

City of Sandstone
Sandstone, Minnesota
MANAGEMENT LETTER
For the Fiscal Year Ended December 31, 2016

City of Sandstone
Sandstone, Minnesota
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REPORT ON MATTERS IDENTIFIED AS A RESULT OF
THE AUDIT OF THE FINANCIAL STATEMENTS

June 7, 2017

Honorable Mayor and Members
of the City Council
City of Sandstone
Sandstone, Minnesota

In planning and performing our audit of the financial statements of the City of Sandstone, Sandstone, Minnesota, as of and for the year ended December 31, 2016, in accordance with auditing standards generally accepted in the United States of America, we considered the City's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion 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.

However, during our audit we became aware of several matters that are opportunities for strengthening internal controls and operating efficiency. The accompanying memorandum includes suggestions for improvement of accounting procedures and internal accounting control measures that came to our attention as a result of our audit of the basic financial statements of the City of Sandstone, Minnesota, for the year ended December 31, 2016. The matters discussed herein were considered by us during our audit and they do not modify the opinion expressed in our independent auditors' report date June 7, 2017, on such statements.

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

A significant deficiency is a deficiency, or 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.

This communication is intended solely for the information and use of management, the City Council, others within the City and state oversight agencies, and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink that reads "Althoff & Nordquist, LLC". The signature is written in a cursive, flowing style.

Althoff & Nordquist LLC
Mora, Minnesota
June 7, 2017

City of Sandstone
Sandstone, Minnesota
SIGNIFICANT DEFICIENCIES
December 31, 2016

LACK OF SEGREGATION OF ACCOUNTING DUTIES

During the year ended December 31, 2016, the City did not have adequate segregation of accounting duties due to a limited number of office employees.

Management and the City council are aware of this condition and have taken certain steps to compensate for the lack of segregation, but due to the small staff needed to handle all of the accounting duties, the costs of obtaining desirable segregation of accounting duties can often exceed benefits which could be derived. However, management and City council must remain aware of this situation and should continually monitor the accounting system, including changes that occur.

PREPARATION OF FINANCIAL STATEMENTS

As a function of the audit process, auditors are required to gain an understanding of the City's internal control, including the financial reporting process.

The City does not have an internal control system designed to provide for the preparation of the financial statements being audited. As auditors we were requested to draft the financial statements and accompanying notes to the financial statements. This circumstance is not unusual in a city of your size.

Even though all management decisions related to financial reporting are made by the City's management and approval of the financial statements lies with management, 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 Sandstone
Sandstone, Minnesota
REQUIRED COMMUNICATIONS
December 31, 2016

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Sandstone, Minnesota for the year then ended December 31, 2016. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated June 7, 2017. Professional standards also require that we communicate to you the following information related to our audit.

OUR RESPONSIBILITY UNDER U.S. GENERALLY ACCEPTED AUDITING STANDARDS AND GOVERNMENT AUDITING STANDARDS

As stated in our engagement letter, our responsibility, as described by professional standards, is to express an opinion about whether financial statements prepared by management with your oversight are fairly presented in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities. Our responsibility is to plan and perform our audit to obtain reasonable, but no absolute, assurance that the financial statements are free of material misstatement. As part of our audit, we considered the internal control of the City. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control. We are responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures specifically to identify such matters.

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit.

PLANNED SCOPE AND TIMING OF THE AUDIT

We performed the audit according to the planned scope and timing previously communicated to you.

City of Sandstone
Sandstone, Minnesota
REQUIRED COMMUNICATIONS
December 31, 2016

QUALITATIVE ASPECTS OF ACCOUNTING PRACTICES

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the City are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during 2016. We noted no transactions entered into during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

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

The disclosures in the financial statements are neutral, consistent, and clear.

DIFFICULTIES ENCOUNTERED IN PERFORMING THE AUDIT

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

CORRECTED AND UNCORRECTED MISSTATEMENTS

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements detected as a result of audit procedures and corrections by management were material, either individually or in the aggregate, to the financial statements taken as a whole.

DISAGREEMENTS WITH MANAGEMENT

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

City of Sandstone
Sandstone, Minnesota
REQUIRED COMMUNICATIONS
December 31, 2016

MANAGEMENT REPRESENTATIONS

We requested certain representations from management which were provided to us in the management representation letter.

MANAGEMENT CONSULTATIONS WITH OTHER INDEPENDENT ACCOUNTANTS

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a “second opinion” on certain situations. If a consultation involves application of an accounting principle to the City’s financial statements or a determination of the type of auditor’s opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. We are not aware of any consultations by the City’s management with other accountants during the course of our audit.

OTHER ISSUES

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

OTHER INFORMATION IN DOCUMENTS CONTAINING AUDITED FINANCIAL STATEMENTS

We have not reviewed, and it is our understanding, that no other published documents exist that contain audited financial statements information, for which we are currently auditing. As stated in our engagement letter, if you publish or reproduce the financial statements or make reference to our Firm name in relation to such documents, you agree to provide us with a copy of the final reproduced material for our approval before it is distributed.

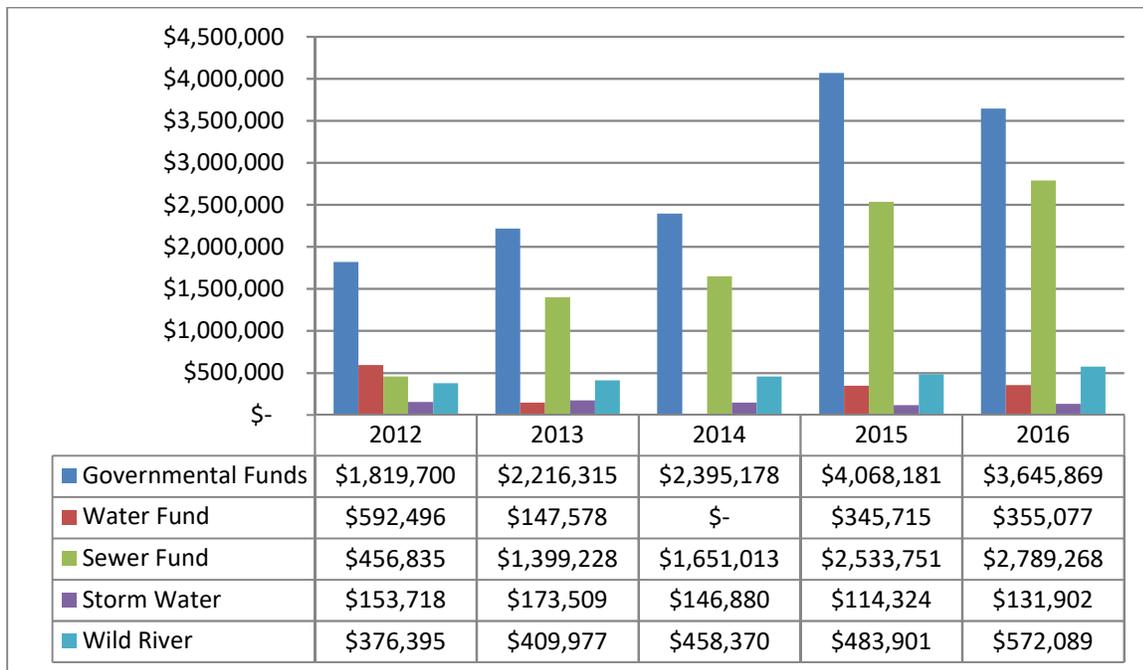
City of Sandstone
Sandstone, Minnesota
FINANCIAL ANALYSIS
December 31, 2016

The following pages provide graphic representation of select data pertaining to the financial position and operations of the City for the past five years. Our analysis of each graph is presented to provide a basis for discussion of past performances and how implementing certain changes may enhance future performance. We suggest you view each graph and document if our analysis is consistent with yours. A subsequent discussion of this information should be useful for planning purposes.

UNRESTRICTED CASH AND INVESTMENT BALANCES

The graph below presents the unrestricted cash and investment balances of the governmental funds, and each proprietary fund for the past five years. Cash and investments decreased \$422,312, or 10.4% in the governmental funds, and cash increased \$370,645, or 10.6% in the proprietary funds taken as a whole.

Cash and Investment Balances

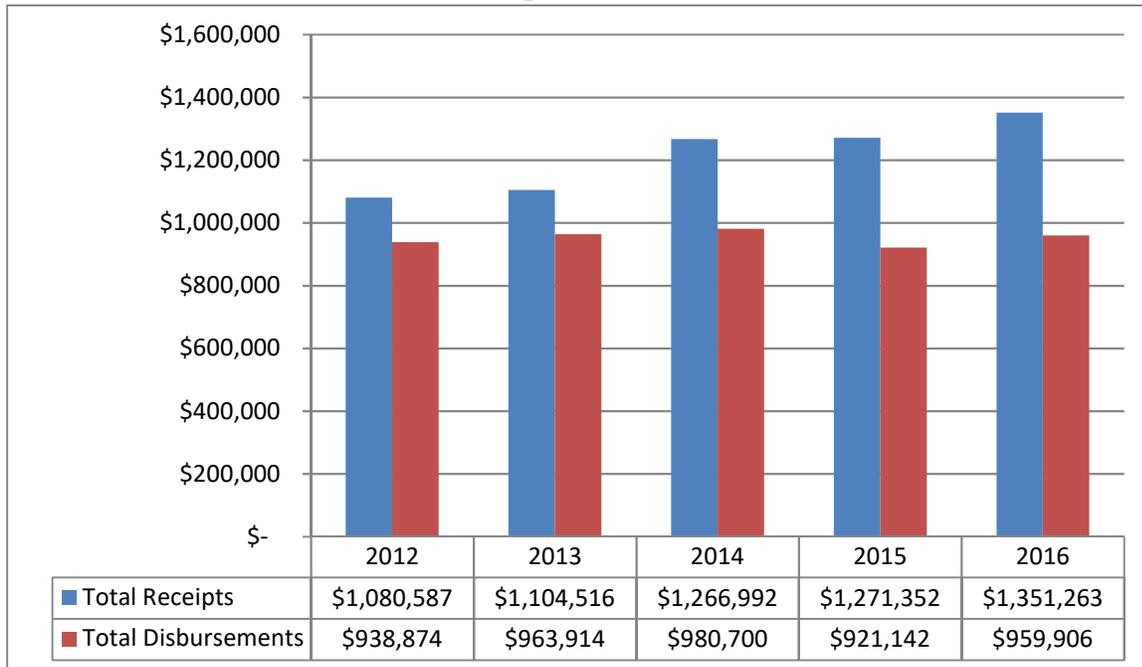


City of Sandstone
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GENERAL FUND – RECEIPTS AND DISBURSEMENTS

As illustrated in the following graph, the general fund receipts and disbursements have fluctuated slightly over the past five years. Revenues have exceeded disbursements every year for the past 5 years. Receipts increased 6.29%, or \$79,911 from 2015 to 2016. This increase was largely due to an increase in intergovernmental revenues and charges for services the City received. Disbursements increased 4.21%, or \$38,764 from 2015 to 2016. This decrease is largely due to the increase in general government disbursements.

General Fund
Receipts and Disbursements



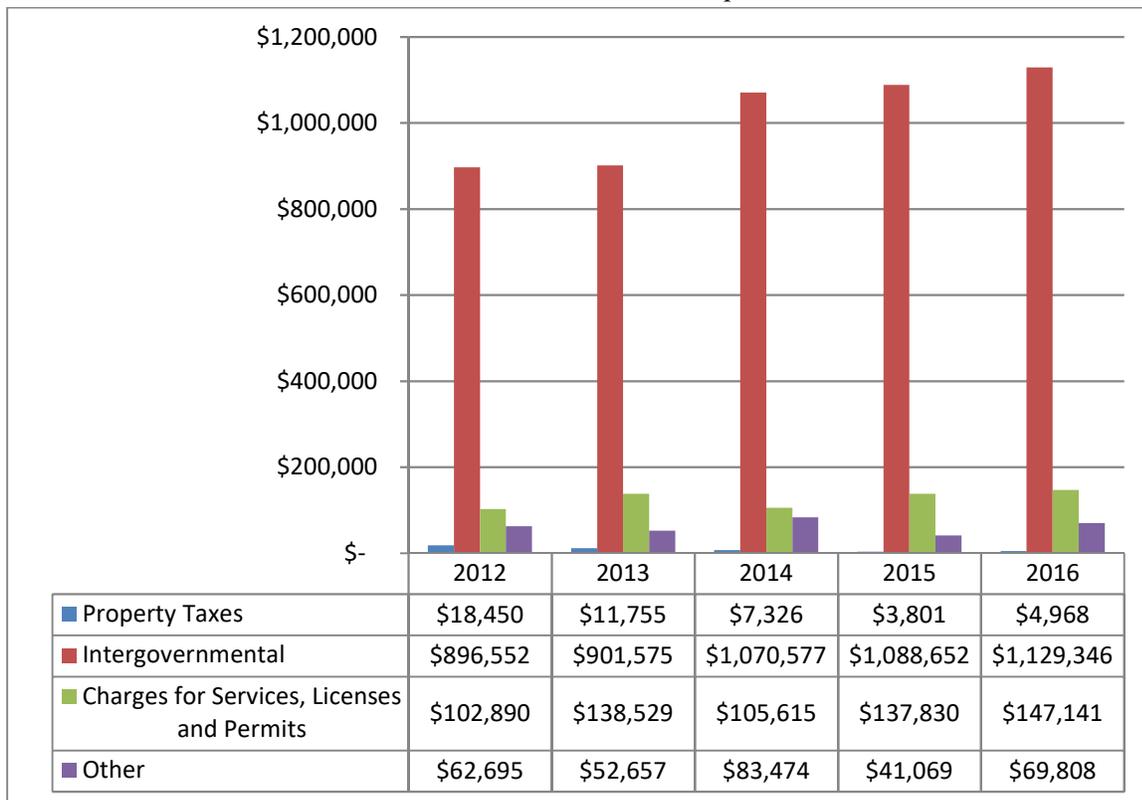
The graphs on the following page outline the sources of the general fund’s receipts and allocation of disbursements. The graph showing receipts for the past five years illustrates the reliance on intergovernmental receipts with significant revenues from the other revenues sources. In 2016, 83.58% of the City’s receipts were intergovernmental receipts. Other revenues include property tax receipts, charges for services, interest revenues, and miscellaneous.

City of Sandstone
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GENERAL FUND – RECEIPTS AND DISBURSEMENTS (Continued)

We recommend the City continue to monitor receipts and disbursements monthly through the financial reporting process and annually through the budget process to ensure continued stable growth of the general fund for future operations. We recommend the City follow a policy targeting a desired cash balance.

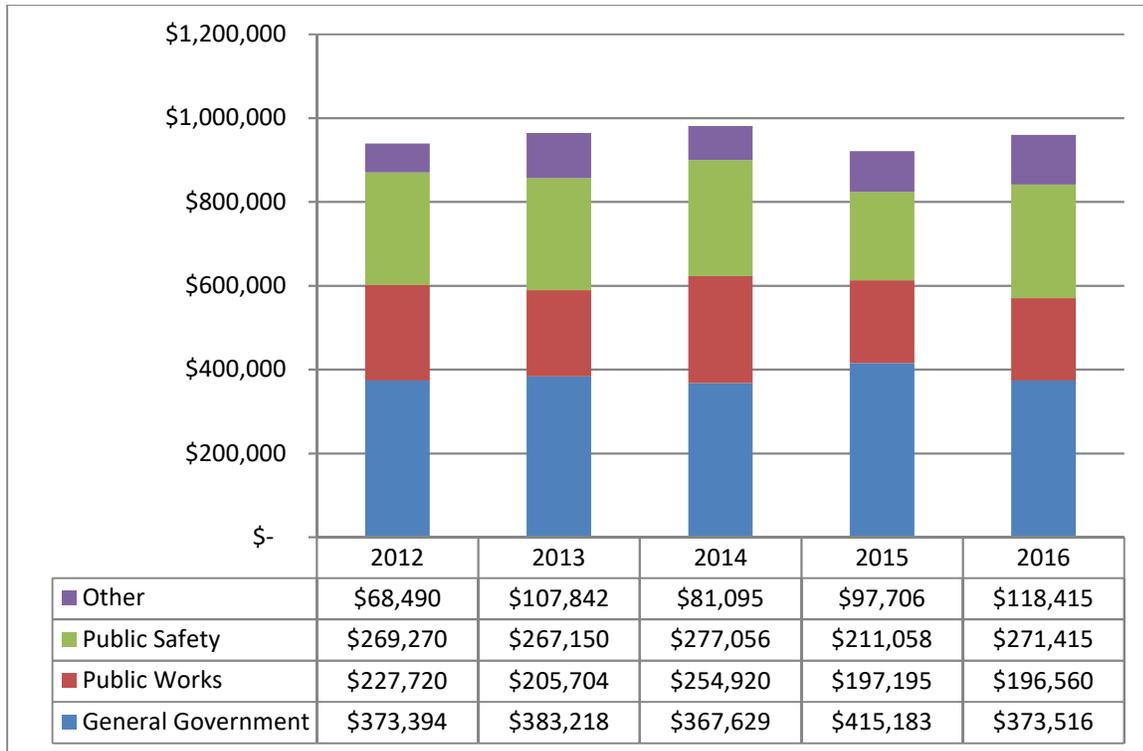
General Fund Receipts



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GENERAL FUND – RECEIPTS AND DISBURSEMENTS (Continued)

General Fund Disbursements

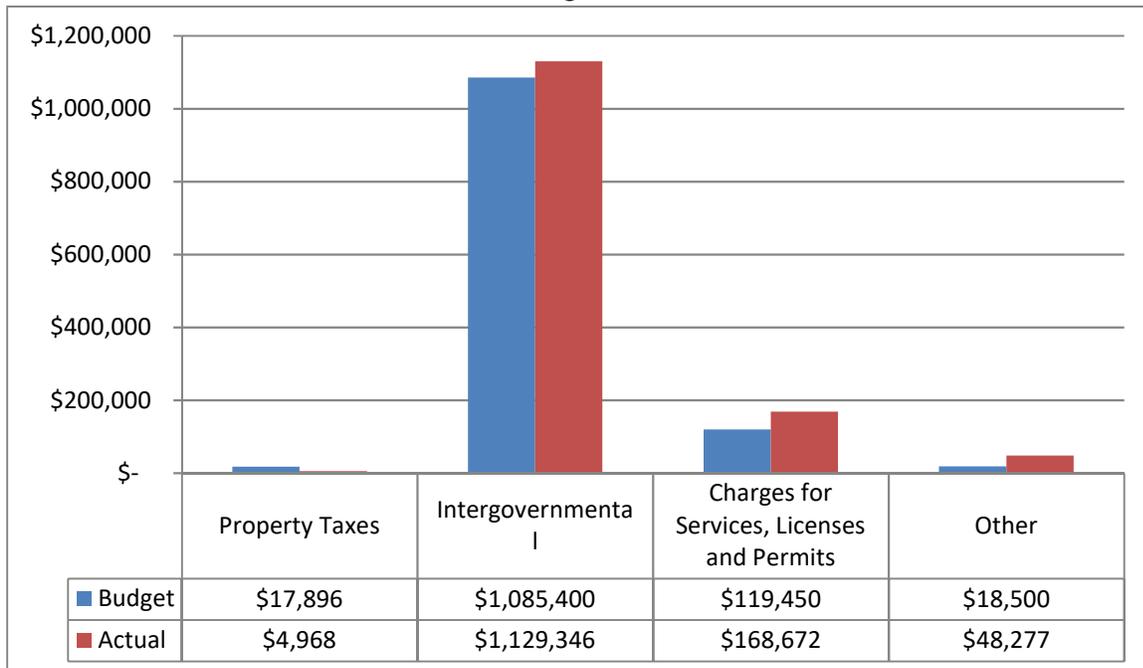


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GENERAL FUND – RECEIPTS BUDGET AND ACTUAL

The following graph below outlines the budget and actual totals for the general fund’s receipts.

**2016 General Fund Receipts
Budget and Actual**



Overall, the City developed an accurate guideline in the budget. The total receipt variance between budget and actual was 8.9%. Property taxes were less than budgeted, while all other areas of sources were greater than budgeted amounts.

The City should continue the budget strategies developed to monitor operations.

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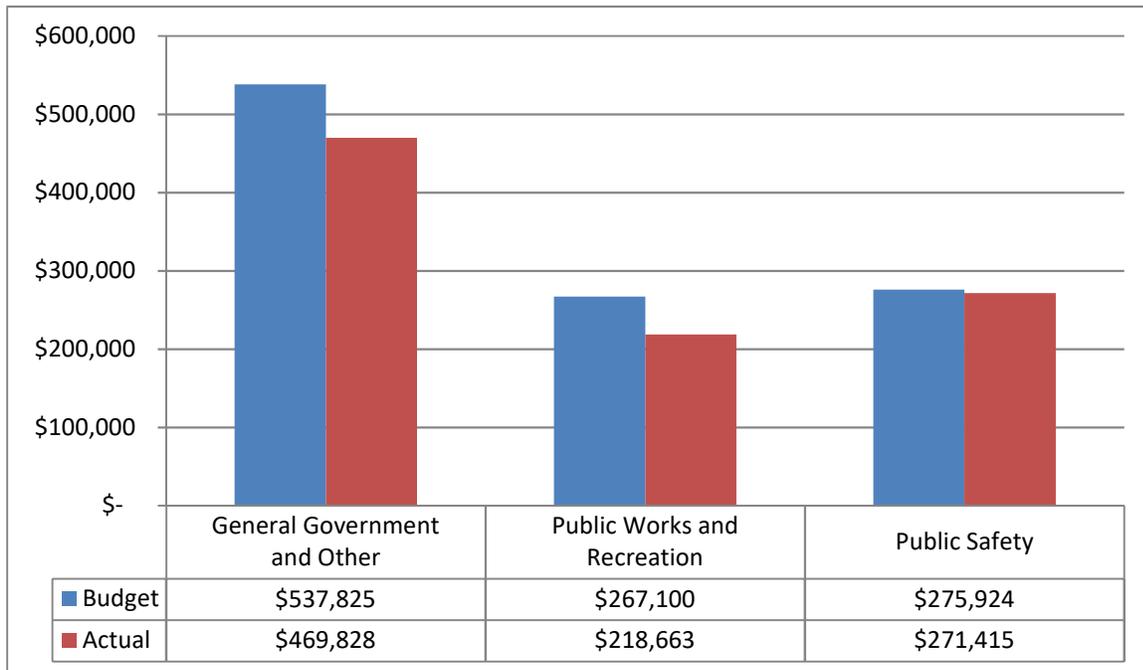
GENERAL FUND – DISBURSEMENTS BUDGET AND ACTUAL

Below is a summary of the budget and actual totals for the general fund’s disbursements.

Disbursements for the general fund resulted in under spending by \$120,943 or a variance of 11.2%. This variance is primarily due to general government expenditures. Public works expenditures were \$48,437 under budget. Public safety expenditures were \$4,509 under budget, and general government expenditures were \$67,997 under budget.

Again, the City should continue the budgeting tactics used in the past. In the end, the City managed an \$271,120 increase in the general fund after accounting for transfers.

2016 General Fund Disbursements
Budget and Actual



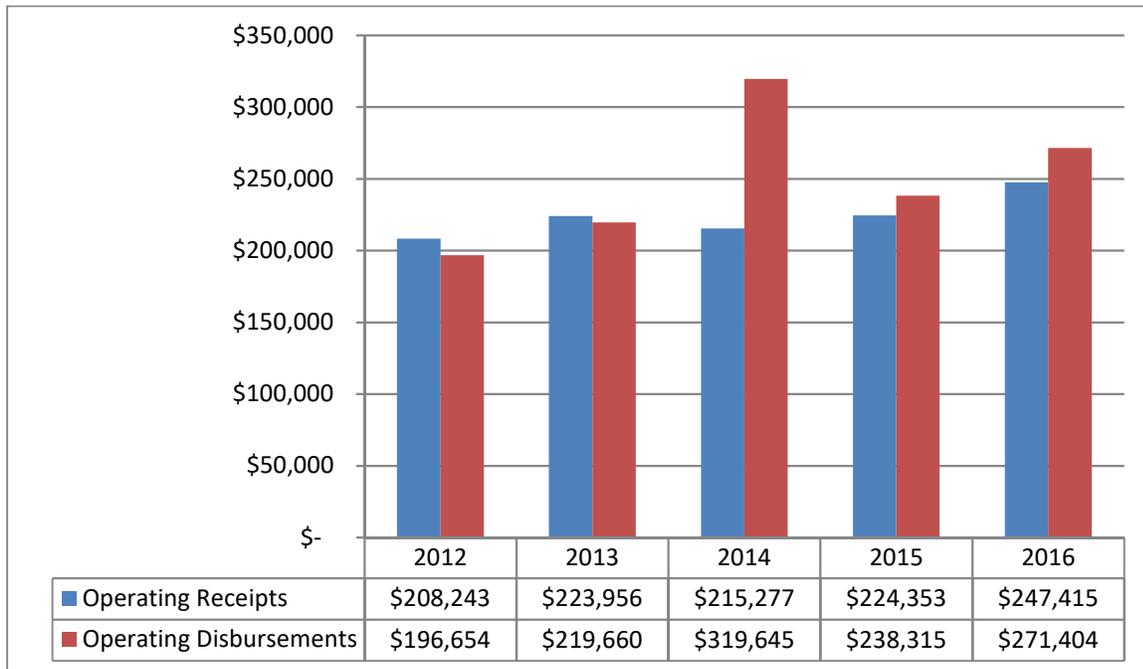
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WATER FUND

Operating expenditures have continually exceeded cash receipts, except for 2012 and 2013, when receipts exceeded expenditures by \$15,885. Water receipts increased \$23,062 from 2015 to 2016 due to increased consumption by customers. Water disbursements increased \$33,089 from 2015 to 2016.

It is important to note that the above notes and the below graphical representation account only for operating revenues and expenditures, and not non-operating revenues and expenses. In 2016 the water fund non-operating activity resulted in \$1,015 in net revenues.

**Water Fund
Receipts and Disbursements**



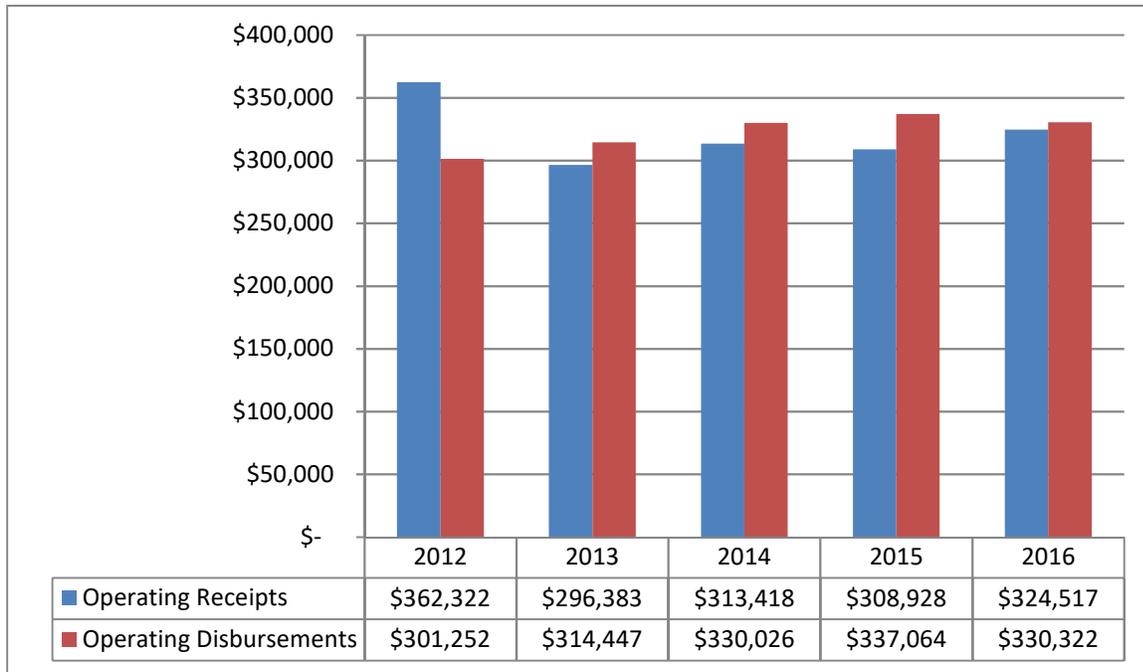
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SEWER FUND

Sewer receipts increased \$15,589 from 2015 to 2016 due to increased usage by customers. Sewer disbursements decreased \$6,742 from 2015 to 2016.

It is important to note that the above notes and the below graphical representation account only for operating revenues and expenditures, and not non-operating revenues and expenses. In 2016 the sewer fund non-operating activity resulting in \$41,295 in net revenues.

Sewer Fund
Receipts and Disbursements



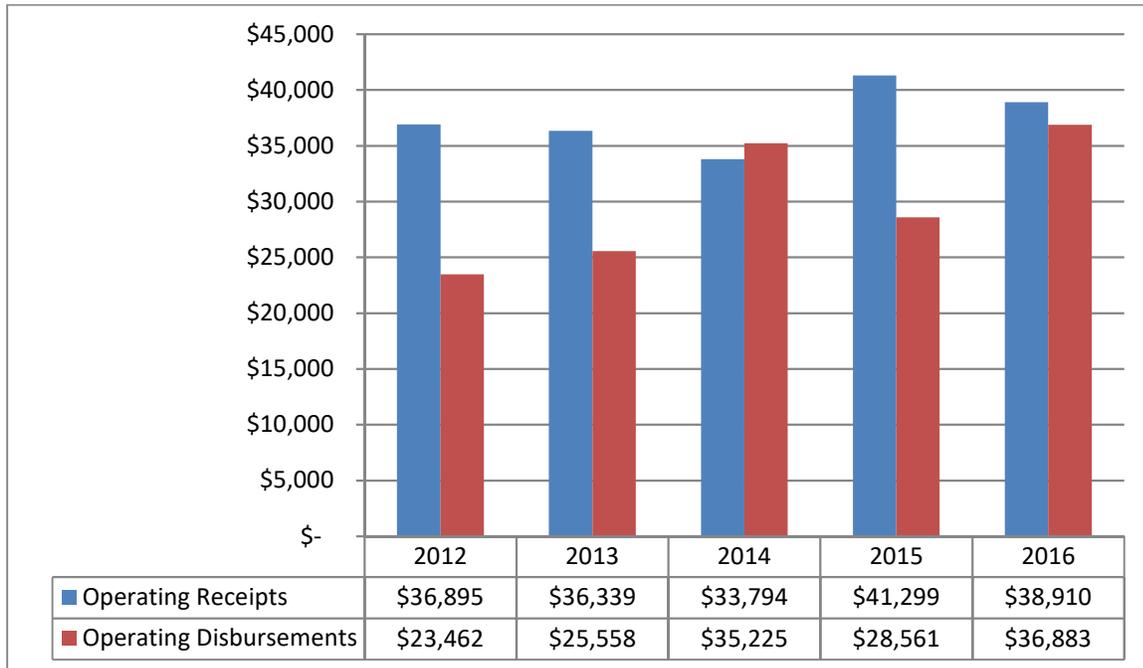
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STORM WATER FUND

Cash receipts have continually exceeded operating disbursements until 2014. Storm water receipts decreased \$2,389 from 2015 to 2016 due to decreased consumption by customers. Storm water disbursements increased \$8,322 from 2015 to 2016.

It is important to note that the above notes and the below graphical representation account only for operating revenues and expenditures, and not non-operating revenues and expenses. In 2016 the storm water fund non-operating activity resulting in \$289 in net revenues.

**Storm Water Fund
Receipts and Disbursements**



City of Sandstone
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WILD RIVER APARTMENT FUND

Cash receipts have exceeded operating disbursements for the past four years. Wild River receipts increased \$27,980 from 2015 to 2016 which indicates a increase in revenues. Wild River disbursements decreased \$82,755 from 2015 to 2016.

It is important to note that the above notes and the below graphical representation account only for operating revenues and expenditures, and not the non-operating revenues and expenses. In 2016 the Wild River fund non-operating activity resulted in \$114,019 in net expenditures.

**Wild River Apartment Fund
Receipts and Disbursements**

