

**CITY OF SHELLY
SHELLY, MINNESOTA**

AUDITED FINANCIAL STATEMENTS

FOR THE YEAR ENDED DECEMBER 31, 2020

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CITY OF SHELLY, MINNESOTA
OFFICIAL DIRECTORY
DECEMBER 31, 2020

Ronald Cakebread	Mayor
George Swenson	Councilperson
Lance Gilbertson	Councilperson
Todd Siemieniewski	Councilperson
Todd Swalstad	Councilperson
Mark Dohman	Clerk/Treasurer

INDEPENDENT AUDITOR'S REPORT

Honorable Mayor and City Council
City of Shelly
Shelly, Minnesota

Report on the Financial Statements

We have audited the accompanying cash basis financial statements of the governmental activities, business-type activities and each major fund of the City of Shelly, Minnesota, as of and for the year ended December 31, 2020, 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 the cash basis of accounting described in Note 1; this includes determining that the cash basis of accounting is an acceptable basis for the preparation of the financial statements in the circumstances. Management is also responsible for 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 cash basis financial position of the governmental activities, the business-type activities and each major fund of the City of Shelly, Minnesota, as of December 31, 2020, and the respective changes in cash basis financial position and, where applicable, cash flows thereof for the year then ended in accordance with the cash basis of accounting described in Note 1.

Basis of Accounting

We draw attention to Note 1 of the financial statements, which describes the basis of accounting. The financial statements are prepared on the cash basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinions are not modified with respect to this matter.

Other Matters

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Shelly, Minnesota's basic financial statements. The supplementary information on pages 19–25 is presented for purposes of additional analysis and are not a required part of the basic financial statements.

Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated May 5, 2021 on our consideration of the City of Shelly, Minnesota's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the City of Shelly, Minnesota's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City of Shelly, Minnesota's internal control over financial reporting and compliance.



BRADY, MARTZ & ASSOCIATES, P.C.
CROOKSTON, MINNESOTA

May 5, 2021

BASIC FINANCIAL STATEMENTS

CITY OF SHELLY, MINNESOTA
STATEMENT OF NET CASH POSITION
DECEMBER 31, 2020

	<u>Governmental Activities</u>	<u>Business- Type Activities</u>	<u>Total</u>
ASSETS			
Current Assets			
Cash and investments	\$ 92,057	\$ 506,771	\$ 598,828
Restricted Assets			
Cash and investments	<u> -</u>	<u> 46,440</u>	<u> 46,440</u>
TOTAL ASSETS	<u><u>\$ 92,057</u></u>	<u><u>\$ 553,211</u></u>	<u><u>\$ 645,268</u></u>
 NET CASH POSITION			
Restricted for:			
Improvements	\$ -	\$ 121,440	\$ 121,440
Unreserved	<u> 92,057</u>	<u> 431,771</u>	<u> 523,828</u>
TOTAL NET CASH POSITION	<u><u>\$ 92,057</u></u>	<u><u>\$ 553,211</u></u>	<u><u>\$ 645,268</u></u>

See Notes to the Basic Financial Statements

CITY OF SHELLY, MINNESOTA
STATEMENT OF ACTIVITIES ARISING FROM CASH TRANSACTIONS
FOR THE YEAR ENDED DECEMBER 31, 2020

FUNCTION	Disbursements	Program Receipts and Sources			Net Cash Sources (Uses) and Changes in Net Cash Position		
		Fees, Fines and Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-Type Activities	Total
Governmental Activities:							
General government	\$ 48,009	\$ 17,289	\$ -	\$ -	\$ (30,720)		\$ (30,720)
Public safety	61,810	7,992	3,360	-	(50,458)		(50,458)
Streets and highways	43,640	2,578	-	-	(41,062)		(41,062)
Culture and recreation	9,514	-	-	-	(9,514)		(9,514)
Housing rehab	2,566	-	-	-	(2,566)		(2,566)
Principal and interest paid on debt	26,187	-	-	-	(26,187)		(26,187)
Other	9,311	-	-	-	(9,311)		(9,311)
Total Governmental Activities	<u>201,037</u>	<u>27,859</u>	<u>3,360</u>	<u>-</u>	<u>(169,818)</u>		<u>(169,818)</u>
Business-Type Activities:							
Electric	216,279	225,565	-	-		\$ 9,286	9,286
Water	21,184	29,712	-	-		8,528	8,528
Sewer	64,419	45,678	-	-		(18,741)	(18,741)
Garbage	19,494	18,840	-	-		(654)	(654)
Total Business-Type Activities	<u>321,376</u>	<u>319,795</u>	<u>-</u>	<u>-</u>		<u>(1,581)</u>	<u>(1,581)</u>
Total Government-Wide	<u>\$ 522,413</u>	<u>\$ 347,654</u>	<u>\$ 3,360</u>	<u>\$ -</u>	<u>(169,818)</u>	<u>(1,581)</u>	<u>(171,399)</u>
General Receipts:							
Property taxes					32,753	-	32,753
Intergovernmental (not restricted for special program)							
State					76,285	-	76,285
Interest earnings					532	5,611	6,143
Transfers					3,250	(3,250)	-
Total General Receipts					<u>112,820</u>	<u>2,361</u>	<u>115,181</u>
Changes in Cash Net Position					(56,998)	780	(56,218)
Net Cash Position, January 1					149,055	552,431	701,486
Net Cash Position, December 31					<u>\$ 92,057</u>	<u>\$ 553,211</u>	<u>\$ 645,268</u>

See Notes to the Basic Financial Statements

CITY OF SHELLY, MINNESOTA
STATEMENT OF BALANCES ARISING FROM CASH TRANSACTIONS
GOVERNMENTAL FUNDS
DECEMBER 31, 2020

	General	Housing Rehab Fund	Total
ASSETS			
Cash and investments	\$ 88,602	\$ 3,455	\$ 92,057
TOTAL ASSETS	\$ 88,602	\$ 3,455	\$ 92,057
 CASH FUND BALANCE			
Assigned	\$ -	\$ 3,455	\$ 3,455
Unassigned	88,602	-	88,602
TOTAL CASH FUND BALANCE	\$ 88,602	\$ 3,455	\$ 92,057

See Notes to the Basic Financial Statements

CITY OF SHELLY, MINNESOTA
STATEMENT OF CASH RECEIPTS, DISBURSEMENTS AND CHANGES IN FUND BALANCE
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2020

	General	Housing Rehab Fund	Total
RECEIPTS			
Taxes	\$ 32,753	\$ -	\$ 32,753
Intergovernmental	81,848	-	81,848
Fire contracts	7,992	-	7,992
Licenses and permits	175	-	175
Charges for services	375	-	375
Rental	5,180	-	5,180
Interest	532	-	532
Other	11,934	-	11,934
	<u>140,789</u>	<u>-</u>	<u>140,789</u>
TOTAL RECEIPTS			
DISBURSEMENTS			
General government	48,009	-	48,009
Public safety	38,604	-	38,604
Streets and highways	43,640	-	43,640
Culture and recreation	9,514	-	9,514
Housing rehab	-	2,566	2,566
Debt service			
Principal	25,128	-	25,128
Interest	1,059	-	1,059
Capital outlay	23,206	-	23,206
Other	9,311	-	9,311
	<u>198,471</u>	<u>2,566</u>	<u>201,037</u>
TOTAL DISBURSEMENTS			
Receipts Over (Under) Disbursements	(57,682)	(2,566)	(60,248)
OTHER FINANCING SOURCES AND USES			
Transfers from (to) other funds	3,250	-	3,250
Net Sources (Uses)	<u>3,250</u>	<u>-</u>	<u>3,250</u>
Receipts and Other Financing Sources Over (Under) Disbursements and Other Financing Uses	(54,432)	(2,566)	(56,998)
Fund Balance - January 1	<u>143,034</u>	<u>6,021</u>	<u>149,055</u>
Fund Balance - December 31	<u>\$ 88,602</u>	<u>\$ 3,455</u>	<u>\$ 92,057</u>

See Notes to the Basic Financial Statements

CITY OF SHELLY, MINNESOTA
STATEMENT OF BALANCES ARISING FROM CASH TRANSACTIONS
PROPRIETARY FUNDS
DECEMBER 31, 2020

	<u>Electric</u>	<u>Water</u>	<u>Sewer</u>	<u>Garbage</u>	<u>Total</u>
ASSETS					
Current Assets					
Cash and investments	\$ 364,942	\$ 49,436	\$ 85,912	\$ 6,481	\$ 506,771
Restricted Assets					
Cash and investments	<u> -</u>	<u> -</u>	<u>46,440</u>	<u> -</u>	<u>46,440</u>
TOTAL ASSETS	<u>\$ 364,942</u>	<u>\$ 49,436</u>	<u>\$ 132,352</u>	<u>\$ 6,481</u>	<u>\$ 553,211</u>
NET CASH POSITION					
Restricted for improvements	\$ -	\$ -	\$ 121,440	\$ -	\$ 121,440
Unrestricted (deficit)	<u>364,942</u>	<u>49,436</u>	<u>10,912</u>	<u>6,481</u>	<u>431,771</u>
TOTAL NET CASH POSITION	<u>\$ 364,942</u>	<u>\$ 49,436</u>	<u>\$ 132,352</u>	<u>\$ 6,481</u>	<u>\$ 553,211</u>

See Notes to the Basic Financial Statements

CITY OF SHELLY, MINNESOTA
STATEMENT OF RECEIPTS, DISBURSEMENTS AND CHANGES IN NET CASH POSITION
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2020

	<u>Electric</u>	<u>Water</u>	<u>Sewer</u>	<u>Garbage</u>	<u>Total</u>
OPERATING RECEIPTS					
Charges for services	\$225,565	\$ 29,712	\$ 45,678	\$ 18,840	\$319,795
OPERATING DISBURSEMENTS					
Contract services	-	-	-	19,494	19,494
Salaries and fringes	50,104	-	-	-	50,104
Maintenance and repairs	19,375	2,686	9,476	-	31,537
Permits and licenses	-	1,593	-	-	1,593
Testing and sampling	-	-	1,875	-	1,875
Chemicals	-	3,456	-	-	3,456
Wheeling and power	108,377	1,794	1,541	-	111,712
Office	9,372	578	510	-	10,460
Other	29,051	408	-	-	29,459
Total Operating Disbursements	<u>216,279</u>	<u>10,515</u>	<u>13,402</u>	<u>19,494</u>	<u>259,690</u>
Operating Income (Loss)	9,286	19,197	32,276	(654)	60,105
NONOPERATING RECEIPTS (DISBURSEMENTS)					
Interest earnings	5,380	47	184	-	5,611
Interest expense and fees	-	(1,255)	(9,005)	-	(10,260)
Net Nonoperating Receipts (Disbursements)	<u>5,380</u>	<u>(1,208)</u>	<u>(8,821)</u>	<u>-</u>	<u>(4,649)</u>
Net Income (Loss) Before Operating Transfers	14,666	17,989	23,455	(654)	55,456
Transfer From (To) Other Funds	<u>(36,800)</u>	<u>-</u>	<u>33,550</u>	<u>-</u>	<u>(3,250)</u>
Net Income (Loss)	(22,134)	17,989	57,005	(654)	52,206
Purchase of Capital Asset	-	(3,614)	(35,012)	-	(38,626)
Debt Principal	<u>-</u>	<u>(5,800)</u>	<u>(7,000)</u>	<u>-</u>	<u>(12,800)</u>
Change in Net Cash Position	(22,134)	8,575	14,993	(654)	780
Net Cash Position, January 1	<u>387,076</u>	<u>40,861</u>	<u>117,359</u>	<u>7,135</u>	<u>552,431</u>
Net Cash Position, December 31	<u>\$364,942</u>	<u>\$ 49,436</u>	<u>\$132,352</u>	<u>\$ 6,481</u>	<u>\$553,211</u>

See Notes to the Basic Financial Statements

CITY OF SHELLY, MINNESOTA
STATEMENT OF CASH FLOWS – CASH BASIS
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2020

	<u>Electric</u>	<u>Water</u>	<u>Sewer</u>	<u>Garbage</u>	<u>Total</u>
CASH FLOWS FROM OPERATING ACTIVITIES					
Receipts from customers	\$ 225,565	\$ 29,712	\$ 45,678	\$ 18,840	\$ 319,795
Payments to suppliers	(166,175)	(10,515)	(13,402)	(19,494)	(209,586)
Payments to employees	(50,104)	-	-	-	(50,104)
Net Cash Provided (Used) by Operating Activities	<u>9,286</u>	<u>19,197</u>	<u>32,276</u>	<u>(654)</u>	<u>60,105</u>
CASH FLOWS FROM NONCAPITAL AND RELATED FINANCING ACTIVITIES					
Transfers from (to) other funds	(36,800)	-	33,550	-	(3,250)
Net Cash Provided (Used) by Noncapital and Related Financing Activities	<u>(36,800)</u>	<u>-</u>	<u>33,550</u>	<u>-</u>	<u>(3,250)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES					
Purchase of capital asset	-	(3,614)	(35,012)	-	(38,626)
Interest paid on bonds	-	(1,255)	(9,005)	-	(10,260)
Debt principal payments made	-	(5,800)	(7,000)	-	(12,800)
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>-</u>	<u>(10,669)</u>	<u>(51,017)</u>	<u>-</u>	<u>(61,686)</u>
CASH FLOWS FROM INVESTING ACTIVITIES					
Interest received	5,380	47	184	-	5,611
Net Increase (Decrease) in Cash	(22,134)	8,575	14,993	(654)	780
Cash Balance, January 1	<u>387,076</u>	<u>40,861</u>	<u>117,359</u>	<u>7,135</u>	<u>552,431</u>
Cash Balance, December 31	<u>\$ 364,942</u>	<u>\$ 49,436</u>	<u>\$ 132,352</u>	<u>\$ 6,481</u>	<u>\$ 553,211</u>

See Notes to the Basic Financial Statements

CITY OF SHELLY, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS
DECEMBER 31, 2020

The City of Shelly, Minnesota, (the "City") was incorporated as a statutory city, under the provision of the State of Minnesota. The City operates under a mayor and four-member council. It provides the following services: public safety, streets, public improvements, planning and zoning, electric, water, sewer, sanitation, and general administrative services.

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The financial statements of the City include all organizations, funds and account groups over which the City's Board exercises significant influence over and, or is financially accountable or organizations for which the nature and significance of their relationship with the City is such that exclusion would cause the City of Shelly, Minnesota's financial statements to be misleading.

Based on the foregoing criteria, the Shelly Volunteer Firefighters Organization is not included in the City's reporting entity. The Organization was established by its members to provide fire safety and protection for the community. Its members have sole authority over daily operations and financial activities.

Currently, the City does not have any component units.

Basis of Presentation

Government-Wide Financial Statements

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

Fund Financial Statements

Fund financial statements of the City 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. Funds are typically organized into three categories: governmental, proprietary and fiduciary.

Governmental Funds

General Fund

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

CITY OF SHELLY, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS - CONTINUED
DECEMBER 31, 2020

Special Revenue Fund

Special revenue funds are used to account for the proceeds of specific revenue sources (other than capital projects) where the expenditures are designated for purposes specified in the grant agreements. The City includes the following special revenue fund as major:

Housing Rehab Fund – is used to account for the cash received and disbursed for the City's housing rehab program.

Proprietary Funds

Enterprise Funds are used to account for business-type activities provided to the general public. These activities are financed primarily by user charges, and the measurement of financial activities focuses on net income measurement similar to the private sector. The City includes the following enterprise funds as major:

Electric Fund – account for the activities in providing electricity services to the public users.

Water Fund – account for the activities in providing water services to the public users.

Sewer Fund – account for the activities in providing sewer services to the public users.

Garbage Fund – account for the activities in providing garbage collection services to the public users.

Measurement Focus and Basis of Accounting

Measurement focus is a term used to describe the recognition of revenues and expenditures within the various financial statements. Basis of accounting refers to “when” transactions are recorded regardless of the measurement focus applied.

Measurement Focus

In the government-wide Statement of Net Cash Position and the Statement of Activities Arising from Cash Transactions, governmental and business-type activities are presented using the economic resources measurement focus, within the limitations of the cash basis of accounting, as defined below.

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

In the fund financial statements, the “current financial resources” measurement focus or the “economic resources” measurement focus, as applied to the cash basis of accounting is used as appropriate:

All governmental and business-type funds utilize a “current financial resources” measurement focus. Only current financial assets and liabilities are generally included on their balance sheets. Their operating statements present sources and uses of available spendable financial resources during a given period. These funds use fund balance as their measure of available spendable financial resources at the end of the period.

CITY OF SHELLY, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS - CONTINUED
DECEMBER 31, 2020

When fund balance resources are available for use, it is the government's policy to use restricted, committed, assigned and unassigned resources as needed in that order.

Basis of Accounting

The financial statements are presented in accordance with the cash basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America.

The City of Shelly, Minnesota, has elected to comply with the Minnesota Office of the State Auditor's minimum reporting requirements prescribed for cities fewer than 2,500 in population.

In the government-wide Statement of Net Cash Position and Statement of Activities Arising from Cash Transactions, governmental and business-type activities are presented using a cash method of accounting. This basis recognizes revenues and receipts and disbursements when they result from cash transactions in government-wide statements. This basis is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

As a result of the use of the cash basis of accounting, certain assets and their related revenues (such as accounts receivable and revenue for billed or unbilled services provided in current year and capital assets) and certain liabilities and their related expense (such as accounts payables, unpaid goods or services received in the current year and accrued expenses and long-term debt) are not recorded in these financial statements.

If the City utilized the basis of accounting recognized as generally accepted, the fund financial statements for governmental funds would use the modified accrual basis of accounting and the government-wide financials and the statements for proprietary funds would be presented on the accrual basis of accounting.

Budgets

The annual budget was adopted this year through the passage of an annual budget ordinance and amended as required for the general fund and all major special revenue funds. The same basis of accounting is used for the budget presentation as is used to reflect the cash receipts and disbursements recognized. Any budget changes are approved by the Council. All unencumbered appropriations lapse at year-end.

Revenues

In the Statement of Activities Arising from Cash Transactions, cash basis revenues that are derived directly from each activity or from parties outside the City's taxpayers are reported as program revenues. The City has the following program revenues: charges for services, licenses, permit and fees, rental income and operating and capital grants specific to programs. All other governmental revenues and general tax levies are classified as general revenue.

CITY OF SHELLY, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS - CONTINUED
DECEMBER 31, 2020

Property Taxes

Property taxes are set by the City Council in October of each year, and are certified to the County for collection in the following year. In Minnesota, counties act as collection agents for all property taxes.

The County spreads all levies over taxable property. Such taxes become an enforceable lien on January 1. Real property taxes may be paid by taxpayers in two equal installments on May 15 and October 15. The County provides tax settlements to the City throughout the year. No receivable is recorded by the City because it used the cash basis method of accounting. Revenues are recognized in the year of collection.

Cities with populations below 2,500, as is the City of Shelly, Minnesota, are exempt from the State's levy limitation law.

Cash and Investments

Cash balances are deposited in each fund's name in separate accounts. All the City's cash and investments during the year were in interest-bearing checking accounts, money market accounts or short-term certificates of deposit, authorized by statute.

Restricted Cash and Investments

A restricted cash balance has been set aside for future water system improvements in accordance with requirements established by USDA in its loan agreement.

Net Position

In the government-wide financial statements, equity is classified as "net position" and displayed in two components:

1. Restricted Net Position – Consists of net assets with constraints placed on the use either by (1) external groups such as creditors, grantors, contributors, or laws and regulations of other governments; or (2) law through constitutional provisions or enabling legislation.
2. Unrestricted Net Position – All other net assets that do not meet the definition of "restricted."

Cash Fund Balance

In the governmental fund financial statements, cash fund balances are classified as nonspendable, restricted, committed, assigned or unassigned.

Nonspendable fund balance represents a portion of fund balance that includes amounts that cannot be spent because they are either (a) not in spendable form or (b) legally or contractually required to be maintained intact.

CITY OF SHELLY, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS - CONTINUED
DECEMBER 31, 2020

Restricted fund balance represents a portion of fund balance that reflects constraints placed on the use of resources (other than nonspendable items) that are either: (a) externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments; or (b) imposed by law through constitutional provisions or enabling legislation.

Committed fund balance includes amounts that can only be used for specific purposes pursuant to constraints imposed by formal action of the government's highest level of decision making authority which is the City Council through an ordinance or resolution.

Assigned fund balance represents amounts constrained by the government's intent to be used for specific purposes, but neither restricted nor committed.

Unassigned fund balance represents residual classification for the general fund. This classification represents fund balance not assigned to other funds and not restricted, committed, or assigned to specific purposes within the general fund. The general fund should be the only fund that reports a positive unassigned fund balance amount. In other governmental funds, if expenditures incurred for specific purposes exceed the amounts restricted, committed, or assigned to those purposes, it would be necessary to report a negative unassigned fund balance.

Estimates

The preparation of financial statements in conformity with a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

NOTE 2 DEPOSITS

Minnesota Statutes require that all deposits with financial institutions be collateralized in an amount equal to 110% of deposits in excess of FDIC (140% if collateralized with notes secured by first mortgages).

At December 31, 2020, the City's carrying amount of deposits was \$645,268 and the bank balance was \$658,760. All of the deposits were covered by FDIC and by an irrevocable and unconditional letter of credit, irrevocably authorized to draw on the Federal Home Loan Bank of Des Moines, in an amount not to exceed \$750,000.

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.

CITY OF SHELLY, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS - CONTINUED
DECEMBER 31, 2020

Credit Risk

The City is authorized by Minnesota Statutes to invest in the following: direct obligations or obligations guaranteed by the federal government or its agencies; share of investment companies registered under the Federal Investment Company Act of 1940 and is rated in one of the two highest rating categories by a statistical rating agency, and all of the investments have a final maturity of thirteen months or less; general obligations rated "A" or better; revenue obligations rated "AA" or better, general obligations of Minnesota Housing Finance Agency rated "A" or better; commercial paper issued by United States' corporations or their Canadian subsidiaries, of the highest quality category by at least two nationally recognized rating agencies, and maturing in 270 days or less; Guaranteed Investment Contracts guaranteed by a United States commercial bank or insurance company, domestic branch of a foreign bank and with a credit quality in one of the top two highest categories; repurchase or reverse repurchase agreements and securities lending agreements with financial institutions qualified as a "depository" by the government entity, with banks that are members of the Federal Reserve System with capitalization exceeding \$10,000,000, a primary reporting dealer in U.S. government securities to the Federal Reserve Bank of New York, or certain Minnesota securities broker-dealers. The City has no investment policy that would further limit its investment choices.

Custodial Credit Risk - Deposits

The City does not have a formal custodial credit risk policy. Custodial credit risk is the risk that in the event of a bank failure, the City's deposits may not be returned to it.

NOTE 3 DEFINED BENEFIT PENSION PLANS

Plan Description

All full-time and certain part-time employees of the City of Shelly are covered by defined benefit plans administered by the Public Employees Retirement Association of Minnesota (PERA). PERA administers the General Employees Retirement Plan (accounted for in the General Employees Fund), which are cost-sharing, multiple-employer retirement plans. These plans are established and administered in accordance with *Minnesota Statutes*, Chapters 353 and 356. PERA's defined benefit pension plans are tax qualified plans under Section 401(a) of the Internal Revenue Code.

General Employees Plan members belong to either the Coordinated Plan or the Basic Plan. Coordinated Plan members are covered by Social Security and Basic Plan members are not. All new members must participate in the Coordinated Plan.

PERA provides retirement benefits as well as disability benefits to members and survivor benefits upon death of eligible members. Benefits are established by state statute. Benefits for members of the General Employees Plan vest after five years of credited service. The defined benefit retirement plan benefits are based on a member's highest average salary for any 5 years of allowable service, age, and years of credit at termination of service.

Two methods are used to compute benefits for PERA's Coordinated Plan members. Members hired prior to July 1, 1989, receive the higher of Method 1 or Method 2 formulas. Only Method 2 is used for members hired after June 30, 1989. Under Method 1, the accrual rate for Coordinated members is 1.2% for each of the first 10 years of service and 1.7% for each additional year. The

CITY OF SHELLY, MINNESOTA
NOTES TO THE BASIC FINANCIAL STATEMENTS - CONTINUED
DECEMBER 31, 2020

rates are 2.2% and 2.7%, respectively, for Basic members. Under Method 2, the accrual rate for Coordinated members is 1.7% for all years of service, and 2.7% for Basic members. For members hired prior to July 1, 1989 a full annuity is available when age plus years of service equal 90 and normal retirement age is 65. For members hired on or after July 1, 1989 normal retirement age is the age for unreduced Social Security benefits capped at 66.

For all General Employee Plan members hired prior to July 1, 1989 whose annuity is calculated using Method 1, a full annuity is available when age plus years of service equal 90. Method 2 provides for unreduced retirement benefits at age 65 for members first hired prior to July 1, 1989 or age 66 (the age for unreduced Social Security benefits), for those first hired on or after that date. Early retirement may begin at age 55 with an actuarial reduction (about six percent per year) for members retiring prior to full retirement age.

Normal retirement age is 65 for Basic and Coordinated members hired prior to July 1, 1989. Normal retirement age is the age for unreduced Social Security benefits capped at 66 for Coordinated members hired on or after July 1, 1989. A reduced retirement annuity is also available to eligible members seeking early retirement with an actuarial reduction in the member's benefit.

There are different types of annuities available to members upon retirement. A single-life annuity is a lifetime annuity that ceases upon the death of the retiree—no survivor annuity is payable. There are also various types of joint and survivor annuity options available which will be payable over joint lives. Members may also leave their contributions in the fund upon termination of public service in order to qualify for a deferred annuity at retirement age. Refunds of contributions are available at any time to members who leave public service before retirement benefits begin.

The benefit provisions stated in the preceding paragraphs of this section are current provisions and apply to active plan participants.

PERA issues a publicly available financial report that includes financial statements and required supplementary information for the General Employees, Police and Fire, and Correctional plans. That report may be obtained on the PERA's website at www.mnpera.org/about/financial/.

Funding Policy

Minnesota Statutes Chapter 353 sets the rates for employer and employee contributions. These statutes are established and amended by the state Legislature. The City of Shelly makes annual contributions to the pension plans equal to the amount required by state statutes. General Employees Basic Plan members and Coordinated Plan members were required to contribute 9.1 percent and 6.5 percent, respectively, of their annual covered salary in 2020. In 2020, the City of Shelly was required to contribute the following percentages of annual covered payroll: 11.78 percent for Basic Plan members and 7.5 percent for Coordinated Plan members.

The City of Shelly's contributions to the General Employees Fund for the years ended December 31, 2020, 2019 and 2018 were \$5,884, \$5,801, and \$8,726, respectively.

NOTE 4 EXCESS EXPENDITURES OVER APPROPRIATIONS

Expenditures exceeded appropriations in the General Fund for the year ended December 31, 2020, by \$69,215.

CITY OF SHELLY, MINNESOTA
 NOTES TO THE BASIC FINANCIAL STATEMENTS - CONTINUED
 DECEMBER 31, 2020

NOTE 5 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.

Workers compensation coverage is provided through a pooled self-insurance program through the League of Minnesota Cities Insurance Trust (LMCIT). The City pays an annual premium to LMCIT. The City is subject to supplemental assessments if deemed necessary by the LMCIT.

The LMCIT reinsures through Workers Compensation Reinsurance Association (WCRA) as required by law, for workers compensation. The City's workers compensation coverage is retrospectively rated. With this type of coverage, final premiums are determined after loss experience is known. The amount of premium adjustment, if any, is considered immaterial and not recorded until received or paid.

Property and casualty insurance coverage is provided through a pooled self-insurance program through the LMCIT. The City pays an annual premium to the LMCIT, which reinsures through commercial companies for claims in excess of various amounts. The City retains risk from the deductible portions.

There were no significant reductions in insurance from the previous year or settlements in excess of insurance for any of the past three years.

NOTE 6 COMMITMENTS

The water fund has a general obligation revenue bond with a balance of \$19,300 as of December 31, 2020, a maturity date of January 1, 2024 and 5% interest rate. The sewer fund has a general obligation revenue bond with a balance of \$354,000 as of December 31, 2020, a maturity date of January 1, 2050 and 3.75% interest rate. The City makes annual payments on these bonds and loan.

NOTE 7 INTERFUND TRANSFER

The composition of the interfund transfers as of December 31, 2020, is as follows:

<u>Transfers In</u>	<u>Transfers Out</u>	<u>Amount</u>	<u>Purpose</u>
Sewer Fund	Electric Fund	\$ 33,550	To provide funds for lift station pumps
General Fund	Electric Fund	3,250	To provide funds for new Fire Dept bank account
		<u>\$ 36,800</u>	

SUPPLEMENTAL INFORMATION

CITY OF SHELLY, MINNESOTA
BUDGETARY COMPARISON SCHEDULE – CASH BASIS
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2020

	Original and Final Budget Amounts	Actual Amounts	Final Budget to Actual
RECEIPTS			
Property taxes	\$ 26,500	\$ 32,753	\$ 6,253
Intergovernmental:			
Local	2,203	2,203	-
State:			
Local governmental aid	62,855	62,855	-
Market value credit aid	178	-	(178)
Other state aid	14,830	16,790	1,960
Total Intergovernmental	80,066	81,848	1,782
Other:			
Fire Contracts and calls	7,425	7,992	567
Licenses and permits	100	175	75
Charges for services	100	375	275
Rental	5,709	5,180	(529)
Interest	800	532	(268)
Other	4,100	11,934	7,834
Total Other	18,234	26,188	7,954
 TOTAL RECEIPTS	 124,800	 140,789	 15,989
DISBURSEMENTS			
General government:			
Mayor and council	3,241	2,017	1,224
City Clerk-Treasurer	15,250	13,224	2,026
Assessing	1,200	1,087	113
Insurance	5,000	4,775	225
Legal and audit	4,300	3,761	539
City hall	8,000	21,273	(13,273)
Elections	900	1,872	(972)
Total General Government	37,891	48,009	(10,118)
Public Safety and Welfare:			
Fire	27,760	29,917	(2,157)
Fire capital outlay	-	23,206	(23,206)
Pest control	2,850	8,687	(5,837)
Total Public Safety and Welfare	30,610	61,810	(31,200)

CITY OF SHELLY, MINNESOTA
BUDGETARY COMPARISON SCHEDULE – CASH BASIS
GENERAL FUND - CONTINUED
FOR THE YEAR ENDED DECEMBER 31, 2020

	Original and Final Budget Amounts	Actual Amounts	Final Budget to Actual
Streets and Highways:			
Maintenance	\$ 40,450	\$ 43,640	\$ (3,190)
Total Streets and Highways	40,450	43,640	(3,190)
Culture and Recreation:			
Park	3,850	6,221	(2,371)
Community building	4,800	3,293	1,507
Total Culture and Recreation	8,650	9,514	(864)
Debt Service:			
Principal paid	5,555	25,128	(19,573)
Interest paid	-	1,059	(1,059)
Total Debt Service	5,555	26,187	(20,632)
Other:			
Real estate taxes	2,100	1,682	418
Post office building	4,000	7,629	(3,629)
Total Other	6,100	9,311	(3,211)
TOTAL DISBURSEMENTS	129,256	198,471	(69,215)
Receipts Over (Under) Disbursements	(4,456)	(57,682)	(53,226)
OTHER SOURCES AND USES			
Transfers from (to) other funds	-	3,250	3,250
Total Other Sources (Uses)	-	3,250	3,250
Receipts and Other Sources Over (Under) Disbursements and Other Uses	(4,456)	(54,432)	(49,976)
Beginning Fund Balance	143,034	143,034	-
Ending Fund Balance	\$ 138,578	\$ 88,602	\$ (49,976)

CITY OF SHELLY, MINNESOTA
SCHEDULE OF INDEBTEDNESS
FOR THE YEAR ENDED DECEMBER 31, 2020

Issued	Interest Rate	Issue Date	Final Maturity Date	Balance January 1, 2020	Issued	Retired	Balance December 31, 2020
Revenue Bonds							
G.O. Water Revenue Bonds	5.0%	1/1/1994	1/1/2024	\$ 25,100	-	\$ 5,800	\$ 19,300
G.O. Sewer Revenue Bonds 2010A	3.75%	12/1/2010	1/1/2050	361,000	-	7,000	354,000
USDA Fire Truck Loan	3.5%	1/1/2014	6/12/2024	25,128	-	25,128	-
Total Indebtedness				<u>\$ 411,228</u>	<u>\$ -</u>	<u>\$ 37,928</u>	<u>\$ 373,300</u>

CITY OF SHELLY, MINNESOTA
SCHEDULE OF ADDITIONAL INFORMATION
AS OF DECEMBER 31, 2020

SCHEDULE OF ACCOUNTS RECEIVABLE

<u>Fund</u>	<u>Source of Revenue and Purpose</u>	<u>Amount</u>
Electric, Water, Sewer & Garbage	Customer user fees	<u>\$ 27,406</u>

SCHEDULE OF ACCOUNTS PAYABLE

<u>Fund</u>	<u>Vendor Name</u>	<u>Item or Purpose</u>	<u>Amount</u>
Electric, Water, Sewer & Garbage	Internal Revenue Service	payroll taxes	\$ 724
	MN PERA	PERA employer contribution	465
	Payroll - December	payroll wages	915
	MN Department of Revenue	payroll taxes	287
	MN Department of Revenue	sales tax	1,246
	Halstad Telephone	telephone	379
Electric	Otter Tail Power	purchased power	5,832
	WAPA	purchased power	3,665
Garbage	Fuch's Sanitation Service	garbage service	<u>1,230</u>
			<u>\$ 14,743</u>

CITY OF SHELLY, MINNESOTA
STATEMENT OF NET POSITION – MODIFIED CASH BASIS
PROPRIETARY FUNDS
DECEMBER 31, 2020

	<u>Electric</u>	<u>Water</u>	<u>Sewer</u>	<u>Garbage</u>	<u>Total</u>
ASSETS					
Current Assets					
Cash and investments	\$ 364,942	\$ 49,436	\$ 85,912	\$ 6,481	\$ 506,771
Restricted Assets					
Cash and investments	-	-	46,440	-	46,440
Capital Assets					
Capital Assets	261,312	568,929	2,153,423	-	2,983,664
Accumulated depreciation	<u>(197,829)</u>	<u>(508,316)</u>	<u>(656,958)</u>	<u>-</u>	<u>(1,363,103)</u>
Net Capital Assets	<u>63,483</u>	<u>60,613</u>	<u>1,496,465</u>	<u>-</u>	<u>1,620,561</u>
TOTAL ASSETS	<u>\$ 428,425</u>	<u>\$ 110,049</u>	<u>\$ 1,628,817</u>	<u>\$ 6,481</u>	<u>\$ 2,173,772</u>
LIABILITIES					
Noncurrent Liabilities					
Bonds payable	<u>\$ -</u>	<u>\$ 19,300</u>	<u>\$ 354,000</u>	<u>\$ -</u>	<u>\$ 373,300</u>
TOTAL LIABILITIES	<u>\$ -</u>	<u>\$ 19,300</u>	<u>\$ 354,000</u>	<u>\$ -</u>	<u>\$ 373,300</u>
NET POSITION					
Net investment in					
capital assets	\$ 63,483	\$ 41,313	\$ 1,142,465	\$ -	\$ 1,247,261
Restricted for improvements	-	-	121,440	-	121,440
Unrestricted	<u>364,942</u>	<u>49,436</u>	<u>10,912</u>	<u>6,481</u>	<u>431,771</u>
TOTAL NET POSITION	<u>\$ 428,425</u>	<u>\$ 90,749</u>	<u>\$ 1,274,817</u>	<u>\$ 6,481</u>	<u>\$ 1,800,472</u>

CITY OF SHELLY, MINNESOTA
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
MODIFIED CASH BASIS - PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2020

	<u>Electric</u>	<u>Water</u>	<u>Sewer</u>	<u>Garbage</u>	<u>Total</u>
OPERATING REVENUES					
Charges for services	\$ 225,565	\$ 29,712	\$ 45,678	\$ 18,840	\$ 319,795
OPERATING EXPENSES					
Contract services	-	-	-	19,494	19,494
Salaries and fringes	50,104	-	-	-	50,104
Maintenance and repairs	19,375	2,686	9,476	-	31,537
Permits and licenses	-	1,593	-	-	1,593
Testing and sampling	-	-	1,875	-	1,875
Chemicals	-	3,456	-	-	3,456
Wheeling and power	108,377	1,794	1,541	-	111,712
Office	9,372	578	510	-	10,460
Depreciation	10,445	5,622	55,724	-	71,791
Other	29,051	408	-	-	29,459
Total Operating Expenses	<u>226,724</u>	<u>16,137</u>	<u>69,126</u>	<u>19,494</u>	<u>331,481</u>
Operating Income (Loss)	(1,159)	13,575	(23,448)	(654)	(11,686)
NONOPERATING REVENUES (EXPENSES)					
Interest earnings	5,380	47	184	-	5,611
Interest expense and bond fees	-	(1,255)	(9,005)	-	(10,260)
Net Nonoperating Revenues (Expenses)	<u>5,380</u>	<u>(1,208)</u>	<u>(8,821)</u>	<u>-</u>	<u>(4,649)</u>
Net Income (Loss) Before Transfers	4,221	12,367	(32,269)	(654)	(16,335)
Transfers From (To) Other Funds	<u>(36,800)</u>	<u>-</u>	<u>33,550</u>	<u>-</u>	<u>(3,250)</u>
Net Income (Loss)	(32,579)	12,367	1,281	(654)	(19,585)
Net Position, January 1	<u>461,004</u>	<u>78,382</u>	<u>1,273,536</u>	<u>7,135</u>	<u>1,820,057</u>
Net Position, December 31	<u>\$ 428,425</u>	<u>\$ 90,749</u>	<u>\$ 1,274,817</u>	<u>\$ 6,481</u>	<u>\$ 1,800,472</u>

CITY OF SHELLY, MINNESOTA
STATEMENT OF CASH FLOWS - MODIFIED CASH BASIS
PROPRIETARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2020

	<u>Electric</u>	<u>Water</u>	<u>Sewer</u>	<u>Garbage</u>	<u>Total</u>
CASH FLOWS FROM OPERATING ACTIVITIES					
Receipts from customers	\$ 225,565	\$ 29,712	\$ 45,678	\$ 18,840	\$ 319,795
Payments to suppliers	(166,175)	(10,515)	(13,402)	(19,494)	(209,586)
Payments to employees	(50,104)	-	-	-	(50,104)
Net Cash Provided (Used) by Operating Activities	<u>9,286</u>	<u>19,197</u>	<u>32,276</u>	<u>(654)</u>	<u>60,105</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:					
Transfer from (to) other funds	<u>(36,800)</u>	-	<u>33,550</u>	-	<u>(3,250)</u>
Net Cash Provided (Used) by Noncapital and Related Financing Activities	<u>(36,800)</u>	-	<u>33,550</u>	-	<u>(3,250)</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES					
Purchase or construction of capital asset	-	(3,614)	(35,012)	-	(38,626)
Interest paid on bonds	-	(1,255)	(9,005)	-	(10,260)
Bond principal paid	-	(5,800)	(7,000)	-	(12,800)
Net Cash Provided (Used) by Capital and Related Financing Activities	<u>-</u>	<u>(10,669)</u>	<u>(51,017)</u>	<u>-</u>	<u>(61,686)</u>
CASH FLOWS FROM INVESTING ACTIVITIES					
Interest received	<u>5,380</u>	<u>47</u>	<u>184</u>	<u>-</u>	<u>5,611</u>
Net Increase (Decrease) in Cash	(22,134)	8,575	14,993	(654)	780
Cash Balance, January 1	<u>387,076</u>	<u>40,861</u>	<u>117,359</u>	<u>7,135</u>	<u>552,431</u>
Cash Balance, December 31	<u>\$ 364,942</u>	<u>\$ 49,436</u>	<u>\$ 132,352</u>	<u>\$ 6,481</u>	<u>\$ 553,211</u>
Cash Balance:					
Current	\$ 364,942	\$ 49,436	\$ 85,912	\$ 6,481	\$ 506,771
Restricted	-	-	46,440	-	46,440
	<u>\$ 364,942</u>	<u>\$ 49,436</u>	<u>\$ 132,352</u>	<u>\$ 6,481</u>	<u>\$ 553,211</u>
Reconciliation of Operating Income to Net Cash Provided (Used) by Operating Activities:					
Operating income (loss)	\$ (1,159)	\$ 13,575	\$ (23,448)	\$ (654)	\$ (11,686)
Adjustments to reconcile operating income to net cash provided (used) by operating activities:					
Depreciation expense	<u>10,445</u>	<u>5,622</u>	<u>55,724</u>	<u>-</u>	<u>71,791</u>
Net Cash Provided (Used) by Operating Activities	<u>\$ 9,286</u>	<u>\$ 19,197</u>	<u>\$ 32,276</u>	<u>\$ (654)</u>	<u>\$ 60,105</u>

INDEPENDENT AUDITOR'S REPORT ON MINNESOTA LEGAL COMPLIANCE

Honorable Mayor and City Council
City of Shelly
Shelly, MN 56568

We have audited, in accordance with auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the governmental activities, business-type activities, and each major fund of the City of Shelly, Minnesota, as of and for the year ended December 31, 2020, and the related notes to the financial statements, which collectively comprise the City of Shelly's basic financial statements, and have issued our report thereon dated May 5, 2021. The City of Shelly, Minnesota, prepares its financial statements on the cash basis, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

Legal Compliance

In connection with our audit, nothing came to our attention that caused us to believe that the City failed to comply with the provisions of the contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements and miscellaneous provisions sections of the *Minnesota Legal Compliance Audit Guide for Cities*, promulgated by the State Auditor pursuant to Minn. Stat. § 6.65, insofar as they relate to accounting matters. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the City's noncompliance with the above referenced provisions, insofar as they relate to accounting matters.

Purpose of the Report

The purpose of this report is solely to describe the scope of our testing of compliance and the results of that testing, and not to provide an opinion on compliance. Accordingly, this communication is not suitable for any other purpose.



BRADY, MARTZ & ASSOCIATES, P.C.
CROOKSTON, MINNESOTA

May 5, 2021

**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**

Honorable Mayor and City Council
City of Shelly
Shelly, MN 56568

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, and each major fund of the City of Shelly, Minnesota as of and for the year ended December 31, 2020, and the related notes to the financial statements, which collectively comprise the City of Shelly, Minnesota's basic financial statements and have issued our report thereon dated May 5, 2021. The City of Shelly, Minnesota, prepares its financial statements on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

Internal Control over Financial Reporting

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

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiency 2020-001 described in the accompanying schedule of findings to be a material weakness.

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 deficiency 2020-002 described in the accompanying schedule of findings to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether City of Shelly, Minnesota'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 financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

The City of Shelly, Minnesota's Responses to Findings

The City of Shelly, Minnesota's responses to the findings identified in our audit are described in the accompanying schedule of findings and corrective action plan. The City of Shelly, Minnesota's responses were not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

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 entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



BRADY, MARTZ & ASSOCIATES, P.C.
CROOKSTON, MINNESOTA

May 5, 2021

CITY OF SHELLY, MINNESOTA
SCHEDULE OF FINDINGS
DECEMBER 31, 2020

FINDING 2020-001 (Material Weakness)

Criteria: Generally, a system of internal control has the proper separation of duties between authorization, custody, record keeping and reconciliation.

Condition: Lack of sufficient segregation of duties relating to utility and service billings and cash receipts. The clerk is responsible for the utility billing, receipt of monies, recording transactions in receivable ledger and bank reconciliations.

Cause: Size and cost constraints limit the number of City personnel available within the municipality to perform accounting duties.

Effect: The lack of segregation of duties reduces the level of internal controls over financial reporting which could adversely affect the ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements.

Recommendation: The areas should be reviewed periodically and consideration given to improving the segregation of duties in the most effective manner possible.

View of Responsible Officials: The corrective action will be determined by management when it becomes cost effective to implement proper segregation of accounting duties.

CITY OF SHELLY, MINNESOTA
SCHEDULE OF FINDINGS - CONTINUED
DECEMBER 31, 2020

FINDING 2020-002 (Significant Deficiency)

Criteria: An appropriate system of internal controls requires the City to identify all journal entries required to maintain a general ledger and prepare financial statements in compliance with the cash basis of accounting.

Condition: The City's personnel prepare periodic financial information for internal use that meets the needs of management and the city council. However, the City currently does not prepare the financial statements, including the accompanying note disclosures, as required by the cash basis of accounting. The City also does not have the internal resources to identify all journal entries required to maintain the general ledger on the cash basis of accounting. The City has elected to have the auditors assist in the preparation of the financial statements and notes.

Cause: The City elected to not allocate resources for the preparation of the financial statements.

Effect: There is an increased risk of material misstatement to the City's financial statements.

Recommendation: We recommend the City consider the additional risk of having the auditors assist in the preparation of the financial statements and note disclosures. As a compensating control, the City should establish an internal control policy to document the annual review of the financial statements and to review the financial statements disclosure checklist.

View of Responsible Officials: The City agrees with the recommendation and will review on an annual basis.

CITY OF SHELLY, MINNESOTA
CORRECTIVE ACTION PLAN
FOR THE YEAR ENDED DECEMBER 31, 2020

FINDING 2020-001 (Material Weakness)

Contact Person – Mark Dohman, City Clerk

Corrective Action Plan – The City has the following procedure in place to mitigate risk:

- 1) Council approves checks.

Completion Date – Ongoing

FINDING 2020-002 (Significant Deficiency)

Contact Person – Mark Dohman, City Clerk

Corrective Action Plan – Will obtain internal expertise to handle all aspects of external financial reporting when it becomes economically feasible.

Completion Date – Ongoing