g. Program Revenues

Program revenues derive directly from the program itself or from parties other than the City's taxpayers or citizenry, as a whole. Program revenues are classified into three categories, as follows:

1. Charges for services – These arise from charges to customers, applicants, or others who purchase, use, or directly benefit from the goods, services, or privileges provided, or are otherwise directly affected by the services.
2. Program-specific operating grants and contributions – These arise from mandatory and voluntary non-exchange transactions with other governments, organizations, or individuals that are restricted for use in a particular program.
3. Program-specific capital grants and contributions – These arise from mandatory and voluntary non-exchange transactions with other governments, organizations, or individuals that are restricted for the acquisition of capital assets for use in a particular program.

h. Proprietary Funds Revenue and Expense Classifications

In the proprietary funds' Statement of Activities, revenues and expenses are classified in a manner consistent with how they are classified in the Statement of Cash Flows. That is, transactions for which related cash flows are reported as capital and related financing activities, noncapital financing activities, or investing activities are not reported as components of operating revenues or expenses.

i. Cash and Cash Equivalents

The City pools the cash resources of its funds for cash management purposes. The proprietary funds essentially have access to the entire amount of their cash resources on demand. Accordingly, each proprietary fund's equity in the cash management pool is considered to be cash and cash equivalents for the purpose of the Statement of Cash Flows.

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2011

(1) Summary of Significant Accounting Policies (Continued)

j. Equity Classifications

Government-wide Financial Statements:

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

1. Invested in capital assets, net of related debt – Consists of capital assets, including restricted capital assets, net of accumulated depreciation (if applicable) 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.
2. Restricted net assets – Consists of net assets with constraints placed on their use either by (a) external groups such as creditors, grantors, contributors, or laws and regulations of other governments; or (b) law through constitutional provisions or enabling legislation.
3. Unrestricted net assets – All other net assets that do not meet the definition of restricted or invested in capital assets, net of related debt.

Fund Financial Statements:

In accordance with Government Accounting Standards Board (GASB) No. 54, Fund Balance Reporting and Governmental Fund Type Definitions, which was implemented in the current year, the City classifies governmental fund balance as follows:

Nonspendable – includes fund balance amounts that cannot be spent either because it is not in spendable form or because of legal or contractual constraints.

Restricted – includes fund balance amounts that are constrained for specific purposes which are externally imposed by providers, such as creditors or amounts constrained due to constitutional provisions or enabling legislation.

Committed – includes fund balance amounts that are constrained for specific purposes that are internally imposed by the government through formal action of the highest level of decision making authority and does not lapse at year-end. The City has one Committed Fund Balance for the year ended December 31, 2011. The Brick Fund was created through an ordinance passed by the City Council, the highest decision making authority. The City Council would have to pass an ordinance to remove the commitment.

Assigned – includes fund balance amounts that are intended to be used for specific purposes that are neither considered restricted or committed. Fund balance may be assigned by the City Council, Mayor, or Finance Officer.

Unassigned – includes positive fund balance within the General Fund which has not been classified within the above-mentioned categories and negative fund balances in other governmental funds.

With regard to the City's governmental funds, the City uses restricted amounts first when both restricted and unrestricted fund balances are available unless there are legal documents/contracts that prohibit doing this, such as a grant agreement requiring dollar-for-dollar spending. Additionally, the City would first use committed, then assigned, and lastly unassigned amounts of unrestricted fund balance when expenditures are made.

Proprietary fund equity is classified the same as in the government-wide financial statements. The City does not have a formal minimum fund balance policy. With regard to the City's proprietary funds, it is the City's policy to first use restricted net assets, prior to the use of unrestricted net assets, when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2011

(1) Summary of Significant Accounting Policies (Concluded)

k. Inventory

Inventory consists of inventory held for resale, which is recorded at the lower of cost or market, using the first-in, first-out method.

Inventory is recorded as an asset at the time of purchase, and charged to expense as it is consumed.

l. Compensated Absences

Full time employees earn up to two weeks of paid vacation, three weeks after the employee has been employed for five years, and four weeks after the employee has been employed for ten years. Maximum annual accrued carryover is forty hours. Upon termination, an employee is entitled to receive compensation for their accrued annual leave balance at their normal wage.

Sick leave is earned by full-time employees at the rate of eight hours per month to a maximum of 1,000 hours. Upon termination, employees are not entitled to receive compensation for their accrued sick leave balance unless they have been employed for ten years, at which time they receive half of their accumulated sick leave at three-quarters of their normal wage.

m. Deferred Revenue

Under the modified accrual basis of accounting, receivables may be measurable but not available. Available means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Reported deferred revenues are those where asset recognition criteria have been met, but for which revenue recognition criteria have not been met, which include property taxes and special assessments.

(2) Deposits and Investments

The City follows the practice of aggregating the cash assets of various funds to maximize cash management efficiency and returns. Various restrictions on deposits and investments are imposed by statutes. These restrictions are summarized below:

Deposits - The City's cash deposits are made in qualified public depositories as defined by SDCL 4-6A-1, 9-22-6, 9-22-6.1 and 9-22-6.2, and may be in the form of demand or time deposits. Qualified depositories are required by SDCL 4-6A-3 to maintain at all times, segregated from their other assets, eligible collateral having a value equal to at least 100 percent of the public deposit accounts which exceed deposit insurance such as the FDIC and NCUA. In lieu of pledging eligible securities, a qualified public depository may furnish irrevocable standby letters of credit issued by Federal Home Loan Banks accompanied by written evidence of that bank's public debt rating, which may not be less than "AA" or a qualified public depository may furnish a corporate surety bond of a corporation duly authorized to do business in South Dakota.

Investments - In general, SDCL 4-5-6 permits City funds to be invested only in (a) securities of the United States and securities guaranteed by the United States Government either directly or indirectly; or (b) repurchase agreements fully collateralized by securities described in (a) above; or in shares of an open-end, no-load fund administered by an investment company whose investments are in securities described in (a) above and repurchase agreements described in (b) above. Also, SDCL 4-5-9 requires investments to be in the physical custody of the political subdivision or may be deposited in a safekeeping account with any bank or trust company designated by the political subdivision as its fiscal agent.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2011**

(2) Deposits and Investments (Continued)

As of December 31, 2011, the City’s cash and investments consisted of checking and savings accounts, and money market accounts. All of these accounts are insured or collateralized in the City’s name. The money market accounts are unrated.

State law allows income from deposits and investments to be credited to either the general fund or the fund making the investment. The City’s policy is to credit all income from deposits and investments to the fund making the investment, with the exception of the Cemetery Perpetual Care Fund, which must be credited to the General Fund, and used only for maintenance of the municipal cemetery, as required by SDCL 9-32-18.

Interest Rate Risk:

The City does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk:

State law limits eligible investments for the City as discussed above. The City has no investment policy that would further limit its investment choices.

Custodial Credit Risk:

Custodial credit risk is the risk that, in the event of a depository failure, the City’s deposits may not be returned to it. The City does not have a deposit policy for custodial credit risk. As of December 31, 2011, none of the City’s deposits were exposed to custodial credit risk.

Concentration Risk:

The City places no limit on the amount that may be invested in any one issuer.

(3) Property Taxes

Property taxes are levied on or before October 1 and payable in two installments before April 30 and October 31 of the following year. They attach as an enforceable lien on property as of January 1 of each year. The county bills and collects the taxes and remits them to the City.

The City is permitted by several state statutes to levy the following amounts of taxes per \$1,000 of taxable valuation on taxable real property in the City:

General Fund	\$27
Bond Redemption Funds	Amounts Required by Bond Agreements
Judgment Fund (Upon Judgment Being Made)	\$10

State statute allows the tax rates to be raised by special election of the voters.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2011**

(4) Changes in Capital Assets

A summary of changes in capital assets for year ending December 31 is as follows:

	(Note 11) Balance 12/31/2010	Additions	Transfers/ Deletions	Balance 12/31/2011
<i>Governmental Activities:</i>				
Capital Assets, not being Depreciated:				
Land	\$ 2,184,497	\$ -	\$ -	\$ 2,184,497
Construction Work in Progress	2,589,424	247,859	2,730,708	106,575
Total Capital Assets, not being Depreciated	4,773,921	247,859	2,730,708	2,291,072
Capital Assets, being Depreciated:				
Buildings	12,444,713	-	-	12,444,713
Improvements Other Than Buildings	23,138,289	3,234,588	-	26,372,877
Machinery and Equipment	3,491,772	108,242	-	3,600,014
Total Capital Assets, being Depreciated	39,074,774	3,342,830	-	42,417,604
Less Accumulated Depreciation for:				
Buildings	3,029,020	272,930	-	3,301,950
Improvements Other Than Buildings	5,192,280	573,098	-	5,765,378
Machinery and Equipment	1,912,334	178,433	-	2,090,767
Total Accumulated Depreciation	10,133,634	1,024,461	-	11,158,095
Total Governmental Activities Capital Assets, being Depreciated, Net				
	28,941,140	2,318,369	-	31,259,509
Total Governmental Capital Assets, Net	\$ 33,715,061	\$ 2,566,228	\$ 2,730,708	\$ 33,550,581

Depreciation expense was charged to functions as follows:

Public Works	\$ 476,795
Culture and Recreation	231,508
General Government	209,095
Public Safety	107,063
Total Depreciation Expense - Governmental	\$ 1,024,461

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2011**

(4) Changes in Capital Assets (Continued)

	(Note 11) Balance 12/31/2010	Additions	Deletions	Balance 12/31/2011
<i>Business-Type Activities:</i>				
Capital Assets, not being Depreciated:				
Land	\$ 741,941	\$ 84,167	\$ -	\$ 826,108
Construction Work in Progress	633,223	795,295	826,042	602,476
Total Capital Assets, not being Depreciated	1,375,164	879,462	826,042	1,428,584
Capital Assets, being Depreciated:				
Buildings	1,357,072	826,042	59,829	2,123,285
Improvements Other Than Buildings	20,220,893	71,569	-	20,292,462
Machinery and Equipment	3,701,108	222,349	20,479	3,902,978
Total Capital Assets, being Depreciated	25,279,073	1,119,960	80,308	26,318,725
Less Accumulated Depreciation for:				
Buildings	300,423	61,088	52,425	309,086
Improvements Other Than Buildings	6,100,754	410,947	-	6,511,701
Machinery and Equipment	2,483,732	243,541	20,480	2,706,793
Total Accumulated Depreciation	8,884,909	715,576	72,905	9,527,580
Total Business-Type Activities Capital Assets, being Depreciated, Net				
	16,394,164	404,384	7,403	16,791,145
Total Business-Type Capital Assets, Net				
	\$ 17,769,328	\$ 1,283,846	\$ 833,445	\$ 18,219,729

Depreciation expense was charged to functions as follows:

Ambulance	\$ 55,822
Wastewater	247,542
Water	235,456
Sanitary	146,628
Liquor	30,128
Total Depreciation Expense - Business-Type	\$ 715,576

Construction Work in Progress

As of December 31, 2011, there are approximately \$2,801,000 of commitments associated with construction projects in progress, the majority of which will be funded through future revenue bonds and grants. Completion of such projects range from 2012 through 2013.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2011**

(5) Long-Term Debt

The following is a summary of the long-term debt transactions for the year ending December 31:

	Balance 12/31/2010	Additions	Deletions	Balance 12/31/2011	Due Within One Year
Primary Government:					
Governmental Activities:					
Revenue Bonds	\$ 5,605,000	\$ -	\$ 430,000	\$ 5,175,000	\$ 445,000
Tax Increment Financing Obligations	406,001	-	-	406,001	41,295
Compensated Absences	173,989	221,012	199,262	195,739	195,739
Total Governmental Activities	6,184,990	221,012	629,262	5,776,740	682,034
Business-Type Activities:					
2010 GO Crossover Refunding Bonds	2,210,000	-	290,000	1,920,000	295,000
2010 Sales Tax Revenue Bond	361,391	449,609	21,199	789,801	8,870
2009 Drinking Water Revenue Bond	547,576	-	36,944	510,632	50,234
2009 Clean Water Revenue Bond	298,617	-	11,075	287,542	11,411
2011 Drinking Water Bond	-	307,377	-	307,377	-
Compensated Absences	60,702	78,425	71,613	67,514	67,514
Total Business-Type Activities	3,478,286	835,411	430,831	3,882,866	433,029
Total Primary Government	\$ 9,663,276	\$ 1,056,423	\$ 1,060,093	\$ 9,659,606	\$1,115,063

The City has a bond reserve of \$625,765 at December 31, 2011, in accordance with debt covenants. However, the City was in violation of the Rural Development debt reserve covenant for \$4,098, but subsequently obtained verbal waiver of such and will meet the requirement during 2012.

The City has pledged future revenues of the Water and Wastewater Funds for the retirement of debt issues associated with those funds through the maturity dates listed below. All debt secured by pledged revenues funded capital projects and improvements. The current principal balance plus interest at the stated applicable rate over the life of the debt represents the amount of future revenue pledged. Below is a comparison by fund of principal and interest payments and total pledged revenue for the current year.

	Water <u>Fund</u>	Wastewater <u>Fund</u>
Current Year Principal and Interest	\$ 83,658	\$ 324,781
Pledged Revenue	1,158,857	949,175

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2011**

(5) Long-Term Debt (Continued)

Debt payable at December 31, 2011, is comprised of the following:

General Obligation

General Obligation Crossover Refunding Bonds, Series 2010A for \$2,210,000, mature in June 2021, interest at 2.00 to 3.65 percent, due in semi-annual installments of \$30,000 to \$155,000. Financed through Water and Wastewater Funds. \$ 1,920,000

Revenue Bonds

Sales Tax Refunding Bonds, 2008 Series for \$6,470,000, mature in March 2020, interest at a fixed 2.50 to 3.80 percent, due in variable annual installments. Financed through the Capital Improvement Fund. 5,175,000

Sales Tax Revenue Bonds, Series 2010 (Build America Bonds - Direct Pay), for \$811,000, mature in July 2050, interest at a fixed 4.00 percent, due in annual installments of \$40,980. Sales tax revenues pledged and financed through the Liquor Fund. The City will receive a credit from the Federal government for 35 percent of the interest paid on the bonds. 789,801

Drinking Water Revenue Borrower Bond, 2009 Series for \$547,576, mature in January 2021, interest at a fixed 2.25 percent, due in quarterly installments of \$15,325. Water revenues pledged and financed through the Water Fund. 510,632

Clean Water Revenue Borrower Bond, 2009 Series for \$298,617, mature in October 2030, interest at a fixed 3.00 percent, due in quarterly installments of \$49,077. Wastewater revenues pledged and financed through the Wastewater Fund. 287,542

Drinking Water Revenue Borrower Bond, 2011 Series, with a maximum borrowing of \$3,460,000. As of December 31, 2011, advances totaled \$307,377. Payments begin in 2012, with interest-only payments at 2.00 percent totaling \$69,200 through October 2014. The interim financing through SRF will then be repaid by USDA Rural Development, and the City will make scheduled debt payments to them at that time. Water revenues pledged and financed through the Water Fund. 307,377

Tax Increment Financing Obligations

TIF #9 for \$406,001, including interest not to exceed 10 percent per annum, due in varying installments within 30 days of property tax collections from the County. Financed through TIF Debt Service Funds. 406,001

Total Bonds and TIF Obligations 9,396,353

Compensated Absences:

General Fund	195,739
Liquor Fund	1,595
Water Fund	29,574
Wastewater Fund	19,494
Sanitation Fund	16,851

Total Compensated Absences 263,253

Total Long-Term Debt \$ 9,659,606

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2011**

(5) Long-Term Debt (Concluded)

The annual requirements to amortize long-term debt outstanding as of December 31, 2011, except for compensated absences are as follows:

	General Obligation		Revenue Bonds		TIF Obligations		Total	
	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>
2012	\$ 46,302	\$ 295,000	\$ 293,658	\$ 515,516	\$ 55,875	\$ 41,295	\$ 395,835	\$ 851,811
2013	40,402	300,000	278,083	834,748	29,594	67,576	348,079	1,202,324
2014	34,352	310,000	261,612	544,270	23,728	73,442	319,692	927,712
2015	28,184	240,000	174,938	561,221	17,353	79,817	220,475	881,038
2016	22,992	175,000	156,430	578,227	10,424	86,746	189,846	839,973
2017-2021	46,290	600,000	437,849	3,196,994	2,428	57,125	486,567	3,854,119
2022-2026	-	-	150,914	153,534	-	-	150,914	153,534
2027-2031	-	-	122,097	162,441	-	-	122,097	162,441
2032-2036	-	-	97,869	107,031	-	-	97,869	107,031
2037-2041	-	-	74,215	130,685	-	-	74,215	130,685
2042-2046	-	-	45,334	159,566	-	-	45,334	159,566
2047-2050	-	-	11,229	126,119	-	-	11,229	126,119
Total	\$ 218,522	\$ 1,920,000	\$ 2,104,228	\$ 7,070,352	\$ 139,402	\$ 406,001	\$ 2,462,152	\$ 9,396,353

As of December 31, 2011, the City was acting as a fiscal agent for the following special assessment issues:

2002 \$107,844

The City is not liable directly or indirectly for the preceding special assessment.

(6) Individual Fund Interfund Receivable and Payable Balances

Interfund receivable and payable balances at December 31, 2011, are as follows:

Fund	Interfund Receivables	Interfund Payables
<i>Major Funds:</i>		
General Fund	\$ -	\$ 35,000
Sanitation Fund	35,000	-
Liquor Fund	-	299,290
Water Fund	299,290	-
Total Interfund Receivable and Payable Balances	\$ 334,290	\$ 334,290

The Sanitation Fund advanced monies to the General Fund to purchase Woodland Trailer Park land. The land was purchased in order to develop more park area for the community. The balance will be paid back over time.

The Water Fund loaned monies to the Liquor Fund for operations. The balance will be paid back within the next year.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2011**

(7) Interfund Transfers

	Transfers In	Transfers Out
<i>Major Funds:</i>		
General Fund	\$ 665,150	\$ 12,000
Liquor Fund	-	190,810
Wastewater Fund	-	250,697
Sanitation Fund	12,000	223,643
Total Transfers	\$ 677,150	\$ 677,150

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 requires 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.

(8) Retirement Plan -- South Dakota Retirement System

All employees, except for part-time employees, participate in the South Dakota Retirement System (SDRS), a cost-sharing, multiple employer public employee retirement system established to provide retirement benefits for employees of the State of South Dakota and its political subdivisions. The SDRS provides retirement, disability and survivor benefits. The right to receive retirement benefits vests after three years of credited service. Authority for establishing, administering and amending plan provisions are found in South Dakota Codified Law 3-12. The SDRS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the SDRS, P.O. Box 1098, Pierre, SD 57501-1098 or by calling (605) 773-3731.

General employees are required by state statute to contribute six percent of their salary to the plan, while public safety and judicial employees contribute eight and nine percent, respectively. State statute also requires the employer to contribute an amount equal to the employee's contribution. State statute also requires the employer to make an additional contribution in the amount of 6.2 percent for any compensation exceeding the maximum taxable amount for social security for general employees only. The City's share of contributions to the SDRS for the fiscal years ended December 31, 2011, 2010, and 2009, were **\$242,673**, \$232,082, and \$212,768, respectively, equal to the required contributions each year.

(9) 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. During the year ended December 31, 2011, the City managed its risks as follows:

Employee Health Insurance:

The City purchases health insurance for its employees from a commercial insurance carrier. Settled claims resulting from these risks have not exceeded the liability coverage during the past four years.

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2011

(9) Risk Management (Continued)

Liability Insurance:

The City joined the South Dakota Public Assurance Alliance (SDPAA), a public entity risk pool currently operating as a common risk management and insurance program for South Dakota local government entities. The objective of the SDPAA is to administer and provide risk management services and risk sharing facilities to the members and to defend and protect the members against liability, to advise members on loss control guidelines and procedures, and provide them with risk management services, loss control and risk reduction information and to obtain lower costs for that coverage. The City's responsibility is to promptly report to and cooperate with the SDPAA to resolve any incident which could result in a claim being made by or against the City. The City pays an annual premium to the pool to provide coverage for general liability, vehicle coverage, wrongful acts, and errors and omissions of public officials.

The agreement with the South Dakota Public Assurance Alliance provides that the above coverage will be provided to a \$2,000,000 limit. Member premiums are used by the pool for payment of claims and to pay for reinsurance for claims in excess of \$250,000 for property coverage and \$500,000 for liability coverage to the upper limit. The City carries a \$1,000 deductible for the wrongful acts coverage and auto coverage.

As of December 31, 2011, the City has a fully vested balance in the cumulative reserve fund of \$135,844. Access to this balance is restricted by SDPAA.

The City does not carry additional insurance to cover claims in excess of the upper limit. Settled claims resulting from the risks have not exceeded the liability coverage during the past four years.

Property and Building Insurance:

The City purchases property and building insurance from a commercial insurance carrier. Settled claims resulting from these risks have not exceeded the liability coverage during the past four years.

Worker's Compensation:

The City joined the South Dakota Municipal League Worker's Compensation Fund (the Fund), a public entity risk pool currently operating as a common risk management and insurance program for South Dakota local government entities. The objective of the Fund is to formulate, develop, and administer, on behalf of the member organizations, a program of worker's compensation coverage, to obtain lower costs for that coverage, and to develop a comprehensive loss control program. The City's responsibility is to initiate and maintain a safety program to give its employees safe and sanitary working conditions and to promptly report to and cooperate with the Fund to resolve any worker's compensation claims. The City pays an annual premium to provide worker's compensation coverage for its employees under a retrospectively rated policy, and the premiums are accrued based on the ultimate cost of the experience to date of the Fund members. Coverage limits are set by state statute. The pool pays the first \$650,000 of any claim per individual. The pool has reinsurance which covers up to \$2,000,000 per individual per incident. The City does not carry additional insurance to cover claims in excess of the upper limit. Settled claims resulting from these risks have never exceeded the liability coverage over the past four years.

Unemployment Benefits:

The City provides coverage for unemployment benefits by paying into the Unemployment Compensation Fund established by state law and managed by the State of South Dakota.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONCLUDED)
DECEMBER 31, 2011**

(10) Notes Receivable

Notes receivable are revolving loans the City makes to promote urban development. The following is a summary of the notes receivable at December 31, 2011:

Governmental:

<u>Loan</u>	<u>Collateral</u>	<u>Rate</u>	<u>Maturity</u>	<u>Balance</u>
Key City Shopping	Building	1.5%	October 2012	\$ 203,463
Jamison International	Inventory and Equipment	7.5%	September 2011	6,664
P & J Industries	Equipment	5%	November 2012	11,116
Western Door Company	Equipment	3%	September 2012	15,890
Independent Cycle	Personal Gurantee of President	5%	June 2015	75,818
				\$ 312,951

Business -Type:

<u>Loan</u>	<u>Collateral</u>	<u>Rate</u>	<u>Maturity</u>	<u>Balance</u>
Mount Rodney RV Park, LLC	None	3%	September 2015	\$ 50,000

(11) Governmental Assets Transferred to Proprietary Funds

In 2011, the Ambulance and Special Sanitation Funds were changed from governmental to proprietary funds, with a transfer of net assets totaling **\$1,065,589**, including capital assets totaling **\$554,969**. The beginning balances were restated for the adoption of GASB No. 54, "Fund Balance Reporting and Governmental Fund Type Definitions."

REQUIRED SUPPLEMENTARY INFORMATION

CITY OF STURGIS

**BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2011**

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual - Budgetary Basis</u>	<u>Variance</u>
Revenue				
<i>Taxes:</i>				
311 General Property Taxes	\$ 2,685,124	\$ 2,685,124	\$ 2,570,812	\$ (114,312)
313 General Sales and Use Taxes	1,322,781	1,322,781	1,339,150	16,369
315 Amusement Taxes	-	-	924	924
319 Penalties and Interest on Delinquent Taxes	-	-	15,104	15,104
320 Licenses and Permits	504,666	504,666	397,835	(106,831)
<i>Intergovernmental Revenue:</i>				
331 Federal Grants	37,248	37,248	11,713	(25,535)
334 State Grants	21,165	21,165	-	(21,165)
335 Bank Franchise Tax	10,442	10,442	2,329	(8,113)
335 Liquor Tax Reversion	35,203	35,203	29,536	(5,667)
335 Motor Vehicle Licenses	51,102	51,102	53,712	2,610
335.1 Local Government Highway and Bridge Fund	73,317	73,317	101,767	28,450
338 County Highway and Bridge Reserve Tax (25%)	5,855	5,855	5,855	-
338 Port of Entry	12,140	12,140	14,373	2,233
339 Other	8,007	8,007	9,478	1,471
<i>Charges for Goods and Services:</i>				
341 General Government	1,096,192	1,096,192	859,291	(236,901)
342 Public Safety	48,208	48,208	40,957	(7,251)
343 Highways and Streets	2,643	2,643	774	(1,869)
345 Health	1,285	1,285	634	(651)
346 Culture and Recreation	338,732	338,732	300,154	(38,578)
349 Other	-	-	43,637	43,637
<i>Fines and Forfeits:</i>				
351 Court Fines and Costs	6,643	6,643	3,910	(2,733)
<i>Miscellaneous Revenue:</i>				
361 Earnings on Deposits and Investments	17,020	17,020	3,813	(13,207)
362 Rentals	4,097	4,097	8,111	4,014
363 Special Assessments	11,059	11,059	1,867	(9,192)
367 Contributions and Donations - Private Sources	12,932	12,932	64,114	51,182
369 Other	2,332	2,332	860	(1,472)
Total Revenue	6,308,193	6,308,193	5,880,710	(427,483)

CITY OF STURGIS

**BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS (CONTINUED)
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2011**

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual - Budgetary Basis</u>	<u>Variance</u>
Expenditures				
<i>General Government:</i>				
411 Legislative	398,208	402,908	199,989	202,919
414 Financial Administration	1,203,816	1,237,366	976,707	260,659
419 Other	1,162,421	1,189,421	1,176,972	12,449
<i>Public Safety:</i>				
421 Police	1,753,489	1,797,611	1,761,263	36,348
422 Fire	182,618	182,618	149,473	33,145
<i>Public Works:</i>				
431 Highway and Streets	620,974	620,974	613,225	7,749
435 Airport	41,671	45,971	43,781	2,190
437 Cemeteries	88,803	88,803	81,455	7,348
<i>Health and Welfare:</i>				
441 Health	2,800	2,800	365	2,435
<i>Culture and Recreation:</i>				
451 Recreation	757,855	757,855	747,572	10,283
452 Parks	617,562	654,062	571,434	82,628
455 Library	362,652	362,652	356,496	6,156
456 Auditorium	34,425	34,425	24,246	10,179
465 Economic Development	37,500	37,500	-	37,500
Total Expenditures	7,264,794	7,414,966	6,702,978	711,988
Excess of Revenue Over (Under) Expenditures	(956,601)	(1,106,773)	(822,268)	284,505
Other Financing Sources (Uses)				
391.1 Transfers In	665,150	665,150	665,150	-
391.4 Compensation for Loss or Damage to Capital Assets	9,756	9,756	40,215	30,459
511 Transfers Out	(12,000)	(12,000)	(12,000)	-
Total Other Financing Sources	662,906	662,906	693,365	30,459
Net Change in Fund Balance	(293,695)	(443,867)	(128,903)	314,964
Fund Balance, December 31, 2010	914,064	914,064	914,064	-
Fund Balance, December 31, 2011	\$ 620,369	\$ 470,197	\$ 785,161	\$ 314,964

The accompanying supplementary notes are an integral part of the required supplementary information.

CITY OF STURGIS

BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS
CAPITAL IMPROVEMENT FUND
FOR THE YEAR ENDED DECEMBER 31, 2011

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual - Budgetary Basis</u>	<u>Variance</u>
Revenue				
<i>Taxes:</i>				
313 General Sales and Use Taxes	\$ 1,322,780	\$ 1,322,780	\$ 1,339,150	\$ 16,370
<i>Intergovernmental Revenue:</i>				
331 Federal Grants	-	225,000	650,605	425,605
334 State Grants	-	-	220,841	220,841
<i>Miscellaneous Revenue:</i>				
361 Earnings on Deposits	15,255	15,255	12,160	(3,095)
363 Special Assessments	12,233	12,233	12,133	(100)
Total Revenue	1,350,268	1,575,268	2,234,889	659,621
Expenditures				
<i>General Government:</i>				
414 Financial Administration	59,000	59,000	58,575	425
419 Other	14,000	15,075	15,072	3
<i>Public Safety:</i>				
422 Fire	20,832	20,832	20,832	-
<i>Public Works:</i>				
431 Highway and Streets	528,768	563,768	559,896	3,872
435 Airport	-	225,000	241,574	(16,574)
<i>Culture and Recreation:</i>				
451 Recreation	15,000	15,000	14,986	14
452 Parks	92,800	92,800	68,990	23,810
470 Debt Service	619,868	619,868	616,050	3,818
Total Expenditures	1,350,268	1,611,343	1,595,975	15,368
Excess of Revenue Over (Under) Expenditures	-	(36,075)	638,914	674,989
Net Change in Fund Balance	-	(36,075)	638,914	674,989
Fund Balance, December 31, 2010	985,579	985,579	985,579	-
Fund Balance, December 31, 2011	\$ 985,579	\$ 949,504	\$ 1,624,493	\$ 674,989

The accompanying supplementary notes are an integral part of the required supplementary information.

CITY OF STURGIS

**BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS
 REVOLVING LOAN FUND
 FOR THE YEAR ENDED DECEMBER 31, 2011**

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual - Budgetary Basis</u>	<u>Variance</u>
Revenue				
<i>Miscellaneous Revenue:</i>				
361 Earnings on Deposits	\$ 5,637	\$ 5,637	\$ 16,644	\$ 11,007
363 Special Assessments	2,885	2,885	-	(2,885)
Total Revenue	8,522	8,522	16,644	8,122
Net Change in Fund Balance	8,522	8,522	16,644	8,122
Fund Balance, December 31, 2010	1,294,334	1,294,334	1,294,334	-
Fund Balance, December 31, 2011	\$ 1,302,856	\$ 1,302,856	\$ 1,310,978	\$ 8,122

The accompanying supplementary notes are an integral part of the required supplementary information.

CITY OF STURGIS

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION DECEMBER 31, 2011

(1) Budgets and Budgetary Accounting

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

1. At the first regular board meeting in September of each year or within ten days thereafter, the governing board introduces the annual appropriation ordinance for the ensuing fiscal year.
2. After adoption by the governing board, the operating budget is legally binding and actual disbursements for each purpose cannot exceed the amounts budgeted, except as indicated in item number 4.
3. A line item for contingencies may be included in the annual budget. Such a line item may not exceed 5 percent of the total municipal budget and may be transferred by resolution of the governing board to any other budget category that is deemed insufficient during the year.
4. If it is determined during the year that sufficient amounts have not been budgeted, state statute allows the adoption of supplemental budgets.
5. Unexpended appropriations lapse at year end unless encumbered by resolution of the governing board.
6. The City did not encumber any amounts at December 31, 2011.
7. Formal budgetary integration is employed as a management control device during the year for the general fund and major special revenue funds.
8. Budgets for the general fund and major special revenue funds are adopted on a basis consistent with accounting principles generally accepted in the United States (USGAAP).

(2) GAAP Budgetary Accounting Basis Differences

The financial statements prepared in conformity with USGAAP applied within the context of the modified cash basis of accounting present capital outlay expenditure information in a separate category of expenditures. Under the budgetary basis of accounting, capital outlay expenditures are reported within the function to which they relate. For example, the purchase of a new fire truck would be reported as a capital outlay expenditure on the Governmental Funds Statement of Revenues, Expenditures and Changes in Fund Balances, however in the Budgetary RSI Schedule, the purchase of a fire truck would be reported as an expenditure of the Public Safety/Fire Department function of government, along with all other current Fire Department related expenditures.

OTHER SUPPLEMENTARY INFORMATION

CITY OF STURGIS

**COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS
DECEMBER 31, 2011**

		Special Sales Tax Fund	Library Fund	TIF Funds	Alice W. Dunn Fund	Perpetual Maintenance Fund	Total Nonmajor Governmental Funds
Assets							
104	Interest Bearing Accounts	\$ 82,779	\$ 79,867	\$ 18,004	\$ 43,071	\$ 152,628	\$ 376,349
105	Savings Certificates	-	-	-	427,535	-	427,535
108	Sales Tax Receivable	13,302	-	-	-	-	13,302
Total Assets		\$ 96,081	\$ 79,867	\$ 18,004	\$ 470,606	\$ 152,628	\$ 817,186
Liabilities and Fund Balances							
<i>Liabilities</i>							
202	Accounts Payable	\$ -	\$ 9,694	\$ 8,308	\$ -	\$ -	\$ 18,002
217	Accrued Taxes Payable	-	-	-	-	58	58
Total Liabilities		-	9,694	8,308	-	58	18,060
<i>Fund Balances</i>							
263.51 Nonspendable -							
	Perpetual Care Cemetary	-	-	-	-	50,000	50,000
263.99 Nonspendable - Library Trust							
		-	-	-	327,535	-	327,535
264.01 Restricted - Debt Service							
		-	-	9,696	-	-	9,696
264.03 Restricted -							
	Perpetual Care Cemetary	-	-	-	-	102,570	102,570
264.04 Restricted - BID Tax							
		96,081	-	-	-	-	96,081
264.05 Restricted - Library Purposes							
		-	70,173	-	143,071	-	213,244
Total Fund Balances		96,081	70,173	9,696	470,606	152,570	799,126
Total Liabilities and Fund Balances		\$ 96,081	\$ 79,867	\$ 18,004	\$ 470,606	\$ 152,628	\$ 817,186

CITY OF STURGIS

**COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
NONMAJOR GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2011**

	<u>Special Sales Tax Fund</u>	<u>Library Fund</u>	<u>TIF Funds</u>	<u>Alice W. Dunn Fund</u>	<u>Perpetual Maintenance Fund</u>	<u>Total Nonmajor Governmental Funds</u>
Revenue:						
311 General Property Taxes	\$ -	\$ -	\$ 97,799	\$ -	\$ -	\$ 97,799
313 General Sales and Use Taxes	260,408	-	-	-	-	260,408
361 Earnings on Deposits and Investments	295	354	-	15,783	-	16,432
367 Contributions and Donations - Private Sources	-	16,511	-	-	-	16,511
369 Other	-	9,676	-	-	5,177	14,853
Total Revenue	260,703	26,541	97,799	15,783	5,177	406,003
Expenditures:						
455 Library	-	33,396	-	-	-	33,396
460 Conservation and Development	273,546	-	-	-	-	273,546
470 Debt Service	-	-	118,596	-	-	118,596
Total Expenditures	273,546	33,396	118,596	-	-	425,538
Net Change in Fund Balances	(12,843)	(6,855)	(20,797)	15,783	5,177	(19,535)
Fund Balance, December 31, 2010	108,924	77,028	30,493	454,823	147,393	818,661
Fund Balance, December 31, 2011	\$ 96,081	\$ 70,173	\$ 9,696	\$ 470,606	\$ 152,570	\$ 799,126

CITY OF STURGIS

**SCHEDULE OF RALLY ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2011**

Revenue

	<i>Taxes:</i>		
313	General Sales and Use Taxes	\$	194,000
320	Licenses and Permits		246,970
	<i>Charges for Goods and Services:</i>		
341	General Government		740,370
Total Revenue			1,181,340

Expenditures

	<i>General Government:</i>		
414	Financial Administration		17,183
419	Other		684,722
	<i>Public Safety:</i>		
421	Police		254,024
422	Fire		9,032
	<i>Public Works:</i>		
431	Highway and Streets		19,100
	<i>Culture and Recreation:</i>		
451	Recreation		22,406
452	Parks		9,585
Total Expenditures			1,016,052
Excess of Revenue over Expenditures			\$ 165,288

SINGLE AUDIT SECTION

CITY OF STURGIS

**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED DECEMBER 31, 2011**

Status of Prior Audit Findings and Recommendations:

The City does not consider the additional costs of preparing its financial statements to be necessary, so Finding #10-1 will be repeated as Finding #11-1 for the year ending December 31, 2011.

The City continues to improve on recording year-end adjustments; however as significant audit adjustments were necessary, Finding #10-2 will be repeated as Finding #11-2 for the year ending December 31, 2011.

The City has created the appropriate segregation of duties, reduced the number of funds, reconciled cash accounts to the general ledger, and reconciled property tax revenue to remittances. Therefore, Findings #10-3, #10-4, #10-6 and #10-8 will not be repeated for the year ending December 31, 2011.

Administration is aware that the budgeting process needs to be more diligent in completing supplemental appropriations, when necessary. Finding #10-5 will be repeated as Finding #11-3 for the year ending December 31, 2011.

The City Council approved all water expenditures including those of the water fund, so Finding #10-7 will not be repeated for the year ending December 31, 2011.

The City complied with Suspension and Debarment requirements for the federal award program. Therefore, Finding #10-9 will not be repeated for the year ending December 31, 2011.

CITY OF STURGIS

SCHEDULE OF FINDINGS AND QUESTIONED COSTS FOR THE YEAR ENDED DECEMBER 31, 2011

A. SUMMARY OF AUDIT RESULTS

1. The auditor's report expresses an unqualified opinion on the financial statements of the City of Sturgis (the City).
2. Material weaknesses and significant deficiencies were disclosed during the audit of the financial statements are reported in the Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards.
3. No instances of noncompliance material to the financial statements of the City were disclosed during the audit.
4. A material weakness was disclosed during the audit of the major federal award program as reported in the Independent Auditor's Report on Compliance with Requirements that Could Have a Direct and Material Effect on Each Major Program and on Internal Control over Compliance in Accordance with OMB Circular A-133.
5. The auditor's report on compliance for the major federal award program for the City expresses an unqualified opinion.
6. Audit findings relative to the major federal award program for the City are reported in Part C of this schedule.
7. The program tested as a major program was the Water and Waste Disposal Systems for Rural Communities (#10.760).
8. The threshold for distinguishing type A and B programs was \$300,000.
9. The City was not considered a low-risk auditee under the criteria established in OMB Circular A-133.

B. FINDINGS – FINANCIAL STATEMENT AUDIT

MATERIAL WEAKNESSES

11-1 FINDING: Financial Statement Preparation

Condition/Cause: As in prior years, we were requested to draft the audited financial statements, related footnote disclosures, and Schedule of Expenditures of Federal Awards (SEFA) as part of our regular audit services. Ultimately, it is management's responsibility to provide for the preparation of the City's statements and footnotes, and the responsibility of the auditor to determine the fairness of presentation of those statements. From a practical standpoint, we do both for the City at the same time in connection with our audit. This is not unusual for us to do with municipalities of your size.

Criteria and Effect: This deficiency could result in a material misstatement to the financial statements and Schedule of Expenditures of Federal Awards that could have been prevented or detected by the City's management.

Questioned Costs: None

Recommendation: As in prior years, we have instructed management to review a draft of the auditor prepared financials in detail for their accuracy; we have answered any questions they might have, and have encouraged research of any accounting guidance in connection with the adequacy and appropriateness of classification and disclosure in the City's statements. We are satisfied that the appropriate steps have been taken to provide the City with the completed financial statements. It is the responsibility of management and those charged with governance to make the decision whether to accept the degree of risk associated with this condition because of cost or other considerations.

CITY OF STURGIS

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED DECEMBER 31, 2011**

B. FINDINGS – FINANCIAL STATEMENT AUDIT (CONTINUED)

MATERIAL WEAKNESSES (CONTINUED)

11-1 FINDING: Financial Statement Preparation (Continued)

Response/Corrective Action Plan: At this time, the City will accept the degree of risk that is associated with this condition. For future audits, the City will continue to monitor the financial statement and SEFA preparation and determine if any modification can be done to the procedure. The Finance Officer is responsible for the corrective action plan for this finding.

11-2 FINDING: Audit Adjustments

Condition/Cause: During the course of our engagement, we proposed material audit adjustments. Adjustments included adjusting fund balance, capital assets, debt balances, liquor fund reserved cash account and special assessment liability. Additionally, we posted several reclassification entries with no effect on net income. In addition, entries were proposed as a part of the audit, but were not recorded due to the overall insignificance on the financial statements.

Criteria and Effect: These adjustments would not have been identified as a result of the City’s existing internal controls, and therefore, could have resulted in a material misstatement of the City’s financial statements.

Questioned Costs: None

Recommendation: We recommend that management consider the following:

- a. All capital assets should be included in the depreciation schedule or construction in progress listing and recorded as such in the general ledger.
- b. Special assessment payments received and remitted should be posted against the liability account, rather than debt service.
- c. Debt reserves should be established to comply with debt covenants.
- d. Debt balances should be reviewed annually and adjusted accordingly.

Response/Corrective Action Plan: The City will make every effort to make the proper accounting adjustments. The City will be implementing a capital assets software program through Caselle that should help with the accuracy in the general ledger. The two programs tie together and allow updating to the general ledger from the capital assets software. More consideration will be taken when new bonds are issued to make sure the debt reserve is properly recorded. The Finance Officer is responsible for the corrective action plan for this finding.

SIGNIFICANT DEFICIENCIES

11-3 FINDING: Budgetary Overdraft

Condition/Cause: The City has a budgetary overdraft in violation of South Dakota Codified Law 9-21-9, in the following department:

Fund	Department	Overdraft
Capital Improvement	Public Works - Airport	\$ 16,574

CITY OF STURGIS

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONTINUED)
FOR THE YEAR ENDED DECEMBER 31, 2011**

B. FINDINGS – FINANCIAL STATEMENT AUDIT (CONTINUED)

SIGNIFICANT DEFICIENCIES (CONTINUED)

11-3 FINDING: Budgetary Overdraft (Continued)

Criteria and Effect: The City did not follow state law.

Questioned Costs: None

Recommendation: The City in the future should complete supplemental appropriations for unbudgeted expenditures.

Response/Corrective Action Plan: The City will develop procedures to ensure budget overdrafts are supplemented. The Finance Officer is responsible for the corrective action plan for this finding.

11-4 FINDING: Debt Reserve Covenant

Condition/Cause: We noted the City is out of compliance with its debt covenant to maintain debt reserves equal to 10 percent of the annual payment over the life of the loan until one installment is accumulated. The City contacted Rural Development who provided a verbal waiver with the understanding the City would have the proper debt reserve balance in 2012.

Criteria and Effect: This could cause difficulty obtaining borrowings in the future, and may cause current debt holders to require sales tax bonds to be paid prior to maturity.

Questioned Costs: None

Recommendation: The City should ensure the appropriate amount is accumulated in a restricted cash account upon each annual installment being made.

Response/Corrective Action Plan: More consideration will be given when new bonds are issued and to make sure the debt reserve is properly recorded. The Finance Officer is responsible for the corrective action plan for this finding.

11-5 FINDING: Subsidiary Ledgers

Condition/Cause: The City was unable to generate utility accounts receivable listings that agreed to the general ledger.

Criteria and Effect: Subsidiary listings should be prepared as part of the year-end process and reconciled to the general ledger. The effects of deficiencies in subsidiary listings can result in undetected errors, omissions, or misappropriation of assets of the City.

Questioned Costs: None

Recommendations: Subsidiary listings should be prepared at least annually as part of the year end-process and reconciled to the general ledger. Significant progress was made, but subsidiary listings should be updated at the same time as year-end entries.

Response/Corrective Action Plan: At year-end the City will be more diligent to ensure all subsidiary listings reconcile to the general ledger. The Finance Officer is responsible for the correcting action plan for this finding.

CITY OF STURGIS

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONCLUDED)
FOR THE YEAR ENDED DECEMBER 31, 2011**

C. FINDINGS – COMPLIANCE AUDIT

MATERIAL WEAKNESS

Finding #11-1 listed in Part B relates to the major federal award program of the City, the Water and Waste Disposal Systems for Rural Communities (#10.760). The finding relates to the reporting compliance requirement.

CITY OF STURGIS

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2011**

	CFDA Number	Amount
<i>U.S. Department of Transportation:</i>		
Pass-Through the S.D. Federal Aviation Administration Airport Improvement Program	20.106	\$ 241,574
<i>U.S. Department of Treasury Direct Program:</i>		
Joint Intelligence Room Computer System	21.XXX	1,765
<i>U.S. Department of Agriculture Direct Program:</i>		
Water and Waste Disposal Systems for Rural Communities (Note 1)	10.760	435,414
<i>National Endowment for the Arts Direct Program:</i>		
Promotion of the Arts Partnership Agreements	45.025	517
<i>U.S. General Services Administration:</i>		
Pass-Through the S.D. Federal Property Agency Donation of Surplus Personal Property	39.003	37,755
Total		\$ 717,025

Note 1: This program was tested as a major program.

Note 2: This schedule is presented on the modified accrual basis of accounting.

OTHER REPORTS



Ketel Thorstenson, LLP

Certified Public Accountants/Business & Personal Consultants

810 Quincy Street
P.O. Box 3140, Rapid City, South Dakota 57709
Telephone (605) 342-5630 • e-mail: ktllp@ktllp.com

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

City Council
City of Sturgis
Sturgis, South Dakota

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the **CITY OF STURGIS** (the City) as of and for the year ended December 31, 2011, which collectively comprise the City's basic financial statements, and have issued our report thereon dated September 19, 2012. 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.

Internal Control over Financial Reporting

In planning and performing our audit, we considered the City's internal control over financial reporting as a basis for designing our auditing procedures 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 over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses and other deficiencies that we consider to be significant deficiencies.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the City's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs as Findings #11-1 and #11-2 to be material weaknesses.

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 deficiencies described in the accompanying Schedule of Findings and Questioned Costs as Findings #11-4 and #11-5 to be significant deficiencies.

City Council

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed one instance of noncompliance or other matter that is required to be reported under Government Auditing Standards which is described in the accompanying Schedule of Findings and Questioned Costs as Finding #11-3.

The City's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the City's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the governing board and management of the City of Sturgis, federal awarding agencies and pass-through entities, the South Dakota Legislature, and state granting agencies, and is not intended to be, and should not be, used by anyone other than those specified parties. However, as required by South Dakota Law 4-11-11 and OMB Circular A-133, this report is a matter of public record and its distribution is not limited.



KETEL THORSTENSON, LLP
Certified Public Accountants

September 19, 2012



Ketel Thorstenson, LLP

Certified Public Accountants/Business & Personal Consultants

810 Quincy Street
P.O. Box 3140, Rapid City, South Dakota 57709
Telephone (605) 342-5630 • e-mail: ktllp@ktllp.com

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

City Council
City of Sturgis
Sturgis, South Dakota

Compliance

We have audited the compliance of the **CITY OF STURGIS** (the City) with the types of compliance requirements described in the "U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement" that could have a direct and material effect on the City's major federal program for the year ended December 31, 2011. The City's major federal program is identified in the summary of audit results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the City's management. Our responsibility is to express an opinion on the City's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and OMB Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations." Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City's compliance with those requirements.

In our opinion, the City complied, in all material respects, with the requirements referred to above that could have a direct and material effect on its major federal program for the year ended December 31, 2011.

Internal Control over Compliance

Management of the City is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the City's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

City Council

Our consideration of the internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in the internal control over compliance that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified a deficiency in internal control over compliance that we consider to be a material weakness.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiency in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as #11-1 to be a material weakness.

The City's response to the finding identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the City's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the governing board and management of the City of Sturgis, federal awarding agencies and pass-through entities, the South Dakota Legislature, and state granting agencies, and is not intended to be, and should not be, used by anyone other than those specified parties. However, as required by South Dakota Law 4-11-11 and OMB Circular A-133, this report is a matter of public record and its distribution is not limited.



KETEL THORSTENSON, LLP
Certified Public Accountants

September 19, 2012