



CITY OF STURGIS

FINANCIAL STATEMENTS AND INDEPENDENT AUDITOR'S REPORT
DECEMBER 31, 2012



Ketel Thorstenson, LLP

Certified Public Accountants/Business & Personal Consultants

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

CITY OF STURGIS

TABLE OF CONTENTS

	<u>PAGE</u>
Independent Auditor’s Report	1-2
Management’s Discussion and Analysis	3-11
<i>Government-Wide Financial Statements:</i>	
Statement of Net Position	12
Statement of Activities	13
<i>Fund Financial Statements:</i>	
Balance Sheet – Governmental Funds	14
Reconciliation of Governmental Funds Balance Sheet to Government-Wide Statement of Net Position	15
Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Funds	16-17
Reconciliation of Governmental Funds Statement of Revenues, Expenditures and Changes in Fund Balances to Government-Wide Statement of Activities	18
Statement of Net Position – Proprietary Funds	19
Statement of Revenues, Expenses, and Changes in Fund Net Position – Proprietary Funds	20
Statement of Cash Flows – Proprietary Funds	21
Statement of Fiduciary Net Position	22
Notes to Financial Statements	23-40
<i>Required Supplementary Information:</i>	
Budgetary Comparison Schedule – Budgetary Basis – General Fund	41-42
Budgetary Comparison Schedule – Budgetary Basis – Capital Improvement Fund	43
Budgetary Comparison Schedule – Budgetary Basis – Revolving Loan Fund	44
Notes to Required Supplementary Information	45
<i>Other Supplementary Information:</i>	
Combining Balance Sheet – Nonmajor Governmental Funds	46
Combining Statement of Revenues, Expenditures, and Changes in Fund Balances – Nonmajor Governmental Funds	47
Schedule of Rally Activities	48

CITY OF STURGIS

TABLE OF CONTENTS (CONTINUED)

Single Audit Section:

Summary Schedule of Prior Audit Findings	49
Schedule of Findings and Questioned Costs	50-52
Schedule of Expenditures of Federal Awards	53

Other Reports:

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 <i>Government Auditing Standards</i>	54-55
Independent Auditor's Report on Compliance for Each Major Federal Program and on Internal Control over Compliance as Required by OMB Circular A-133	56-57



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

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the **CITY OF STURGIS** (the City), as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City as of December 31, 2012, 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.

Report on Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 11, and budgetary comparison information on pages 41 through 45 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.

Report on Other Supplementary Information

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 46 through 48 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 53 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 and schedule of expenditures of federal awards 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.

The schedule of rally activities on page 48 has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated August 13, 2013, 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. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's internal control over financial reporting and compliance.



KETEL THORSTENSON, LLP
Certified Public Accountants

August 13, 2013

CITY OF STURGIS

MANAGEMENT'S DISCUSSION AND ANALYSIS DECEMBER 31, 2012

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, 2012. 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 \$232,293 more than the \$8,123,433 governmental program expenditures. This does not take into account any transfers in/out. The overall change in net position, transfers included, in governmental activities increased three percent compared to last year.
- In the City's business-type activities, revenues exceeded expenses by \$459,198, which includes transfers and any activity due to the disposal of fixed assets. The increase is due to a substantial usage of water due to a very dry spring, summer, and fall, and an increase in water rates. Additionally, the ambulance fund had an increase in calls for service.

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, 2012**

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 Position and Statement of Activities	Balance Sheet and Statement of Revenues, Expenditures, and Changes in Fund Balances	Statement of Net Position; Statement of Revenues, Expenses, and Changes in Net Position; 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 position 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, 2012

OVERVIEW OF THE FINANCIAL STATEMENTS (CONCLUDED)

Government-wide Statements (Continued)

The two government-wide statements report the City's net position and how they have changed. Net position – 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 position 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, 2012**

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE

Net Position

The City's combined net position increased three percent between fiscal year 2011 and 2012. (See Table A-1).

Table A-1 Summarized Statement of Net Position						
	Governmental Activities		Business-Type Activities		Total	
	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>
Current and Other Assets	\$ 6,013,358	\$ 5,166,440	\$ 2,110,558	\$ 2,216,229	\$ 8,123,916	\$ 7,382,669
Capital Assets	33,635,090	33,550,581	21,155,702	18,219,729	54,790,792	51,770,310
Total Assets	\$ 39,648,448	\$ 38,717,021	\$ 23,266,260	\$ 20,435,958	\$ 62,914,708	\$ 59,152,979
Long-Term Debt	\$ 5,835,342	\$ 5,776,740	\$ 5,771,873	\$ 3,882,866	\$ 11,607,215	\$ 9,659,606
Other Liabilities	334,221	368,769	848,223	366,126	1,182,444	734,895
Total Liabilities	6,169,563	6,145,509	6,620,096	4,248,992	12,789,659	10,394,501
<i>Net Position:</i>						
Net Investment in Capital Assets	27,981,596	27,969,580	15,462,829	14,404,377	43,444,425	42,373,957
Restricted	3,479,993	3,583,942	8,196	4,098	3,488,189	3,588,040
Unrestricted	2,017,296	1,017,990	1,175,139	1,778,491	3,192,435	2,796,481
Total Net Position	\$ 33,478,885	\$ 32,571,512	\$ 16,646,164	\$ 16,186,966	\$ 50,125,049	\$ 48,758,478
Beginning Net Position	32,571,512	31,718,448	16,186,966	16,335,330	48,758,478	48,053,778
Prior Period Adjustment (Note 11)	139,128	-	-	-	139,128	-
Increase (Decrease) in Net Position	\$ 768,245	\$ 853,064	\$ 459,198	\$ (148,364)	\$ 1,227,443	\$ 704,700
Percentage of Increase (Decrease) in Net Position	2%	3%	3%	-1%	3%	1%

The Statement of Net Position 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 position.

Changes in Net Position

The City's revenues totaled \$14,844,351 (See Table A-2). Well over half of the City's revenue comes from charges for services and taxes, with 55 cents of every dollar raised coming from charges for services (primarily liquor and water operations) and 38 cents of every dollar raised coming from some type of tax (See Figure A-2). Of the City's total revenue, 3 percent comes from state and federal grants for capital purposes, and the rest comes from operating grants, contributions, state shared revenue, interest and miscellaneous.

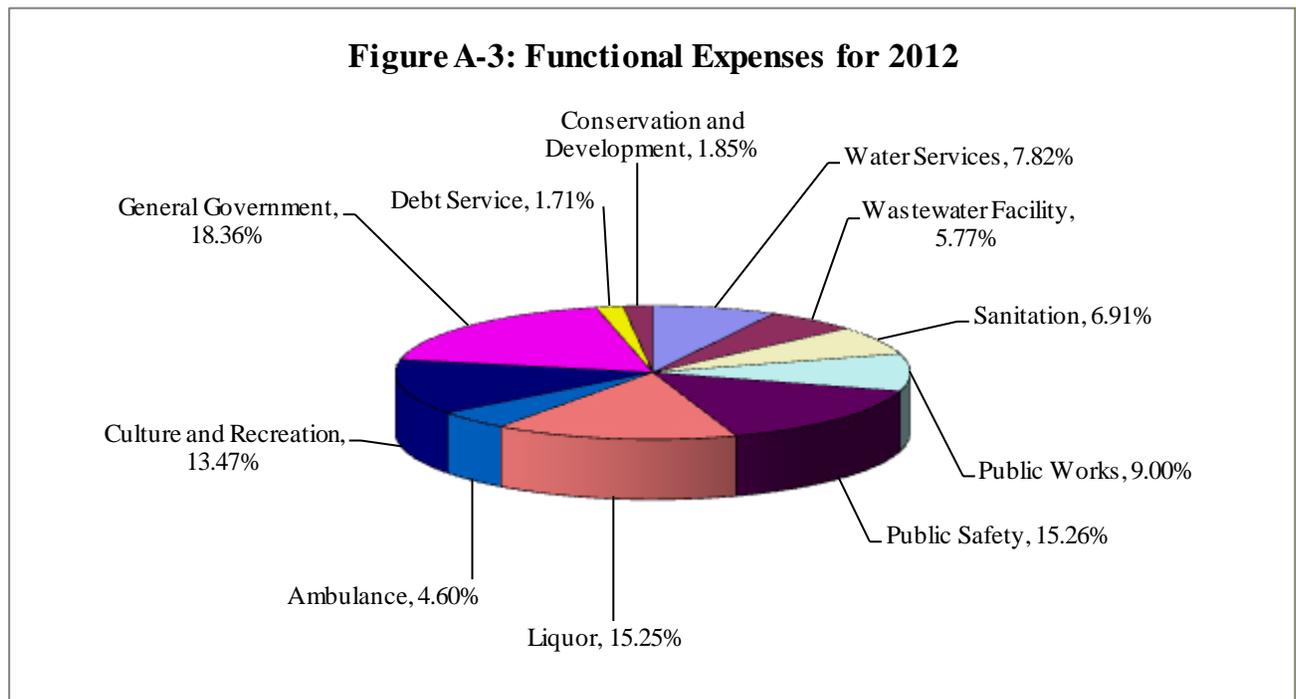
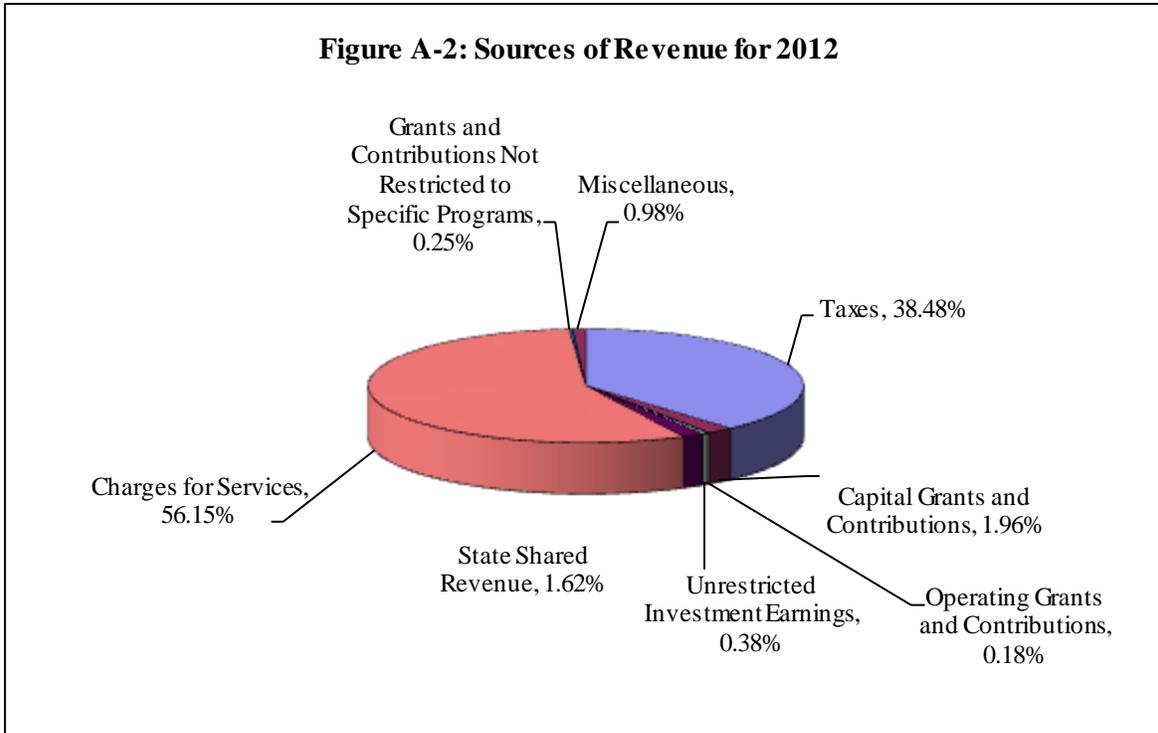
CITY OF STURGIS

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
DECEMBER 31, 2012**

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONTINUED)

Changes in Net Position (Continued)

The total cost of all programs and services was \$13,616,908 (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, 2012**

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONTINUED)

Changes in Net Position (Concluded)

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

Table A-2 Changes in Net Position						
	Governmental Activities		Business - Type Activities		Total	
	2012	2011	2012	2011	2012	2011
Revenues						
Program Revenues						
Charges for Services	\$ 1,764,818	\$ 1,633,261	\$ 6,569,983	\$ 5,806,484	\$ 8,334,801	\$ 7,439,745
Operating Grants and Contributions	25,952	2,282	-	-	25,952	2,282
Capital Grants and Contributions	272,968	882,891	18,243	44,276	291,211	927,167
General Revenues						
Taxes	5,711,811	5,654,893	-	-	5,711,811	5,654,893
State Shared Revenue	240,932	187,344	-	-	240,932	187,344
Grants and Contributions not Program Specific	36,795	80,625	-	-	36,795	80,625
Unrestricted Investment Earnings	40,140	49,049	16,010	21,435	56,150	70,484
Miscellaneous	123,182	107,676	23,517	28,028	146,699	135,704
Total Revenues	8,216,598	8,598,021	6,627,753	5,900,223	14,844,351	14,498,244
Expenses						
General Government	2,499,684	2,557,890	-	-	2,499,684	2,557,890
Public Safety	2,078,228	2,008,909	-	-	2,078,228	2,008,909
Public Works	1,225,870	1,307,224	-	-	1,225,870	1,307,224
Health and Welfare	-	365	-	-	-	365
Culture and Recreation	1,834,223	2,028,141	-	-	1,834,223	2,028,141
Conservation and Development	253,323	273,546	-	-	253,323	273,546
Debt Service	232,105	222,032	-	-	232,105	222,032
Liquor	-	-	2,075,988	2,026,433	2,075,988	2,026,433
Water Services	-	-	1,064,488	1,038,152	1,064,488	1,038,152
Wastewater Services	-	-	785,027	748,589	785,027	748,589
Sanitation Services	-	-	941,334	996,604	941,334	996,604
Ambulance	-	-	626,638	585,659	626,638	585,659
Total Expenses	8,123,433	8,398,107	5,493,475	5,395,437	13,616,908	13,793,544
Excess Before Transfers	93,165	199,914	1,134,278	504,786	1,227,443	704,700
Transfers	675,080	653,150	(675,080)	(653,150)	-	-
Increase (Decrease) in Net Position	768,245	853,064	459,198	(148,364)	1,227,443	704,700
Prior Period Adjustment (Note 11)	139,128	-	-	-	139,128	-
Ending Net Position	\$ 33,478,885	\$ 32,571,512	\$ 16,646,164	\$ 16,186,966	\$ 50,125,049	\$ 48,758,478

CITY OF STURGIS

MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED) DECEMBER 31, 2012

FINANCIAL ANALYSIS OF THE CITY AS A WHOLE (CONCLUDED)

Governmental Activities

Total revenues of the governmental activities for the City decreased by 4 percent compared to the prior year, while total expenses decreased by 3 percent. The primary reason for the decrease of revenue is the City did not receive as much grant funding in 2012, compared to 2011.

Business-Type Activities

Operating revenues of the City's business-type activities increased by approximately 11 percent compared to the prior year, while total expenses remained flat. The overall increase in revenues and expenses is due to an increase in usage of water, an increase in water rates, and more calls for service in the ambulance fund. The increase in expenses is due to higher interest expense on bonds and the conveying of real property to SEDC, resulting in a loss on the donation of such property.

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 and Revolving Loan Funds), Debt Service Funds, 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 City had a budget overrun in capital improvements within the recreation department, due to the purchase of the new HVAC and boiler equipment for the community center. Supplemental appropriations should have been made to cover the additional expenses for the community center equipment.

CITY OF STURGIS

**MANAGEMENT'S DISCUSSION AND ANALYSIS (CONTINUED)
DECEMBER 31, 2012**

CAPITAL ASSET ADMINISTRATION

By the end of 2012, the City had invested \$54,790,792 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 \$3,020,482, primarily due to the construction of phase I and phase II of the drinking water project, as well as construction on the Lazelle Street water line replacement.

Table A-3 Capital Assets (net of depreciation)				
	Governmental Activities		Business-type Activities	
	2012	2011	2012	2011
Land	\$ 2,184,497	\$ 2,184,497	\$ 738,681	\$ 826,108
Construction Work in Progress	11,250	106,575	4,065,422	602,476
Buildings	8,873,674	9,142,763	1,753,565	1,814,199
Improvements Other Than Buildings	20,945,658	20,607,499	13,426,629	13,780,761
Machinery and Equipment	1,620,011	1,509,247	1,171,405	1,196,185
Total Capital Assets	\$ 33,635,090	\$ 33,550,581	\$ 21,155,702	\$ 18,219,729

LONG-TERM DEBT

At year-end, the City had \$11,607,215 in Sales Tax Revenue Bonds, Contract Payable, General Obligation Bonds and other long-term obligations. This is an increase of \$1,947,609 as shown on Table A-4 below.

Table A-4 Outstanding Debt and Obligations				
	Governmental Activities		Business-type Activities	
	2012	2011	2012	2011
Compensated Absences	\$ 181,848	\$ 195,739	\$ 79,000	\$ 67,514
Tax Increment Financing Obligations	376,204	406,001	-	-
Marcotte Property	547,290	-	-	-
Sales Tax Revenue Bonds	4,730,000	5,175,000	4,067,873	1,895,352
General Obligation Bonds	-	-	1,625,000	1,920,000
Total Outstanding Debt and Obligations	\$ 5,835,342	\$ 5,776,740	\$ 5,771,873	\$ 3,882,866

During the current year, the City obtained additional water revenue bonds 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, 2012

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 slight decrease in total property valuation of \$2,709,722, or .0078 percent. The City requested a 2.5 percent increase in property taxes for 2012. The growth factor of 2011 taxes payable in 2012 was .48 percent. The growth factor for 2012 taxes payable in 2013 was .769 percent.

The second largest portion of revenue within the general fund is retail sales tax. In 2012, the City experienced an increase of 2 percent compared to 2011. The increase was due to more tourist traffic before and after the annual motorcycle rally. The City also hosted other events in the downtown area, resulting in more sales revenue.

The adopted 2013 general fund expenditures budget decreased by 3.7 percent, as the City is decreasing spending to increase the general fund reserves, as well as the reserves of all other operating funds.

The City's business-type activities, other than liquor and sanitation, will have changes in 2013 compared to 2012. The wastewater fund increased the sewer use fee by 3 percent and the Council adopted a water and wastewater availability fee for customers who do not stay year-round in their homes. This will increase revenue for 2013 in these two funds. The ambulance fund will be billing internally, which will decrease expenses. Additionally, they are anticipating an increase in revenue to due to an increased demand each year for ambulance service in the area.

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 POSITION
DECEMBER 31, 2012

	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTAL
Assets			
Cash and Cash Equivalents (Note 2)	\$ 3,948,878	\$ 1,403,677	\$ 5,352,555
Receivables, Net	542,821	417,851	960,672
Notes Receivable (Note 10)	15,890	37,500	53,390
Internal Balances (Note 6)	(10,000)	10,000	-
Inventories	1,485	221,860	223,345
Deferred Charges	123,103	-	123,103
Other Assets	21,472	11,474	32,946
Investment Real Estate Held for Sale	608,100	-	608,100
Restricted Assets:			
Cash with Fiscal Agent (Note 5)	625,765	8,196	633,961
Deposits (Note 9)	135,844	-	135,844
Capital Assets (Note 4)			
Land and Construction Work in Progress	2,195,747	4,804,103	6,999,850
Other Capital Assets, Net of Depreciation	31,439,343	16,351,599	47,790,942
Total Assets	\$ 39,648,448	\$ 23,266,260	\$ 62,914,708
Liabilities			
Accounts Payable	\$ 192,502	\$ 618,345	\$ 810,847
Other Current Liabilities	141,719	229,878	371,597
Noncurrent Liabilities (Note 5):			
Due Within One Year	902,829	451,370	1,354,199
Due in More Than One Year	4,932,513	5,320,503	10,253,016
Total Liabilities	6,169,563	6,620,096	12,789,659
Net Position			
Net Investment in Capital Assets	27,981,596	15,462,829	43,444,425
Restricted for:			
Debt Service	653,180	8,196	661,376
SDPAA (Note 9)	135,844	-	135,844
Revolving Loans	1,316,429	-	1,316,429
Special Sales Tax	671,357	-	671,357
Library Purposes	219,297	-	219,297
Permanently Restricted Purposes:			
Expendable	106,351	-	106,351
Nonexpendable	377,535	-	377,535
Unrestricted	2,017,296	1,175,139	3,192,435
Total Net Position	33,478,885	16,646,164	50,125,049
Total Liabilities and Net Position	\$ 39,648,448	\$ 23,266,260	\$ 62,914,708

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

CITY OF STURGIS

STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2012

	----- Program Revenues -----				Net (Expense) Revenue and ----- Changes in Net Position -----		
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-Type Activities	Total
Functions/Programs							
Primary Government							
Governmental Activities:							
General Government	\$ 2,499,684	\$ 1,388,088	\$ -	\$ -	\$ (1,111,596)	\$ -	\$ (1,111,596)
Public Safety	2,078,228	48,715	25,952	-	(2,003,561)	-	(2,003,561)
Public Works	1,225,870	21,785	-	272,968	(931,117)	-	(931,117)
Health and Welfare	-	1,101	-	-	1,101	-	1,101
Culture and Recreation	1,834,223	305,129	-	-	(1,529,094)	-	(1,529,094)
Conservation and Development	253,323	-	-	-	(253,323)	-	(253,323)
Interest on Long-Term Debt	232,105	-	-	-	(232,105)	-	(232,105)
Total Governmental Activities	8,123,433	1,764,818	25,952	272,968	(6,059,695)	-	(6,059,695)
Business-Type Activities:							
Liquor	2,075,988	2,134,435	-	-	-	58,447	58,447
Water	1,064,488	1,613,195	-	-	-	548,707	548,707
Wastewater	785,027	964,936	-	-	-	179,909	179,909
Sanitation	941,334	1,010,785	-	18,243	-	87,694	87,694
Ambulance	626,638	846,632	-	-	-	219,994	219,994
Total Business-Type Activities	5,493,475	6,569,983	-	18,243	-	1,094,751	1,094,751
Total Primary Government	\$ 13,616,908	\$ 8,334,801	\$ 25,952	\$ 291,211	(6,059,695)	1,094,751	(4,964,944)
General Revenues:							
Taxes:							
Property Taxes					2,697,461	-	2,697,461
Sales Taxes					3,014,350	-	3,014,350
State Shared Revenue					240,932	-	240,932
Grants and Contributions Not Restricted to Specific Programs					36,795	-	36,795
Unrestricted Investment Earnings					40,140	16,010	56,150
Miscellaneous Revenue					123,182	23,517	146,699
Transfers					675,080	(675,080)	-
Total General Revenues and Transfers					6,827,940	(635,553)	6,192,387
Change in Net Position					768,245	459,198	1,227,443
Net Position, Beginning					32,571,512	16,186,966	48,758,478
Prior Period Adjustment (Note 11)					139,128	-	139,128
Net Position, Beginning, as Restated					32,710,640	16,186,966	48,897,606
Net Position, Ending					\$ 33,478,885	\$ 16,646,164	\$ 50,125,049

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

CITY OF STURGIS

**BALANCE SHEET - GOVERNMENTAL FUNDS
DECEMBER 31, 2012**

	General Fund	Capital Improvement Fund	Revolving Loan Fund	Other Governmental Funds	Total Governmental Funds
Assets					
101 Cash (Note 2)	\$ 5,415	\$ -	\$ -	\$ -	\$ 5,415
104 Interest Bearing Accounts (Note 2)	750,650	361,383	800,623	353,272	2,265,928
105 Savings Certificates (Note 2)	250,000	500,000	500,000	427,535	1,677,535
106 Restricted Cash with Fiscal Agent (Note 5)	-	625,765	-	-	625,765
108 Property Taxes Receivable	118,619	-	-	4,232	122,851
108 Sales Tax Receivable	145,943	145,943	-	21,435	313,321
115 Accounts Receivable	62,108	4,255	186	-	66,549
116 Estimated Uncollectible Accounts Receivable	(10,000)	-	-	-	(10,000)
121 Special Assessments Receivable	3,469	13,143	-	-	16,612
128 Notes Receivable (Note 10)	-	-	15,890	-	15,890
132 Due from Federal/State Government	33,488	-	-	-	33,488
142 Inventory of Supplies Purchased for Resale	1,485	-	-	-	1,485
151 Investment Held for Sale	-	-	-	608,100	608,100
154.1 Restricted Deposits	135,844	-	-	-	135,844
155 Prepaid Expense	21,472	-	-	-	21,472
Total Assets	\$ 1,518,493	\$ 1,650,489	\$ 1,316,699	\$ 1,414,574	\$ 5,900,255
Liabilities and Fund Balances					
<i>Liabilities</i>					
202 Accounts Payable	\$ 157,125	\$ 35,107	\$ 270	\$ -	\$ 192,502
216 Accrued Wages Payable	89,719	-	-	-	89,719
217 Accrued Taxes Payable	1,341	-	-	19	1,360
224 Deferred Revenue	68,601	13,143	-	-	81,744
236 Advance from Other Funds (Note 6)	10,000	-	-	-	10,000
Total Liabilities	326,786	48,250	270	19	375,325
<i>Fund Balances</i>					
263.01 Nonspendable - Inventory	1,485	-	-	-	1,485
263.02 Nonspendable - Prepaid Expenses	21,472	-	-	-	21,472
263.05 Nonspendable - Notes Receivable	-	-	15,890	-	15,890
263.49 Nonspendable - Investment Held for Sale	-	-	-	608,100	608,100
263.49 Nonspendable - SDPAA Reserve (Note 9)	135,844	-	-	-	135,844
263.51 Nonspendable - Perpetual Care Cemetery	-	-	-	50,000	50,000
263.99 Nonspendable - Library Trust	-	-	-	327,535	327,535
264.01 Restricted - Debt Service	-	625,765	-	27,415	653,180
264.03 Restricted - Perpetual Care Cemetery	-	-	-	106,351	106,351
264.04 Restricted - Special Sales Tax	-	-	-	63,257	63,257
264.05 Restricted - Library Purposes	-	-	-	219,297	219,297
264.97 Restricted - Revolving Loan	-	-	1,300,539	-	1,300,539
265.97 Committed - Brick Fund	79,291	-	-	-	79,291
265.97 Committed - Capital Improvements	-	976,474	-	-	976,474
266.01 Assigned - Subsequent Year's Budget	-	-	-	12,600	12,600
267 Unassigned	953,615	-	-	-	953,615
Total Fund Balances	1,191,707	1,602,239	1,316,429	1,414,555	5,524,930
Total Liabilities and Fund Balances	\$ 1,518,493	\$ 1,650,489	\$ 1,316,699	\$ 1,414,574	\$ 5,900,255

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 POSITION
DECEMBER 31, 2012**

Total Fund Balances - Governmental Funds \$ 5,524,930

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

Capital assets used in governmental activities are not current financial
resources and therefore are not reported in the funds. 33,635,090

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. (5,835,342)

Accrued interest on long-term debt is not due and payable in the current period
and therefore is not reported in the funds. (50,640)

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. 81,744

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. 123,103

Total Net Position - Governmental Funds **\$ 33,478,885**

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, 2012**

	<u>General Fund</u>	<u>Capital Improvement Fund</u>	<u>Revolving Loan Fund</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Revenue					
<i>Taxes:</i>					
311	General Property Taxes (Note 3)	\$ 2,679,965	\$ -	\$ -	\$ 2,786,875
313	General Sales and Use Taxes	1,367,726	1,367,727	-	3,014,350
315	Amusement Taxes	900	-	-	900
319	Penalties and Interest on Delinquent Taxes	20,512	-	-	20,512
320	Licenses and Permits	411,168	-	-	411,168
<i>Intergovernmental Revenue:</i>					
331	Federal Grants	20,698	271,635	-	292,333
334	State Grants	5,254	-	-	5,254
335.01	Bank Franchise Tax	9,427	-	-	9,427
335.03	Liquor Tax Reversion	41,014	-	-	41,014
335.04	Motor Vehicle Licenses	67,189	-	-	67,189
335.08	Local Government Highway and Bridge Fund	123,302	-	-	123,302
338.02	County Highway and Bridge Reserve Tax	5,855	-	-	5,855
338.04	Port of Entry	13,114	-	-	13,114
338.99	Other	2,816	-	-	2,816
<i>Charges for Goods and Services:</i>					
341	General Government	976,920	-	-	976,920
342	Public Safety	42,996	-	-	42,996
345	Health	1,101	-	-	1,101
346	Culture and Recreation	305,129	-	-	305,129
349	Other	55,961	-	-	55,961
<i>Fines and Forfeits:</i>					
351	Court Fines and Costs	5,719	-	-	5,719
<i>Miscellaneous Revenue:</i>					
361	Investment Earnings	1,353	15,843	6,817	40,140
362	Rentals	5,000	-	-	5,000
363	Special Assessments	1,172	13,470	-	14,642
367	Contributions and Donations from Private Sources	19,226	957	-	36,795
369	Other	2,092	-	3,781	5,873
Total Revenue		6,185,609	1,669,632	6,817	422,327
		8,284,385			

CITY OF STURGIS

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES (CONTINUED)
 GOVERNMENTAL FUNDS
 FOR THE YEAR ENDED DECEMBER 31, 2012

	<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	Legislative	198,141	-	-	198,141
414	Financial Administration	1,022,688	-	-	1,022,688
419	Other	1,055,550	13,992	-	1,069,542
<i>Public Safety:</i>					
421	Police	1,825,186	-	-	1,825,186
422	Fire	145,709	-	-	145,709
<i>Public Works:</i>					
431	Highway and Streets	564,683	-	-	564,683
435	Airport	45,521	14,904	-	60,425
437	Cemeteries	72,221	4,940	-	77,161
<i>Culture and Recreation:</i>					
451	Recreation	697,075	8,820	-	705,895
452	Parks	496,645	12,676	-	509,321
455	Library	339,225	-	13,952	353,177
456	Auditorium	23,946	5,614	-	29,560
460	Conservation and Development	912	-	1,366	253,323
470	Debt Service	-	618,140	-	150,001
485	Capital Outlay	22,989	1,151,928	-	1,174,917
Total Expenditures		6,510,491	1,831,014	1,366	414,998
Excess of Revenue Over (Under) Expenditures		(324,882)	(161,382)	5,451	7,329
Other Financing Sources (Uses)					
391.01	Transfers In (Note 7)	687,080	-	-	687,080
391.03	Sale of Municipal Property	38,923	-	-	38,923
391.04	Compensation for Loss or Damage to Capital Assets	17,425	-	-	17,425
391.05	Sale of Bonds	-	-	608,100	608,100
511	Transfers Out (Note 7)	(12,000)	-	-	(12,000)
Total Other Financing Sources		731,428	-	-	608,100
Net Change in Fund Balances		406,546	(161,382)	5,451	615,429
Fund Balance, December 31, 2011		785,161	1,624,493	1,310,978	799,126
Prior Period Adjustment (Note 11)		-	139,128	-	139,128
Fund Balance, December 31, 2011, as Restated		785,161	1,763,621	1,310,978	799,126
Fund Balance, December 31, 2012		\$ 1,191,707	\$ 1,602,239	\$ 1,316,429	\$ 1,414,555
		\$ 5,524,930			

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, 2012

Net Change in Fund Balances - Total Government Funds \$ 866,044

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 capital outlays exceeded depreciation in the current period.	154,251
Governmental funds reflect proceeds from capital asset sales, if any, while the Statement of Activities reports a loss on sale or disposal of capital assets.	(69,742)
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.	(124,135)
Repayment of bond principal, tax increment financing, and long-term debt are expenditures in the governmental funds, but the repayment reduces long-term liabilities in the Statement of Net Position.	535,607
Borrowings on long-term debt is an other financing source in the governmental funds, but increases long-term debt in the Statement of Net Position.	(608,100)
Debt issuance costs are deferred in the government wide statements and amortized over the term of the related debt.	(14,102)
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.	14,531
Governmental funds do not reflect the change in accrued leave, but the Statement of Activities reflects the change in accrued leave through expenditures.	13,891

Change in Net Position of Governmental Activities \$ **768,245**

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

CITY OF STURGIS

**STATEMENT OF NET POSITION
PROPRIETARY FUNDS
DECEMBER 31, 2012**

Assets	Liquor Fund	Water Fund	Wastewater Fund	Sanitation Fund	Ambulance Fund	Total Proprietary Funds
Current Assets						
101 Cash	\$ 3,900	\$ 561,527	\$ 144,134	\$ 156,807	\$ 537,309	\$ 1,403,677
107 Restricted Cash in Bank (Note 5)	8,196	-	-	-	-	8,196
115 Accounts Receivable, Net	21,485	102,301	85,758	60,331	147,976	417,851
128 Notes Receivable (Note 10)	-	-	37,500	-	-	37,500
131 Due from Liquor Fund (Note 6)	-	293,271	-	-	-	293,271
133 Advance to Other Fund (Note 6)	-	-	-	10,000	-	10,000
142 Inventory of Supplies Purchased for Resale	221,860	-	-	-	-	221,860
155 Prepaid Expenses	1,570	3,338	1,714	3,072	1,780	11,474
Total Current Assets	257,011	960,437	269,106	230,210	687,065	2,403,829
Capital Assets (Note 4)						
160 Land	6,500	1,800	646,214	84,167	-	738,681
162 Buildings	826,042	181,183	445,257	310,994	359,809	2,123,285
163 Accumulated Depreciation - Buildings	(50,063)	(49,909)	(147,649)	(61,531)	(60,568)	(369,720)
164 Improvements Other Than Buildings	-	10,139,737	10,186,861	22,789	-	20,349,387
165 Accumulated Depreciation - Improvements Other Than Buildings	-	(3,950,049)	(2,957,096)	(15,613)	-	(6,922,758)
166 Machinery and Equipment	46,433	731,302	694,834	2,149,810	486,262	4,108,641
167 Accumulated Depreciation - Machinery and Equipment	(24,623)	(518,665)	(511,684)	(1,604,177)	(278,087)	(2,937,236)
168 Construction Work in Progress	-	4,065,422	-	-	-	4,065,422
Total Capital Assets	804,289	10,600,821	8,356,737	886,439	507,416	21,155,702
Total Assets	\$ 1,061,300	\$ 11,561,258	\$ 8,625,843	\$ 1,116,649	\$ 1,194,481	\$ 23,559,531

Liabilities and Net Position	Liquor Fund	Water Fund	Wastewater Fund	Sanitation Fund	Ambulance Fund	Total Proprietary Funds
Current Liabilities						
202 Accounts Payable	\$ 111,593	\$ 472,847	\$ 4,537	\$ 20,081	\$ 9,287	\$ 618,345
208 Due to Water Fund (Note 6)	293,271	-	-	-	-	293,271
215 Accrued Interest Payable	15,608	14,060	4,136	-	-	33,804
216 Accrued Wages Payable	4,112	11,582	7,892	8,540	11,848	43,974
217 Accrued Taxes Payable	12,473	47	-	3,290	-	15,810
220 Customer Deposits	300	135,990	-	-	-	136,290
226 Bonds Payable - Current (Note 5)	9,239	84,374	278,757	-	-	372,370
233 Accrued Leave Payable (Note 5)	1,601	38,715	17,965	15,751	4,968	79,000
Total Current Liabilities	448,197	757,615	313,287	47,662	26,103	1,592,864
Long-Term Liabilities (Note 5)						
231 Bonds Payable	771,174	3,105,705	1,443,624	-	-	5,320,503
Total Liabilities	1,219,371	3,863,320	1,756,911	47,662	26,103	6,913,367
Net Position						
253.10 Net Investment in Capital Assets	23,876	7,410,742	6,634,356	886,439	507,416	15,462,829
253.21 Restricted for Revenue Bond Debt Service	8,196	-	-	-	-	8,196
253.9 Unrestricted (Deficit)	(190,143)	287,196	234,576	182,548	660,962	1,175,139
Total Net Position	(158,071)	7,697,938	6,868,932	1,068,987	1,168,378	16,646,164
Total Liabilities and Net Position	\$ 1,061,300	\$ 11,561,258	\$ 8,625,843	\$ 1,116,649	\$ 1,194,481	\$ 23,559,531

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

CITY OF STURGIS

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2012

	<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	\$ 2,134,435	\$ 1,613,195	\$ 964,936	\$ 1,010,785	\$ 846,632	\$ 6,569,983
Operating Expenses						
410 Personal Services	161,409	445,330	299,328	340,884	456,088	1,703,039
420 Other Current Expense	176,222	345,844	103,652	453,113	125,290	1,204,121
426.2 Materials (Cost of Goods Sold)	1,668,513	-	-	-	-	1,668,513
457 Depreciation	28,667	235,983	244,887	147,337	45,260	702,134
Total Operating Expenses	2,034,811	1,027,157	647,867	941,334	626,638	5,277,807
Operating Revenue	99,624	586,038	317,069	69,451	219,994	1,292,176
Nonoperating Revenue (Expense)						
330 State Operating Grants	-	-	-	18,243	-	18,243
361 Investment Earnings	12,181	1,835	656	190	1,148	16,010
369 Other	-	-	-	21,939	215	22,154
391 Donated Property	-	-	(87,427)	-	-	(87,427)
391.40 Compensation for Loss or Damage to Capital Assets	-	735	-	-	628	1,363
442 Interest Expense	(41,177)	(37,331)	(49,733)	-	-	(128,241)
Total Nonoperating Revenue (Expense)	(28,996)	(34,761)	(136,504)	40,372	1,991	(157,898)
Income before Transfers	70,628	551,277	180,565	109,823	221,985	1,134,278
391.1 Transfers In (Note 7)	-	-	-	12,000	-	12,000
511 Transfers Out (Note 7)	(207,080)	-	(300,000)	(180,000)	-	(687,080)
Total Transfers	(207,080)	-	(300,000)	(168,000)	-	(675,080)
Change in Net Position	(136,452)	551,277	(119,435)	(58,177)	221,985	459,198
Net Position (Deficit), December 31, 2011	(21,619)	7,146,661	6,988,367	1,127,164	946,393	16,186,966
Net Position (Deficit), December 31, 2012	\$ (158,071)	\$ 7,697,938	\$ 6,868,932	\$ 1,068,987	\$ 1,168,378	\$ 16,646,164

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, 2012**

	Liquor Fund	Water Fund	Wastewater Fund
Cash Flows from Operating Activities			
Receipts from Customers	\$ 2,140,795	\$ 1,600,779	\$ 960,229
Payments to Suppliers	(1,739,857)	(383,381)	(131,350)
Payments to Employees	(160,818)	(433,899)	(300,305)
Net Cash Flows Provided by Operating Activities	240,120	783,499	528,574
Cash Flows from Noncapital Financing Activities			
Transfers In	-	-	-
Transfers Out	(207,080)	-	(300,000)
Internal Activity - Receipts from (Payments to) Other Funds	(6,019)	6,019	-
Cash Receipts from Notes Receivable	-	-	12,500
Net Cash Flows Provided By (Used in) Noncapital Financing Activities	(213,099)	6,019	(287,500)
Cash Flows from Capital and Related Financing Activities			
Purchases of Capital Assets	-	(3,136,984)	(93,654)
State Operating Grants	-	-	-
Compensation for Loss or Damage to Capital Assets	-	735	-
Principal Paid on Debt	(9,388)	(82,684)	(273,961)
Borrowings on Long-Term Debt	-	2,243,554	-
Interest Paid	(31,592)	(23,271)	(50,064)
Other Receipts	-	-	-
Net Cash Flows Provided by (Used in) Capital and Related Financing Activities	(40,980)	(998,650)	(417,679)
Cash Flows Provided by Investing Activities			
Cash Received From Investment Earnings	12,181	1,835	656
Increase (Decrease) in Cash and Cash Equivalents	(1,778)	(207,297)	(175,949)
Cash and Cash Equivalents, January 1, 2012	13,874	768,824	320,083
Cash and Cash Equivalents, December 31, 2012	\$ 12,096	\$ 561,527	\$ 144,134
Reconciliation of Operating Income to Net Cash Provided by Operating Activities			
Operating Income	\$ 99,624	\$ 586,038	\$ 317,069
<i>Adjustments to Reconcile Operating Income to Net Cash Flows Provided by Operating Activities:</i>			
Depreciation Expense	28,667	235,983	244,887
Change in Assets and Liabilities:			
Accounts Receivable	6,510	(17,246)	(4,707)
Inventory of Supplies Purchased for Resale	13,950	-	-
Prepaid Expenses	344	(570)	401
Accounts Payable	90,505	(36,968)	(28,099)
Accrued Wages Payable	585	2,290	552
Accrued Taxes Payable	79	1	-
Customer Deposits	(150)	4,830	-
Accrued Leave Payable	6	9,141	(1,529)
Net Cash Flows Provided by Operating Activities	\$ 240,120	\$ 783,499	\$ 528,574
Noncash Capital and Related Financing Activities			
Donated Property	-	-	87,427
Purchase of Capital Assets Included in Accounts Payable	-	453,172	-

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

Sanitation Fund	Ambulance Fund	Total Proprietary Funds
\$ 1,021,417	\$ 714,580	\$ 6,437,800
(486,256)	(120,093)	(2,860,937)
(341,780)	(449,693)	(1,686,495)
<u>193,381</u>	<u>144,794</u>	<u>1,890,368</u>
12,000	-	12,000
(180,000)	-	(687,080)
25,000	-	25,000
-	-	12,500
<u>(143,000)</u>	<u>-</u>	<u>(637,580)</u>
(41,724)	-	(3,272,362)
18,243	-	18,243
-	628	1,363
-	-	(366,033)
-	-	2,243,554
-	-	(104,927)
<u>21,939</u>	<u>215</u>	<u>22,154</u>
<u>(1,542)</u>	<u>843</u>	<u>(1,458,008)</u>
190	1,148	16,010
<u>49,029</u>	<u>146,785</u>	<u>(189,210)</u>
<u>107,778</u>	<u>390,524</u>	<u>1,601,083</u>
<u>\$ 156,807</u>	<u>\$ 537,309</u>	<u>\$ 1,411,873</u>
\$ 69,451	\$ 219,994	\$ 1,292,176
147,337	45,260	702,134
10,632	(132,052)	(136,863)
-	-	13,950
53	1,646	1,874
(33,263)	3,551	(4,274)
204	1,427	5,058
67	-	147
-	-	4,680
<u>(1,100)</u>	<u>4,968</u>	<u>11,486</u>
<u>\$ 193,381</u>	<u>\$ 144,794</u>	<u>\$ 1,890,368</u>
-	-	87,427
-	-	453,172

CITY OF STURGIS

**STATEMENT OF FIDUCIARY NET POSITION
DECEMBER 31, 2012**

	Agency Fund
Assets	
Interest Bearing Accounts	\$ 5,831
Total Assets	\$ 5,831
Liabilities	
Amounts Held for Others	\$ 5,831
Total Liabilities	\$ 5,831

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

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2012

(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 Position 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, 2012

(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 – From January 1, 2012 through April 3, 2012, 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. Effective April 4, 2012, Title 20 was amended through Ordinance 2012-01, changing the applicable percentage to 40 percent. 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 businesses 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.

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2012

(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.

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 Position 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, 2012

(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 Position 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, 2012 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, 2012**

(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 Position and on each proprietary fund's Statement of Net Position/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-----
Buildings	\$ 15,000	Straight-line	10-50 years
Improvements Other Than 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, 2012

(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, contract payable, 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, 2012

(1) Summary of Significant Accounting Policies (Continued)

j. Equity Classifications

Government-wide Financial Statements:

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

1. Net investment in capital assets – 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 position – Consists of net position 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 position – All other net position that do not meet the definition of restricted or net investment in capital assets.

Fund Financial Statements:

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 two Committed Fund Balances for the year ended December 31, 2012. The Brick Fund and Capital Improvements funds were created through ordinances passed by the City Council, the highest decision making authority. The City Council would have to pass ordinances to remove the commitments.

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. The subsequent year's budget assignment was established by the City Council when it passed the 2013 Appropriations Ordinance for the City's 2013 budget.

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. The City does not have a formal minimum fund balance policy.

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 position, prior to the use of unrestricted net position, when an expense is incurred for purposes for which both restricted and unrestricted net position are available.

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2012

(1) Summary of Significant Accounting Policies (Concluded)

k. Inventory of Supplies Purchased for Resale

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 rate.

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 rate.

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.

n. Emerging Accounting Standard

During 2012, the Governmental Accounting Standards Board issued statement No. 65, "Items Previously Reported as Assets and Liabilities," which will improve financial reporting by clarifying the appropriate use of the financial statement elements deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting. The standard will be implemented for the year ending December 31, 2013 and will require expensing debt issuance costs previously reported as deferred charges on the Statement of Net Position.

(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.

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED) DECEMBER 31, 2012

(2) Deposits and Investments (Continued)

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.

As of December 31, 2012, the City's cash and investments consisted of checking, savings, money market accounts, South Dakota Public Investment Trust (SDFIT), and certificates of deposit. All of these accounts are insured or collateralized in the City's name.

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. The money market accounts are unrated.

SDFIT is an external investment pool created for South Dakota local government investing. It is regulated by a nine member board with representation from municipalities, school districts and counties. The net asset value of the SDFIT money market account (GCR) is kept at one dollar per share by adjusting the rate of return on a daily basis. Earnings are credited to each account on a monthly basis.

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, 2012, 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. More than five percent of the City's certificates of deposit are in: American Express (15 percent), First Premier Bank (16 percent), GE Capital (15 percent), American Express (18 percent), and Goldman Sachs (36 percent).

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2012**

(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.

(4) Changes in Capital Assets

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

	Balance 12/31/2011	Additions	Transfers/ Deletions	Balance 12/31/2012
<i>Governmental Activities:</i>				
Capital Assets, not being Depreciated:				
Land	\$ 2,184,497	\$ -	\$ -	\$ 2,184,497
Construction Work in Progress	106,575	11,250	106,575	11,250
Total Capital Assets, not being Depreciated	2,291,072	11,250	106,575	2,195,747
Capital Assets, being Depreciated:				
Buildings	12,444,713	-	-	12,444,713
Improvements Other Than Buildings	26,372,877	918,960	-	27,291,837
Machinery and Equipment	3,600,014	351,282	176,051	3,775,245
Total Capital Assets, being Depreciated	42,417,604	1,270,242	176,051	43,511,795
Less Accumulated Depreciation for:				
Buildings	3,301,950	269,089	-	3,571,039
Improvements Other Than Buildings	5,765,378	580,801	-	6,346,179
Machinery and Equipment	2,090,767	170,776	106,309	2,155,234
Total Accumulated Depreciation	11,158,095	1,020,666	106,309	12,072,452
Total Governmental Activities Capital Assets, being Depreciated, Net	31,259,509	249,576	69,742	31,439,343
Total Governmental Capital Assets, Net	\$ 33,550,581	\$ 260,826	\$ 176,317	\$ 33,635,090

Depreciation expense was charged to functions as follows:

Public Works	\$ 480,998
Culture and Recreation	230,270
General Government	209,313
Public Safety	100,085
Total Depreciation Expense - Governmental	\$ 1,020,666

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2012**

(4) Changes in Capital Assets (Continued)

	Balance 12/31/2011	Additions	Deletions	Balance 12/31/2012
<i>Business-Type Activities:</i>				
Capital Assets, not being Depreciated:				
Land	\$ 826,108	\$ -	\$ 87,427	\$ 738,681
Construction Work in Progress	602,476	3,462,946	-	4,065,422
Total Capital Assets, not being Depreciated	1,428,584	3,462,946	87,427	4,804,103
Capital Assets, being Depreciated:				
Buildings	2,123,285	-	-	2,123,285
Improvements Other Than Buildings	20,292,462	56,925	-	20,349,387
Machinery and Equipment	3,902,978	205,663	-	4,108,641
Total Capital Assets, being Depreciated	26,318,725	262,588	-	26,581,313
Less Accumulated Depreciation for:				
Buildings	309,086	60,634	-	369,720
Improvements Other Than Buildings	6,511,701	411,057	-	6,922,758
Machinery and Equipment	2,706,793	230,443	-	2,937,236
Total Accumulated Depreciation	9,527,580	702,134	-	10,229,714
Total Business-Type Activities Capital Assets, being Depreciated, Net	16,791,145	(439,546)	-	16,351,599
Total Business-Type Capital Assets, Net	\$ 18,219,729	\$ 3,023,400	\$ 87,427	\$ 21,155,702

Depreciation expense was charged to functions as follows:

Ambulance	\$ 45,260
Wastewater	244,887
Water	235,983
Sanitary	147,337
Liquor	28,667
Total Depreciation Expense - Business-Type	\$ 702,134

Construction Commitments

As of December 31, 2012, there are approximately \$1,040,840 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 is expected in 2013.

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2012**

(5) Long-Term Debt

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

	Balance 12/31/2011	Additions	Deletions	Balance 12/31/2012	Due Within One Year
Primary Government:					
Governmental Activities:					
Revenue Bonds	\$ 5,175,000	\$ -	\$ 445,000	\$ 4,730,000	\$ 455,000
Tax Increment Financing Obligations	406,001	-	29,797	376,204	83,551
Marcotte Property	-	608,100	60,810	547,290	182,430
Compensated Absences	195,739	147,110	161,001	181,848	181,848
Total Governmental Activities	5,776,740	755,210	696,608	5,835,342	902,829
Business-Type Activities:					
2010 GO Crossover Refunding Bonds	1,920,000	-	295,000	1,625,000	300,000
2010 Sales Tax Revenue Bond	789,801	-	9,388	780,413	9,239
2009 Drinking Water Revenue Bond	510,632	-	50,234	460,398	51,374
2009 Clean Water Revenue Bond	287,542	-	11,411	276,131	11,757
2011 Drinking Water Revenue Bond	307,377	1,352,726	-	1,660,103	-
2012 Drinking Water Revenue Bond	-	890,828	-	890,828	-
Compensated Absences	67,514	333,653	322,167	79,000	79,000
Total Business-Type Activities	3,882,866	2,577,207	688,200	5,771,873	451,370
Total Primary Government	\$ 9,659,606	\$ 3,332,417	\$ 1,384,808	\$ 11,607,215	\$1,354,199

The City has bond reserves of \$625,765 and \$8,196 at December 31, 2012, in accordance with debt covenants.

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	\$ 105,955	\$ 324,025
Pledged Revenue	1,613,195	964,936

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2012**

(5) Long-Term Debt (Continued)

Debt payable at December 31, 2012, 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. \$ 1,625,000

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. 4,730,000

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. 780,413

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. 460,398

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. 276,131

Drinking Water Revenue Borrower Bond, 2011 Series, with a maximum borrowing of \$3,460,000. As of December 31, 2012, advances totaled \$1,660,103. Interest-only payments at 2.00 percent totaling \$69,200 will be made 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. 1,660,103

Borrower Bond, Series 2012, with a maximum borrowing of \$2,200,000. As of December 31, 2012, advances totaled \$890,828. Payments begin in October 2014 through July 2034, with interest at a fixed 3.00 percent. Water revenues pledged and financed through the Water Fund. 890,828

Contract Payable

Note payable to Game Fish and Parks for purchase of real property totaling \$608,100, matures July 2015, non-interest bearing, first installment due in 2012 totaling \$60,810, with three subsequent equal installments totaling \$182,430 due in 2013-2015. Financed through the Special Sales Tax Fund. 547,290

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. 376,204

Total Bonds, Contract Payable, and TIF Obligations 11,346,367

CITY OF STURGIS

NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2012

(5) Long-Term Debt (Continued)

Compensated Absences:

General Fund	181,848
Liquor Fund	1,601
Water Fund	38,715
Wastewater Fund	17,965
Sanitation Fund	15,751
Ambulance Fund	4,968
Total Compensated Absences	260,848
<hr/>	
Total Long-Term Debt	\$ 11,607,215

The annual requirements to amortize long-term debt outstanding as of December 31, 2012, except for compensated absences are as follows:

	General Obligation		Revenue Bonds		TIF Obligations	
	Interest	Principal	Interest	Principal	Interest	Principal
2013	\$ 40,403	\$ 300,000	\$ 277,248	\$ 527,370	\$ 27,124	\$ 83,551
2014	34,352	310,000	369,612	3,095,202	23,052	87,622
2015	28,184	240,000	174,938	561,221	15,446	95,228
2016	22,991	175,000	156,430	578,227	7,180	103,495
2017	18,337	165,000	93,886	600,288	268	6,308
2018-2022	27,953	435,000	376,232	2,625,327	-	-
2023-2027	-	-	145,509	158,939	-	-
2028-2032	-	-	116,482	148,146	-	-
2033-2037	-	-	93,498	111,392	-	-
2038-2042	-	-	68,891	136,009	-	-
2043-2047	-	-	38,833	166,067	-	-
2048-2050	-	-	6,166	89,685	-	-
Total	\$ 172,220	\$ 1,625,000	\$ 1,917,725	\$ 8,797,873	\$ 73,070	\$ 376,204

Contract Payable	Total	
	Principal	Interest
\$ 182,430	\$ 344,775	\$ 1,093,351
182,430	427,016	3,675,254
182,430	218,568	1,078,879
-	186,601	856,722
-	112,491	771,596
-	404,185	3,060,327
-	145,509	158,939
-	116,482	148,146
-	93,498	111,392
-	68,891	136,009
-	38,833	166,067
-	6,166	89,685
\$ 547,290	\$ 2,163,015	\$ 11,346,367

CITY OF STURGIS

**NOTES TO FINANCIAL STATEMENTS (CONTINUED)
DECEMBER 31, 2012**

(5) Long-Term Debt (Concluded)

Tax Increment Financing Obligations

Tax increment financing is a method of financing improvements and development in an area which has been determined to be blighted according to the criteria set forth in SDCL 11-9. In some instances, the City pledges future tax revenues generated by the tax increment district to acquire public improvements within the established Tax Increment District which were constructed by a private developer.

It is a specific condition of the developer’s agreement and a condition of the City’s obligation that all sums payable shall be limited to the proceeds of the positive tax increment. It is also specifically agreed that the City has made no representation that the proceeds from such funds shall be sufficient to retire the indebtedness incurred by the developer to construct the public improvements.

During the year ended December 31, 2012, property tax revenues were \$89,191 for TIF #9. Interest expenditures, excluding corresponding accruals, related to TIF obligations totaled \$59,394 for the year ended December 31, 2012.

Special Assessment Issue

The City was acting as a fiscal agent for the 2002 special assessment issue with a balance of \$53,926 as of December 31, 2012. The City is not liable directly or indirectly for the special assessment.

(6) Individual Fund Interfund Receivable and Payable Balances

Interfund receivable and payable balances at December 31, 2012, are as follows:

Fund	Interfund Receivables	Interfund Payables
<i>Major Funds:</i>		
General Fund	\$ -	\$ 10,000
Sanitation Fund	10,000	-
Liquor Fund	-	293,271
Water Fund	293,271	-
Total Interfund Receivable and Payable Balances	\$ 303,271	\$ 303,271

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, 2012**

(7) Interfund Transfers

	Transfers In	Transfers Out
<i>Major Funds:</i>		
General Fund	\$ 687,080	\$ 12,000
Liquor Fund	-	207,080
Wastewater Fund	-	300,000
Sanitation Fund	12,000	180,000
Total Transfers	\$ 699,080	\$ 699,080

Transfers between the funds were made to cover general operational costs of the City.

(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, 2012, 2011, and 2010, were **\$244,509**, \$242,673, and \$232,082, 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, 2012, 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, 2012

(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, 2012, 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, 2012**

(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, 2012:

Governmental:

<u>Loan</u>	<u>Collateral</u>	<u>Rate</u>	<u>Maturity</u>	<u>Balance</u>
Western Door Company	Equipment	3%	September 2012	15,890

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	\$ 37,500

(11) Prior Period Adjustment

A receivable was not recorded at December 31, 2011 for revenue totaling \$139,128 pertaining to 2011 expenditures for the airport improvement grant. The error resulted in an understatement of revenue and net position in the Capital Improvement Fund for 2011.

REQUIRED SUPPLEMENTARY INFORMATION

CITY OF STURGIS

**BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2012**

Revenue	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual - Budgetary Basis</u>	<u>Variance</u>
<i>Taxes:</i>				
311 General Property Taxes	\$ 2,741,997	\$ 2,741,997	\$ 2,679,965	\$ (62,032)
313 General Sales and Use Taxes	1,421,833	1,421,833	1,367,726	(54,107)
315 Amusement Taxes	-	-	900	900
319 Penalties and Interest on Delinquent Taxes	-	-	20,512	20,512
320 Licenses and Permits	375,877	375,877	411,168	35,291
<i>Intergovernmental Revenue:</i>				
331 Federal Grants	15,000	15,000	20,698	5,698
334 State Grants	-	25,952	5,254	(20,698)
335 Bank Franchise Tax	9,862	9,862	9,427	(435)
335 Liquor Tax Reversion	36,410	36,410	41,014	4,604
335 Motor Vehicle Licenses	50,142	50,142	67,189	17,047
335.1 Local Government Highway and Bridge Fund	89,004	89,004	123,302	34,298
336 State Payment in Lieu of Taxes	3,000	3,000	-	(3,000)
338 County Highway and Bridge Reserve Tax (25%)	5,855	5,855	5,855	-
338 Port of Entry	12,190	12,190	13,114	924
339 County Payments in Lieu of Taxes	8,000	8,000	2,816	(5,184)
<i>Charges for Goods and Services:</i>				
341 General Government	1,069,987	1,069,987	976,920	(93,067)
342 Public Safety	38,697	38,697	42,996	4,299
343 Highways and Streets	1,991	1,991	-	(1,991)
345 Health	1,093	1,093	1,101	8
346 Culture and Recreation	311,174	311,174	305,129	(6,045)
349 Other	-	-	55,961	55,961
<i>Fines and Forfeits:</i>				
351 Court Fines and Costs	3,494	3,494	5,719	2,225
<i>Miscellaneous Revenue:</i>				
361 Investment Earnings	2,233	2,233	1,353	(880)
362 Airport Hangar Lease	3,579	3,579	5,000	1,421
363 Special Assessments	5,965	5,965	1,172	(4,793)
367 Contributions and Donations - Private Sources	11,022	11,022	19,226	8,204
369 Other	1,553	149,553	2,092	(147,461)
Total Revenue	6,219,958	6,393,910	6,185,609	(208,301)

CITY OF STURGIS

**BUDGETARY COMPARISON SCHEDULE - BUDGETARY BASIS (CONTINUED)
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2012**

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual - Budgetary Basis</u>	<u>Variance</u>
Expenditures				
<i>General Government:</i>				
411 Legislative	298,413	250,937	198,141	52,796
414 Financial Administration	1,071,624	1,071,624	1,022,688	48,936
419 Other	1,210,511	1,357,599	1,078,539	279,060
<i>Public Safety:</i>				
421 Police	1,831,869	1,907,141	1,825,186	81,955
422 Fire	178,591	178,591	145,709	32,882
<i>Public Works:</i>				
431 Highway and Streets	635,759	647,369	564,683	82,686
435 Airport	44,991	47,315	45,521	1,794
437 Cemeteries	92,447	92,447	72,221	20,226
<i>Culture and Recreation:</i>				
451 Recreation	793,120	805,121	697,075	108,046
452 Parks	639,396	639,396	496,645	142,751
455 Library	359,841	360,607	339,225	21,382
456 Auditorium	35,568	35,568	23,946	11,622
460 Conservation and Development	-	912	912	-
Total Expenditures	7,192,130	7,394,627	6,510,491	884,136
Excess of Revenue Under Expenditures	(972,172)	(1,000,717)	(324,882)	675,835
Other Financing Sources (Uses)				
391.01 Transfers In	687,080	687,080	687,080	-
391.03 Sale of Municipal Property	-	-	38,923	38,923
391.04 Compensation for Loss or Damage to Capital Assets	-	16,944	17,425	481
511 Transfers Out	(12,000)	(12,400)	(12,000)	400
Total Other Financing Sources	675,080	691,624	731,428	39,804
Net Change in Fund Balance	(297,092)	(309,093)	406,546	715,639
	785,161	785,161	785,161	-
Fund Balance, December 31, 2012	\$ 488,069	\$ 476,068	\$ 1,191,707	\$ 715,639

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, 2012

	<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	\$ 1,421,836	\$ 1,421,836	\$ 1,367,727	\$ (54,109)
<i>Intergovernmental Revenue:</i>				
331 Federal Grants	-	-	271,635	271,635
<i>Miscellaneous Revenue:</i>				
361 Earnings on Deposits	15,255	15,255	15,843	588
363 Special Assessments	15,000	15,000	13,470	(1,530)
367 Contributions and Donations	-	-	957	957
Total Revenue	1,452,091	1,452,091	1,669,632	217,541
Expenditures				
<i>General Government:</i>				
419 Other	214,000	214,000	53,310	160,690
<i>Public Works:</i>				
431 Highway and Streets	230,000	530,000	467,007	62,993
435 Airport	-	325,000	302,343	22,657
437 Cemetery	40,500	40,500	4,940	35,560
<i>Culture and Recreation:</i>				
451 Recreation	53,801	253,801	302,261	(48,460)
452 Parks	288,000	288,000	77,399	210,601
456 Auditorium	8,000	8,000	5,614	2,386
470 Debt Service	617,790	618,140	618,140	-
Total Expenditures	1,452,091	2,277,441	1,831,014	446,427
Excess of Revenue Over (Under) Expenditures	-	(825,350)	(161,382)	663,968
Other Financing Sources				
391.1 Transfers In	-	350	-	(350)
Net Change in Fund Balance	-	(825,000)	(161,382)	663,618
Fund Balance, December 31, 2011	1,624,493	1,624,493	1,624,493	-
Prior Period Adjustment (Note 11)	139,128	139,128	139,128	-
Fund Balance, December 31, 2011 as Restated	1,763,621	1,763,621	1,763,621	-
Fund Balance, December 31, 2012	\$ 1,763,621	\$ 938,621	\$ 1,602,239	\$ 663,618

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, 2012**

	<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	\$ 13,000	\$ 13,000	\$ 6,817	\$ (6,183)
363 Special Assessments	6,500	6,500	-	(6,500)
Total Revenue	19,500	19,500	6,817	(12,683)
Expenditures				
460 Conservation and Development	19,500	19,500	1,366	18,134
Net Change in Fund Balance	-	-	5,451	5,451
Fund Balance, December 31, 2011	1,310,978	1,310,978	1,310,978	-
Fund Balance, December 31, 2012	\$ 1,310,978	\$ 1,310,978	\$ 1,316,429	\$ 5,451

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

CITY OF STURGIS

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION DECEMBER 31, 2012

(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, 2012.
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, 2012

	Special Sales Tax Fund	Library Fund	TIF Funds	Alice W. Dunn Fund	Perpetual Maintenance Fund	Total Nonmajor Governmental Funds
Assets						
104 Interest Bearing Accounts	\$ 41,822	\$ 73,002	\$ 23,183	\$ 58,895	\$ 156,370	\$ 353,272
105 Savings Certificates	-	-	-	427,535	-	427,535
108 Property Taxes Receivable	-	-	4,232	-	-	4,232
108 Sales Tax Receivable	21,435	-	-	-	-	21,435
151 Investment Held for Sale	608,100	-	-	-	-	608,100
Total Assets	\$ 671,357	\$ 73,002	\$ 27,415	\$ 486,430	\$ 156,370	\$ 1,414,574
Liabilities and Fund Balances						
<i>Liabilities</i>						
217 Accrued Taxes Payable	-	-	-	-	19	19
<i>Fund Balances</i>						
263.49 Nonspendable - Investment Held for Sale	608,100	-	-	-	-	608,100
263.51 Nonspendable - Perpetual Care Cemetery	-	-	-	-	50,000	50,000
263.99 Nonspendable - Library Trust	-	-	-	327,535	-	327,535
264.01 Restricted - Debt Service	-	-	27,415	-	-	27,415
264.03 Restricted - Perpetual Care Cemetery	-	-	-	-	106,351	106,351
264.04 Restricted - BID Tax	63,257	-	-	-	-	63,257
264.05 Restricted - Library Purposes	-	60,402	-	158,895	-	219,297
266.01 Assigned - Subsequent Year's Budget	-	12,600	-	-	-	12,600
Total Fund Balances	671,357	73,002	27,415	486,430	156,351	1,414,555
Total Liabilities and Fund Balances	\$ 671,357	\$ 73,002	\$ 27,415	\$ 486,430	\$ 156,370	\$ 1,414,574

CITY OF STURGIS

**COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
NONMAJOR GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2012**

	Special Sales Tax Fund	Library Fund	TIF Funds	Alice W. Dunn Fund	Perpetual Maintenance Fund	Total Nonmajor Governmental Funds
Revenue:						
311 General Property Taxes	\$ -	\$ -	\$ 106,910	\$ -	\$ -	\$ 106,910
313 General Sales and Use Taxes	278,897	-	-	-	-	278,897
361 Investment Earnings	134	169	-	15,824	-	16,127
367 Contributions and Donations - Private Sources	-	16,612	-	-	-	16,612
369 Other	-	-	-	-	3,781	3,781
Total Revenue	279,031	16,781	106,910	15,824	3,781	422,327
Expenditures:						
455 Library	-	13,952	-	-	-	13,952
460 Conservation and Development	251,045	-	-	-	-	251,045
470 Debt Service	60,810	-	89,191	-	-	150,001
Total Expenditures	311,855	13,952	89,191	-	-	414,998
Excess of Revenue Over (Under)						
Expenditures	(32,824)	2,829	17,719	15,824	3,781	7,329
Other Financing Sources						
391.5 Sale of Bonds	608,100	-	-	-	-	608,100
Net Change in Fund Balances	575,276	2,829	17,719	15,824	3,781	615,429
Fund Balance, December 31, 2011	96,081	70,173	9,696	470,606	152,570	799,126
Fund Balance, December 31, 2012	\$ 671,357	\$ 73,002	\$ 27,415	\$ 486,430	\$ 156,351	\$ 1,414,555

CITY OF STURGIS

**SCHEDULE OF RALLY ACTIVITIES (UNAUDITED)
FOR THE YEAR ENDED DECEMBER 31, 2012**

Revenue

Taxes:

320 Licenses and Permits \$ 262,875

Charges for Goods and Services:

341 General Government 969,199

346 Culture & Recreation 22,917

344 Special Sanitation Fee 160,116

Total Revenue **1,415,107**

Expenditures

General Government:

419 Other 1,005,731

Public Works:

429 Sanitation 24,557

Total Expenditures **1,030,288**

Excess of Revenue over Expenditures **\$ 384,819**

SINGLE AUDIT SECTION

CITY OF STURGIS

**SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED DECEMBER 31, 2012**

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 #11-1 will be repeated as Finding #12-1 for the year ending December 31, 2012.

The City continues to improve on recording year-end adjustments; however as significant audit adjustments were necessary, Finding #11-2 will be repeated as Finding #12-2 for the year ending December 31, 2012.

Administration is aware that the budgeting process needs to be more diligent in completing supplemental appropriations, when necessary. Finding #11-3 will be repeated as Finding #12-3 for the year ending December 31, 2012.

The City properly established a debt reserve account during the year ended December 31, 2012. Therefore, Finding #11-4 will not be repeated for the year ended December 31, 2012.

The City provided subsidiary ledgers that agreed to the general ledger for the year ended December 31, 2012. Therefore, Finding #11-5 will not be repeated for the year ended December 31, 2012.

CITY OF STURGIS

SCHEDULE OF FINDINGS AND QUESTIONED COSTS FOR THE YEAR ENDED DECEMBER 31, 2012

A. SUMMARY OF AUDIT RESULTS

1. The auditor's report expresses an unmodified 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 and 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 for Each Major Federal 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 unmodified 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

12-1 FINDING: Financial Statement Preparation

Condition and 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 SEFA that could have been prevented or detected by the City's management.

Recommendation: As in prior years, we have instructed management to review a draft of the auditor prepared financials and SEFA 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, 2012**

B. FINDINGS – FINANCIAL STATEMENT AUDIT (CONTINUED)

MATERIAL WEAKNESSES (CONTINUED)

12-1 FINDING: Financial Statement Preparation (Continued)

Response and 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.

12-2 FINDING: Audit Adjustments

Condition and Cause: During the course of our engagement, we proposed material audit adjustments. Adjustments included adjusting investments held for sale and, correspondingly, capital assets and accounts receivable. Additionally, we posted several reclassification entries with no effect on net income. Furthermore, 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.

Recommendation: We recommend that management consider the following:

- a. All assets purchased with the intent to sell them in the future should be recorded as investments held for sale, rather than capital assets.
- b. Any monies that will be received in the future as a result of overpayment of health insurance should be recorded as accounts receivable as of year-end.

Response and Corrective Action Plan: The City will make every effort to make accurate accounting adjustments throughout the year. When recording a journal entry that is unfamiliar, the Finance Officer will inquire on how to make the correct entry. The Finance Officer will make every effort to make sure all accounts receivable are properly recorded.

SIGNIFICANT DEFICIENCIES

12-3 FINDING: Budgetary Overdraft

Condition and 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	Culture and Recreation	\$ 48,460

CITY OF STURGIS

SCHEDULE OF FINDINGS AND QUESTIONED COSTS (CONCLUDED) FOR THE YEAR ENDED DECEMBER 31, 2012

B. FINDINGS – FINANCIAL STATEMENT AUDIT (CONTINUED)

SIGNIFICANT DEFICIENCIES (CONTINUED)

12-3 FINDING: Budgetary Overdraft (Continued)

Criteria and Effect: The City did not follow state law, which could result in additional inquiries from state officials regarding such violations.

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

Response and 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.

12-4 FINDING: Inventory

Condition and Cause: During the physical inventory count, the City had issues with the scanners uploading the inventory count accurately into the software which caused errors within the inventory listing involving negative amounts and duplications. Additionally, there is an overall lack of segregation of duties involving the Liquor Store Manager's ability to order inventory, receive inventory, adjust inventory costs, and perform inventory counts.

Criteria and Effect: Employees performing the count should be very detail-oriented and specific, in order to count each item correctly. This includes testing the items counted to ensure they are accurately uploaded in the system. This could cause misstatements to the financial statements if counts are performed incorrectly. Additionally, a lack of segregation of duties could lead to misstatements to the financial statements, and misappropriation of liquor inventory.

Recommendation: We recommend that the liquor store management use greater precaution when performing the inventory count. We recommend the scanners be tested prior to the inventory count to ensure the software is working properly. Additionally, individuals other than the Liquor Store Manager should be receiving inventory and performing inventory counts. A separate individual should review cost adjustments for reasonableness.

Response and Corrective Action Plan: The City had made arrangements with the software/hardware providers to be at all inventories at the liquor store. The City will continue to perform quarterly inventories, as well as spot-counts throughout the year. The City will look at other options for segregations of duties when receiving inventory. A separate individual will be named who will oversee the cost adjustments made to the inventory list. The Finance Officer is responsible for the correction of this finding.

C. FINDINGS – COMPLIANCE AUDIT

MATERIAL WEAKNESS

Finding #12-1 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, 2012**

	CFDA Number	Amount
<i>U.S. Department of Transportation:</i>		
Pass-Through the S.D. Department of Transportation		
Airport Improvement Program	20.106	\$ 271,635
Pass-Through the S.D. Department of Highway Safety		
Highway Safety Grant for Cameras & Radar	20.601	15,792
Total U.S. Department of Transportation		287,427
 <i>U.S. Department of Treasury Direct Program:</i>		
Joint Intelligence Room Computer System	21.XXX	4,906
 <i>U.S. Department of Agriculture Direct Program:</i>		
Water and Waste Disposal Systems for Rural Communities	10.760	1,818,473
 <i>National Endowment for the Arts Direct Program:</i>		
Promotion of the Arts Partnership Agreements	45.025	530
 <i>U.S. General Services Administration:</i>		
Pass-Through the S.D. Federal Property Agency		
Donation of Surplus Personal Property	39.003	12,705
Total		\$ 2,124,041

Note 1: 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, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of **CITY OF STURGIS** (the City) as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated August 13, 2013.

Internal Control over Financial Reporting

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

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified certain deficiencies in internal control that we consider to be material weaknesses and 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 a 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 #12-1 and #12-2 to be material weaknesses.

City Council

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 #12-3 and #12-4 to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed one instance of noncompliance or other matters that is required to be reported under *Government Auditing Standards* and which is described in the accompanying Schedule of Findings and Questioned Costs as #12-3.

City's Response to Findings

The City's response to the findings identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. The City's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the response.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the City's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. However, as required by South Dakota Codified Law 4-11-11, this report is a matter of public record and its distribution is not limited.



KETEL THORSTENSON, LLP
Certified Public Accountants

August 13, 2013



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 FOR EACH MAJOR FEDERAL PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE AS REQUIRED BY OMB CIRCULAR A-133

City Council
City of Sturgis
Sturgis, South Dakota

Report on Compliance for Each Major Federal Program

We have audited the compliance of **CITY OF STURGIS** (the City) with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the City's major federal programs for the year ended December 31, 2012. The City's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the City's major federal programs based on our audit of the types of compliance requirements referred to above. 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 on compliance for each major federal program. However, our audit does not provide a legal determination on the City's compliance.

Opinion on Each Major Federal Program

In our opinion, the City complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2012.

Report on Internal Control over Compliance

Management of the City is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the City's internal control over compliance with the types of requirements that could have a direct and material effect on a major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program 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 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 material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses.

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 a 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 #12-1 to be a material weakness.

The City's response to the internal control over compliance findings identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. The City's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose. However, as required by South Dakota Codified Law 4-11-11, this report is a matter of public record and its distribution is not limited.



KETEL THORSTENSON, LLP
Certified Public Accountants

August 13, 2013