

CITY OF MIDDLESBORO, KENTUCKY

BASIC FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION
YEAR ENDED JUNE 30, 2015
with
REPORT ON INDEPENDENT AUDITORS

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INDEPENDENT AUDITOR'S REPORT

Mayor and Council
City of Middlesboro
Middlesboro, Kentucky

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information, as applicable, of the City of Middlesboro, Kentucky, as of and for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise the basic financial statements of the City's primary government 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. 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.

Summary of Opinions

<u>Opinion Unit</u>	<u>Type of Opinion</u>
Governmental Activities	Adverse
Business-Type Activities	Unmodified
General Fund	Qualified
Sewer Fund	Unmodified
Garbage Fund	Unmodified
Ambulance Fund	Unmodified
Aggregate Remaining Fund Information	Qualified

Basis for Adverse Opinion on Governmental Activities

Generally accepted auditing standards require the auditor to obtain sufficient appropriate audit evidence to ensure that all opinion units are not materially misstated. The City has not presented the Net Pension Liability related to the Kentucky County Employee's Retirement System, or the related deferred inflows and outflows. The City has also failed to present the Net Pension Obligation related to the Police and Firemen's Pension Fund. Consequently, the required supplementary information and notes related to those funds cannot be presented. The City has also failed to properly present information related for the police asset forfeiture account.

Adverse Opinion

In our opinion, because of the significance of the matter discussed in the "Basis for Adverse Opinion on Governmental Activities" the financial statements referred to above do not present fairly the financial position of the City of Middlesboro, Kentucky as of June 30, 2015, or the changes in financial position or cash flows, as applicable, thereof for the year then ended.

Basis for Qualified Opinion on the General Fund and the Aggregate Remaining Fund Information

Accounting principles generally accepted in the United States of America requires certain financial data to be presented and disclosed for all revenues and expenditures. The City has not properly presented data related to the Police Forfeiture accounts and has failed to record receivables related to municipal accounts. Because of this departure from accounting principles generally accepted in the United States of America, the information presented is not complete. The difference, if any, is not known.

In addition, Accounting principles generally accepted in the United States of America requires certain financial data to be presented and disclosed for the Police and Fireman Pension Fund. The City has not presented the data for the fund. Because of this departure from accounting principles generally accepted in the United States of America, the disclosures and required supplemental schedules are incomplete at June 30, 2015.

Qualified Opinions

In our opinion, except for the departures from accounting principles generally accepted in the United States of America and omitted disclosures as discussed in the "Basis for Qualified Opinion on the General Fund" and "Basis for Qualified Opinion on the Aggregate Remaining Fund Information" paragraph, the financial statements referred to above present fairly in all material respects the financial position of the general fund and the aggregate remaining fund information and the City of Middlesboro, Kentucky as of June 30, 2015, and the changes in financial position or cash flows, as applicable, thereof for the year then ended.

Unmodified 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, and each major fund, for the primary government of the City of Middlesboro, Kentucky, as of June 30, 2015, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of a Matter

Additional required supplementary information (RSI) is required due to the mandatory adoption of GASB 68. The RSI has not been presented.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information per the table of contents be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

The management's discussion and analysis and the budgetary comparison information have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

Other Reporting Required by *Governmental Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report, dated July 6, 2018 on our consideration of City of Middlesboro, Kentucky'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 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 internal control over financial reporting or on compliance. The report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering City of Middlesboro, Kentucky's internal control over financial reporting and compliance.

Clayd & Associates, PSC

July 6, 2018
Middlesboro, KY

As management of the City of Middlesboro (City), we offer readers of the City's financial statements this narrative overview and analysis of the financial activities of the City for the fiscal year ended June 30, 2015. We encourage readers to consider the information presented here in conjunction with additional information found within the body of the financial statements and notes.

FINANCIAL HIGHLIGHTS

- The City's ending cash balance was \$1,341,207 comprised of \$90,875 in restricted cash and \$1,250,332 in unrestricted cash. The prior year's cash balance was \$2,001,633 comprised of \$13,695 in restricted cash and \$1,988,138 in unrestricted cash.
- The City's governmental net position decreased by \$627,182 or approximately 3.8% between 2015 and 2014.
- The General Fund had approximately \$4.82 million in revenue, which primarily consisted of tax revenue, fees for services, regulatory fees, and intergovernmental revenue. There was an overall decrease in the General Fund net fund balance of approximately \$161,614 compared to an increase of \$330,756 for 2014. The total overall decrease for governmental funds was \$155,135 for 2013 compared to an increase of \$429,880 for 2013.
- The City's total long-term liabilities increased by \$4,429, relative to 2014 due to a \$130,000 note for a street sweeper. The ending long-term debt balance was \$759,490 including the accrued absences and proprietary leases.

OVERVIEW OF FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the basic financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

Government-wide financial statements. The government-wide financial statements are designed to provide readers with a broad overview of the City's finances, in a manner similar to a private-sector business.

The Statement of Net Position presents information on all the City's assets and liabilities, with the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the City is improving or deteriorating.

The Statement of Activities presents information showing how the City's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future

CITY OF MIDDLESBORO, KENTUCKY

MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)

Year ended June 30, 2015

fiscal periods.

The government-wide financial statements outline functions of the City that are primarily supported by property taxes and intergovernmental revenues (governmental activities). The governmental activities of the City include general government, police department, fire protection, public works, recycling, building inspection, parks and recreation, main street and special projects. Fixed asset acquisitions and related debt are also supported by taxes and intergovernmental revenues. The government-wide financial statements can be found on pages 8 and 9 of this report.

Fund financial statement. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities and objectives. The City uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City can be divided into three categories: governmental, proprietary, and fiduciary funds. Fiduciary funds are trust funds established by benefactors to provide benefits for employees. The City has no proprietary funds. All other activities of the City are included in the governmental funds.

The basic governmental fund financial statements can be found on pages 10 through 18 of this report.

Notes to the financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the governmental-wide and fund financial statements. The notes to the financial statements can be found on pages 19 through 34 of this report.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Net assets may serve over time as a useful indicator of a government's financial position. In the case of the City, governmental assets exceeded liabilities by approximately \$16.34 Million. The largest portion of the City's net assets reflects its investment in capital assets (e.g., land and improvements, buildings and improvements, vehicles, furniture and equipment and construction in progress); less any related debt used to acquire those assets that are still outstanding. The City uses these capital assets to provide services to its citizens; consequently, these assets are not available for future spending. Although the City's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities. The City's financial position is the product of several financial transactions including the net results of activities, the acquisition and payment of debt, the acquisition and disposal of capital assets, and the depreciation of capital assets.

The City as a Whole

The following is a summary of the City's net assets:

CITY OF MIDDLESBORO, KENTUCKY

MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)

Year ended June 30, 2015

	<u>2015</u>	<u>2014</u>
Current and other assets	\$ 1,844,624	\$ 2,396,443
Capital assets, net	<u>15,276,069</u>	<u>15,309,206</u>
Total assets	<u>17,120,693</u>	<u>17,705,649</u>
Current liabilities	812,572	745,008
Noncurrent liabilities	<u>594,839</u>	<u>620,175</u>
Total liabilities	<u>1,407,411</u>	<u>1,365,183</u>
Investment in capital assets, net of related debt	14,682,289	14,564,597
Restricted net assets	91,085	84,682
Unrestricted net assets	<u>939,908</u>	<u>1,691,187</u>
Total net assets	<u>\$ 15,713,282</u>	<u>\$ 16,340,466</u>

The following table presents a fund accounting comparison and summary of revenue and expense for Government Funds only for fiscal years 2015 and 2014:

	2015	2014
REVENUES		
Taxes	\$ 3,274,621	\$ 3,728,823
Licenses, permits, and fees	680,379	640,793
Intergovernmental programs	581,654	411,484
Fines and forfeits	38,878	21,345
Other	<u>598,892</u>	<u>261,600</u>
Total revenue	<u>5,174,424</u>	<u>5,064,045</u>
EXPENDITURES		
General government	1,086,110	951,190
Public safety	3,600,369	3,867,896
Highways and streets	1,284,701	1,284,761
Debt service	115,054	109,462
Capital outlay	<u>271,765</u>	<u>80,616</u>
Total expenditures	<u>6,357,999</u>	<u>6,293,925</u>
Excess revenues/(expenditures)	(1,183,575)	(1,229,880)
Other financing sources and uses		
Proceeds from debt	130,000	-
Transfers in	<u>898,440</u>	<u>800,000</u>
Total other financing sources and uses	<u>1,028,440</u>	<u>800,000</u>
Net change in fund balance	<u>\$ (155,135)</u>	<u>\$ (429,880)</u>

CITY OF MIDDLESBORO, KENTUCKY

MANAGEMENT'S DISCUSSION AND ANALYSIS (MD&A)

Year ended June 30, 2015

General Fund Revenue

The majority of revenue, net of debt, was derived from tax revenue (63% in 2015 and 79% in 2014). License, permits, and fees made up 14% of revenue in 2015 and 13% in 2014.

BUDGETARY IMPLICATION

The City's fiscal year is July 1 - June 30; other programs, i.e., some federal programs operate on a different fiscal calendar, but are reflected in the City's overall budget. Significant events that may impact the finances include expected state budget deficits that may impact grant or other revenue. The City routinely attempts to keep expenditures to a minimum because of the anticipated revenue problems. The City's budget was not exceeded in the current year.

Questions regarding this report should be directed to the Middlesboro City Clerk, PO Box 756, Middlesboro, Kentucky, 40965.

City of Middlesboro, Kentucky
Statement of Net Position
June 30, 2015

	<u>Governmental Activities</u>	<u>Business-Type Activities</u>	<u>Total</u>
Current Assets			
Cash	\$ 471,909	\$ 778,423	\$ 1,250,332
Accounts receivable, net			
Taxes		-	-
Other	2,500	495,118	497,618
Inventory	-	5,799	5,799
Total Current Assets	<u>474,409</u>	<u>1,279,340</u>	<u>1,753,749</u>
Noncurrent Assets			
Restricted cash	90,875	-	90,875
Capital assets, net of accumulated depreciation	<u>8,556,042</u>	<u>6,720,027</u>	<u>15,276,069</u>
Total Noncurrent Assets	<u>8,646,917</u>	<u>6,720,027</u>	<u>15,366,944</u>
Total Assets	<u>9,121,326</u>	<u>7,999,367</u>	<u>17,120,693</u>
Liabilities			
Current liabilities			
Accounts payable	72,812	155,333	228,145
Accrued liabilities	86,904	20,562	107,466
Compensated absences	241,262	64,390	305,652
Accrued interest	6,658	-	6,658
Bonds and notes payable	123,871	-	123,871
Leases payable	-	40,780	40,780
Total current liabilities	<u>531,507</u>	<u>281,065</u>	<u>812,572</u>
Non current liabilities			
Bonds and notes payable	429,129	-	429,129
Leases payable	-	-	-
Compensated absences	<u>165,710</u>	<u>-</u>	<u>165,710</u>
Total non-current liabilities	<u>594,839</u>	<u>-</u>	<u>594,839</u>
Total liabilities	<u>1,126,346</u>	<u>281,065</u>	<u>1,407,411</u>
Net Position			
Invested in capital assets, net of related debt	8,003,042	6,679,247	14,682,289
Restricted for:			
Debt service	13,210	-	13,210
Other	77,875	-	77,875
Unrestricted	<u>(99,147)</u>	<u>1,039,055</u>	<u>939,908</u>
Total Net Position	<u>\$ 7,994,980</u>	<u>\$ 7,718,302</u>	<u>\$ 15,713,282</u>

City of Middlesboro, Kentucky
Balance Sheet - Governmental Funds
June 30, 2015

	<u>General Fund</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Assets			
Cash	\$ 471,909	\$ -	\$ 471,909
Restricted cash	13,210	77,665	90,875
Accounts receivable, net			
Tax and license	-	-	-
Other	<u>2,500</u>	<u>-</u>	<u>2,500</u>
Total Assets	<u>\$ 487,619</u>	<u>\$ 77,665</u>	<u>\$ 565,284</u>
Liabilities and Fund Balances			
Liabilities			
Accounts payable	93,554	-	93,554
Accrued liabilities	<u>322,989</u>	<u>-</u>	<u>322,989</u>
Total Liabilities	<u>416,543</u>	<u>-</u>	<u>416,543</u>
Fund Balances			
Restricted	13,210	77,665	90,875
Unassigned	<u>57,866</u>	<u>-</u>	<u>57,866</u>
Total Fund Balances	<u>71,076</u>	<u>77,665</u>	<u>148,741</u>
Total Liabilities and Fund Balances	<u>\$ 487,619</u>	<u>\$ 77,665</u>	<u>\$ 565,284</u>

City of Middlesboro, Kentucky
 Reconciliation of the Balance Sheet - Governmental Funds
 to the Statement of Net Position
 June 30, 2015

Total fund balance per fund financial statements	\$ 148,739
<p>Amounts reported for governmental activities in the statement of net position are different because:</p>	
<p>Capital assets are not reported in this fund financial statement because they are not current financial resources, but they are reported in the statement of net position.</p>	8,556,042
<p>Certain assets are not reported in this fund financial statements because they are not current financial resources, but they are reported in the statement of net position</p>	-
<p>Bonds payable are not reported in this fund financial statement because they are not due and payable, but they are presented in the statement of net position.</p>	(553,000)
<p>Certain liabilities (such as long-term portion of compensated absences and accrued interest) are not reported in this fund financial statement because they are not due and payable, but they are presented in the statement of net position</p>	<u>(156,801)</u>
<p>Net Position For Governmental Activities</p>	<u>\$ 7,994,980</u>

City of Middlesboro, Kentucky
Statement of Revenues, Expenditures and Changes In
Fund Balances - Governmental Funds
For the Year Ended June 30, 2015

	General Fund	Other Governmental Funds	Total Governmental Funds
Revenue			
Taxes	\$ 3,724,621	\$ -	\$ 3,724,621
Licenses and permits	680,379	-	680,379
Fines and forfeits	38,978	-	38,978
Interest income	453	121	574
Rental income	7,785	-	7,785
Intergovernmental programs	249,530	332,124	581,654
Miscellaneous income	140,433	-	140,433
Total revenue	<u>4,842,179</u>	<u>332,245</u>	<u>5,174,424</u>
Expenditures			
General government	1,063,230	22,880	1,086,110
Public safety	3,600,369	-	3,600,369
Highways and streets	1,141,815	142,886	1,284,701
Debt service	115,054	-	115,054
Capital outlay	271,765	-	271,765
Total Expenditures	<u>6,192,233</u>	<u>165,766</u>	<u>6,357,999</u>
Excess of Revenues Over (Under) Expenditures	(1,350,054)	166,479	(1,183,575)
Other Financing Sources (Uses)			
Proceeds from bond	130,000	-	130,000
Proceed from sale of fixed assets	-	-	-
Operating transfers in (out)	1,058,440	(160,000)	898,440
Total Other Financing Sources (Uses)	<u>1,188,440</u>	<u>(160,000)</u>	<u>1,028,440</u>
Net Change in Fund Balance	(161,614)	6,479	(155,135)
Fund Balance July 1, 2014	<u>232,689</u>	<u>71,187</u>	<u>303,876</u>
Fund Balance June 30, 2015	<u>\$ 71,075</u>	<u>\$ 77,666</u>	<u>\$ 148,741</u>

City of Middlesboro, Kentucky
 Reconciliation of the Statement of Revenues, Expenditures and
 Changes in Fund Balances of Governmental Funds to the Statement of Activities
 For the Year Ended June 30, 2015

Net Changes in Total Fund Balances Per Fund Financial Statements	\$ (155,135)
Amounts reported for governmental activities in the statement of activities are different because:	
Governmental funds report capital outlays as expenditures because they use current financial resources. However in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which depreciation expense exceeds capital outlays for the year.	155,745
Generally , expenditures recognized in this fund financial statement are limited to only those that use current financial resources, but expenses are recognized in the statement of revenues, expenses, and changes in net position when they are incurred	(7,836)
Payments for notes and leases are reported as expenditures in governmental funds and thus contribute to the change in fund balance. In the statement of net assets however, repayment of long-term debt reduces the liability and does not affect the statement of activities.	<u>34,000</u>
Changes in Net Position of Governmental Activities	<u>\$ 26,774</u>

City of Middlesboro, Kentucky
Statement of Net Position - Proprietary Funds
June 30, 2015

	Sewer	Garbage	Ambulance	Total Proprietary Funds
Current Assets				
Cash	\$ 445,740	\$ 38,169	\$ 294,514	\$ 778,423
Accounts receivable, net	180,285	56,004	258,829	495,118
Inventory	5,799	-	-	5,799
Total Current Assets	<u>631,824</u>	<u>94,173</u>	<u>553,343</u>	<u>1,279,340</u>
Noncurrent Assets				
Restricted cash	-	-	-	-
Capital assets, net of accumulated depreciation	6,438,592	-	281,435	6,720,027
Total Noncurrent Assets	<u>6,438,592</u>	<u>-</u>	<u>281,435</u>	<u>6,720,027</u>
Total Assets	<u>\$ 7,070,416</u>	<u>\$ 94,173</u>	<u>\$ 834,778</u>	<u>\$ 7,999,367</u>
Current Liabilities				
Capital leases	\$ -	\$ -	\$ 40,780	\$ 40,780
Accounts payable	14,998	135,519	4,816	155,333
Accrued expenses	12,715	-	7,847	20,562
Compensated absences	54,842	-	9,548	64,390
Total Current Liabilities	<u>82,555</u>	<u>135,519</u>	<u>62,991</u>	<u>281,065</u>
Noncurrent Liabilities				
Capital leases	-	-	-	-
Compensated absences	-	-	-	-
Total Noncurrent Liabilities	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total Liabilities	82,555	135,519	62,991	281,065
Net Position				
Invested in capital assets, net of related debt	6,987,861	-	240,655	7,228,516
Restricted for debt service	-	-	-	-
Unrestricted	-	(41,346)	531,132	489,786
Total Net Position	<u>\$ 6,987,861</u>	<u>\$ (41,346)</u>	<u>\$ 771,787</u>	<u>\$ 7,718,302</u>

City of Middlesboro, Kentucky
Statement of Revenues, Expenses, and Changes in
Net Position - Proprietary Funds
For the Year Ended June 30, 2015

	Sewer	Garbage	Ambulance	Total Proprietary Funds
Operating Revenues				
Charges for services	\$ 1,373,005	\$ 352,087	\$ 1,150,664	\$ 2,875,756
Intergovernmental revenue	-	-	-	-
Other income	-	-	-	-
Total Operating Revenue	<u>1,373,005</u>	<u>352,087</u>	<u>1,150,664</u>	<u>2,875,756</u>
Operating Expense				
Salaries	453,263	-	254,688	707,951
Engineering	8,340	398,516	-	406,856
Rescue squad	-	-	15,000	15,000
Depreciation	412,776	-	36,630	449,406
Repairs & Maintenance	111,501	-	27,284	138,785
Utilities	209,326	-	-	209,326
Chemicals	56,982	-	-	56,982
Employee benefits	54,801	-	11,068	65,869
Retirement expense	78,424	-	44,662	123,086
Payroll taxes	32,204	-	15,762	47,966
Insurance	25,000	-	10,541	35,541
Supplies	27,384	-	74,728	102,112
Professional fees	-	-	-	-
Testing	24,904	-	-	24,904
Telephone	5,585	-	-	5,585
Equipment rental	-	-	-	-
Fuel	27,171	-	46,774	73,945
Uniforms	5,626	-	9,275	14,901
Travel	4,597	-	990	5,587
Taxes	42,455	-	-	42,455
Dumping expenses	4,338	-	-	4,338
Billing expense	-	-	60,251	60,251
Other operating expenses	21,920	-	-	21,920
Other general expenses	6,392	-	10,498	16,890
Total Operating Expenses	<u>1,612,989</u>	<u>398,516</u>	<u>618,151</u>	<u>2,629,656</u>
Operating Income (Loss)	<u>(239,984)</u>	<u>(46,429)</u>	<u>532,513</u>	<u>246,100</u>
Other Revenues (Expenses)				
Interest revenue	1,166	83	1,017	2,266
Interest expense	-	-	(3,882)	(3,882)
Total Other Revenues (Expenses)	<u>1,166</u>	<u>83</u>	<u>(2,865)</u>	<u>(1,616)</u>
Income (loss) before transfers	(238,818)	(46,346)	529,648	244,484
Transfers (to) / from governmental activities	<u>(393,440)</u>	<u>-</u>	<u>(505,000)</u>	<u>(898,440)</u>
Net Income (Loss)	(632,258)	(46,346)	24,648	(653,956)
Net Position , July 1, 2013	<u>7,620,119</u>	<u>5,000</u>	<u>747,139</u>	<u>8,372,258</u>
Net Position, June 30, 2014	<u>\$ 6,987,861</u>	<u>\$ (41,346)</u>	<u>\$ 771,787</u>	<u>\$ 7,718,302</u>

City of Middlesboro, Kentucky
Statement of Cash Flows - Proprietary Funds
For the Year Ended June 30, 2015

	Sewer	Garbage	Ambulance	Total Proprietary Funds
Cash Flows From Operating Activities				
Receipts from customers	\$ 1,262,991	\$ 340,920	\$ 1,165,739	\$ 2,769,650
Payments for goods and services	<u>(1,181,898)</u>	<u>(363,539)</u>	<u>(563,165)</u>	<u>(2,108,602)</u>
Net Cash Provided (Used) by Operating Activities	<u>81,093</u>	<u>(22,619)</u>	<u>602,574</u>	<u>661,048</u>
Cash Flows From Noncapital Financing Activities				
Transfers (to) from other funds	<u>(393,440)</u>	<u>-</u>	<u>(505,000)</u>	<u>(898,440)</u>
Net Cash Provided (Used) by Noncapital Financing Activities	<u>(393,440)</u>	<u>-</u>	<u>(505,000)</u>	<u>(898,440)</u>
Cash Flows From Capital Financing Activities				
Proceeds from debt	-	-	-	-
Acquisition and construction of capital assets	(113,944)	-	(146,582)	(260,526)
Principal and interest paid on debt	<u>-</u>	<u>-</u>	<u>(42,768)</u>	<u>(42,768)</u>
Net Cash Used by Capital Financing Activities	<u>(113,944)</u>	<u>-</u>	<u>(189,350)</u>	<u>(303,294)</u>
Cash Flows From Investing Activities				
Interest	<u>1,166</u>	<u>83</u>	<u>1,017</u>	<u>2,266</u>
Net Cash Provided by Investing Activities	<u>1,166</u>	<u>83</u>	<u>1,017</u>	<u>2,266</u>
Net Decrease in Cash	(425,125)	(22,536)	(90,759)	(538,420)
Cash - July 1, 2014	<u>870,865</u>	<u>60,705</u>	<u>385,273</u>	<u>1,316,843</u>
Cash - June 30, 2015	<u>\$ 445,740</u>	<u>\$ 38,169</u>	<u>\$ 294,514</u>	<u>\$ 778,423</u>
Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities:				
Operating income (loss)	\$ (239,984)	\$ (46,429)	\$ 532,513	\$ 246,100
Adjustments to reconcile operating income (loss) to net cash from operating activities:				
Depreciation	412,776	-	36,630	449,406
Net change in pension expense	-	-	-	-
(Increase) Decrease in:				
Accounts receivable	(110,014)	(11,167)	15,075	(106,106)
Inventory	-	-	-	-
Undeposited funds	-	-	-	-
Increase (Decrease) in:				
Accounts payable	8,231	34,977	961	44,169
Compensated absences	5,091	-	9,548	14,639
Accrued expenses	<u>4,993</u>	<u>-</u>	<u>7,847</u>	<u>12,840</u>
Net Cash Provided (Used) by Operating Activities	<u>\$ 81,093</u>	<u>\$ (22,619)</u>	<u>\$ 602,574</u>	<u>\$ 661,048</u>

See notes to the financial statements.

City of Middlesboro, Kentucky
Statement of Fiduciary Net Position - Fiduciary Funds
For the Year Ended June 30, 2015

	<u>P&F Pension Fund</u>
ASSETS	
Cash and cash equivalents	\$ 153,677
Investments	1,047,966
Receivables	
Interest	<u>-</u>
Total Assets	<u>1,201,643</u>
LIABILITIES	
Due to agencies	-
Total Liabilities	<u>-</u>
NET POSITION	
Held in trust for pension benefits	<u>\$ 1,201,643</u>

City of Middlesboro, Kentucky
Statement of Changes in Fiduciary Net Position - Fiduciary Funds
For the Year Ended June 30, 2015

	P&F Pension Fund
ADDITIONS	
Tax revenue	\$ -
Employee contributions	-
Interest	12,663
Other	-
Total revenues	12,663
 DEDUCTIONS	
Benefits	231,677
Plan administration	-
Total expenditures	231,677
 Increase/(Decrease) in net assets	(219,014)
 Net Assets, July 1, 2014	1,420,657
 Net Position Held in Trust for Pension Benefits, June 30, 2015	\$ 1,201,643

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED

Year ended June 30, 2015

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. The financial reporting entity

The City of Middlesboro, Kentucky is Home-Rule city and operates under a Mayor-Council form of government. The City's major operations include public safety, fire protection, public works, recreation and parks, and general administrative services. The accounting policies of the City of Middlesboro, Kentucky conform to generally accepted accounting principles applicable to governmental units. The following is a summary of the more significant accounting policies.

The financial statements of the City of Middlesboro, Kentucky include the funds, activities and entities over which the Mayor and Council exercise significant responsibility. Oversight responsibility, as defined by Section 2100 of the *GASB Codification of Governmental Accounting and Financial Reporting Standards*, was determined on the basis of the City's ability to significantly influence operations, select the governing body, and participate in fiscal management and scope of public service.

The City's basic financial statements include all the accounts of the city including any component units. The criteria for including organizations as component units within the City's reporting entity is set forth in Section 2100 of *GASB Codification of Governmental Accounting and Financial Reporting Standards* and primarily includes those organizations over which the City exercises significant operational or functional control. The criteria include whether:

- The organization is legally separate (can sue or be sued in their own name)
- The City holds the corporate powers of the organization
- The City appoints a voting majority of the organization's board
- The City can impose its will on the organization
- The organization has the potential to impose a financial benefit or burden on the City
- The organization is fiscally dependent on the City

Based on the criteria listed above, the City does not have any component units.

B. Basic financial statements

In accordance with *GASB Statement No. 34, Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*, the basic financial statements include both government-wide and fund financial statements.

The government-wide financial statements (Statement of Net Position and Statement of Activities) generally report on the City and its component units, excluding fiduciary activities. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, if any, which rely to a significant extent on fees and charges for support. All activities, both governmental and business-type, are reported in the government-wide financial statements using the economic resources measurement focus and the accrual basis of accounting, which includes long-term assets and receivables as well as long-term debt and obligations. The government-wide financial statements focus more on the sustainability of the City as an entity and the change in aggregate financial position resulting from the activities of the fiscal period.

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED

Year ended June 30, 2015

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Generally, the effect of interfund activity has been removed from the government-wide financial statements. Net interfund activity and balances between governmental activities and business-type activities are shown in the government-wide financial statements.

The government-wide Statement of Net Position reports all financial and capital resources of the City (excluding fiduciary funds). It is displayed in a format of assets less liabilities equals net position, with the assets and liabilities shown in order of their relative liquidity. Net position is required to be displayed in three components: 1) Net investment in capital assets, 2) restricted, and 3) unrestricted. Net investment in capital assets is capital assets net of accumulated depreciation and reduced by outstanding balances of any bonds, mortgages, notes or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. Restricted net assets are those with constraints placed on their use by either: 1) externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments, or 2) imposed by law through constitutional provisions or enabling legislation. All net assets not otherwise classified as restricted, are shown as unrestricted. Generally, the City would first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

The government-wide Statement of Activities presents a comparison between direct expenses and program revenues for each function or program of the City's governmental activities. Direct expenses are those that are specifically associated with a service, program, or function. The City does not charge indirect expense to programs or functions. Interest on general long-term bonded debt is not allocated to the various functions, and interest on capital leases may be allocated to various functions. Program revenues include: 1) charges paid by the recipients of the goods, services, or privileges offered by the program and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a function or program. Taxes, unrestricted investment income and other revenues not identifiable with particular functions or programs are included as general revenues. The general revenues support the net costs of the functions and programs not covered by program revenues.

Also, part of the basic financial statements are fund financial statements for governmental funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. The City does not have any proprietary funds except in discretely presented component units (business-type activities in the government-wide financial statements). The focus of the fund financial statements is on major funds, as defined by GASB Statement No. 34. Although this reporting model sets forth minimum criteria for determination of major funds (a percentage of assets, liabilities, revenues, or expenditures/expenses of fund category and of the governmental and enterprise funds combined), it also gives governments the option of displaying other funds as major funds.

Governmental Funds

The City reports the following governmental funds:

General Fund – The general fund is the City's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund. The General Fund is a major fund.

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED

Year ended June 30, 2015

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

The Special Revenue Funds are used to account for the proceeds of specific revenue sources (other than special assessments, expendable trusts, or major capital projects) that are restricted by law to be expended for specific purposes. The following Special Revenue Funds are maintained by the City:

Municipal Road Aid Fund – A special revenue fund to account for money received from the State of Kentucky to be used exclusively for repair of roads.

LGEA Fund – A special revenue fund used to account for the Local Government Economic Assistance activity.

Proprietary Fund Types

Proprietary Funds are maintained on the accrual basis of accounting. Proprietary funds apply all statements of the Financial Accounting Standards Board issued after November 30, 1989, as they relate to business enterprises unless they contradict existing Government Accounting Standards Board pronouncements. The City's enterprise operations include sewer, sanitation services, and ambulance services.

Sewer Fund – The sewer fund reports activities which are financed and operated in a manner similar to private business enterprise where the intent of the governing body is that the costs of providing services to the general public on a continuing basis be financed or recorded primarily through user charges. City employees perform sewer operations. The City and the local water utility agreed to combine utility billing and collection services. The sewer fund is a major fund.

Sanitation Fund – The sanitation fund reports activities which are financed and operated in a manner similar to private business enterprise where the intent of the governing body is that the costs of providing services to the general public on a continuing basis be financed or recorded primarily through user charges. The City has contracted with an outside provider to perform sanitation services. The City and the local water utility agreed to combine utility billing and collection services.

Ambulance Fund – The ambulance fund is financed by fees earned from emergency transport. The City has contracted with an outside provider to perform the billing function. Employees of the city's fire department provided the services. The employment cost associated with this service is recorded and paid by the general fund. No formal determination is made to allocated salaries and benefits to the ambulance fund; however, the City annually budgets and transfers funds from the Ambulance fund to offset operational costs in the general fund the ambulance fund is a major fund.

Fiduciary Funds

Pension Trust Funds – The pension trust funds account for assets held on behalf of City employees.

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED

Year ended June 30, 2015

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

C. Measurement focus and basis of accounting

The governmental fund financial statements are prepared on a current financial resources measurement focus and modified accrual basis of accounting. To conform to the modified accrual basis of accounting, certain modifications must be made to the accrual method. These modifications are outlined below:

- A. Revenue is recorded when it becomes both measurable and available (received within 60 days after year-end). Revenue considered susceptible to accrual includes: property taxes, licenses, fees and permits, intergovernmental revenues charges for services, fines, forfeits and penalties, and interest.
- B. Expenditures are recorded when the related fund liability is incurred. Principal and interest on general long-term debt are recorded as fund liabilities when due or when amounts have been accumulated in the debt service fund for payments to be made early in the following year.
- C. Disbursements for the purchase of capital assets providing future benefits are considered expenditures. Debt proceeds and cost are reported as other financing sources.

With this measurement focus, operating statements present increases and decreases in net current assets and unreserved fund balance as a measure of available resources.

This is the traditional basis of accounting for governmental funds and also is the manner in which these funds are normally budgeted. This presentation is deemed most appropriate to; 1) demonstrate legal and covenant compliance, 2) demonstrate the sources and uses of liquid resources, and 3) demonstrate how the City's actual revenues and expenditures conform to the annual budget. Since the governmental funds financial statements are presented on a different basis than the governmental activities column of the government-wide financial statements, reconciliation is provided immediately following each fund statement. These reconciliations briefly explain the adjustments necessary to transform the fund financial statements into the governmental activities column of the government-wide financial statements.

D. Cash and cash equivalents and investments

For purposes of the basic financial statements, the City considers cash and cash equivalents to be all demand deposits, all certificates of deposit, and highly liquid, short-term security investments that are readily convertible to known amounts of cash and mature within three months of the date they are acquired. Deposits (cash and investments) are carried at cost which approximates market value. The carrying amount of all deposits is separately displayed on the balance sheet depending on the terms of the deposit. Restricted cash and investments are separately displayed on the balance sheet.

The City of Middlesboro, Kentucky is authorized by state statute to invest in:

1. Obligations of the United States and of its agencies and instrumentalities;
2. Bonds or certificates of indebtedness of this state and of its agencies and

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED

Year ended June 30, 2015

Instrumentalities;

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

3. Shares of any savings and loan association insured by an agency of the government of the United States up to the amount so insured;
4. Interest bearing deposits in nationally chartered or state banks chartered in Kentucky and insured by an agency of the government of the United States up to the amount so insured, and in large amounts provided such bank shall pledge as security obligations of the United States government, its agencies and instrumentalities. Investments are stated as cost or amortized cost, which approximates market.

E. Receivables

All trade receivables are shown net of an allowance for uncollectible accounts and estimated refunds. In the ambulance fund, the City considers the following to be uncollectible; 1) all accounts turned over the district court for collection, 2) all private pay accounts over 90 days old, 3) 40% of all claims billed to Medicare, and 4) 90% of all Medicaid claims. As of June 30, 2015, the net receivable less allowance for uncollectible accounts for business-type activities was 495,118

F. Prepaid expenses

Certain prepayments to vendors reflect cost applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

G. Restricted assets

Certain grant proceeds, as well as funds set aside for the repayment of bonds or restricted by enabling legislation may be classified as restricted on the balance sheet and statement of net assets, because they are maintained in separate bank accounts or their use is limited by applicable grant agreements or debt covenants.

H. Capital assets

Under Governmental Accounting Standards Board Statement No. 34 (GASB-34), all capital assets, whether owned by governmental activities or business-type activities, as applicable, are recorded and depreciated in the government-wide financial statements. No capital assets or depreciation are shown in the governmental funds financial statements. The City generally considers assets with a cost of \$5,000 and useful lives in excess of one year or more to be a capital asset.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized. Major improvements are capitalized and depreciated over the remaining useful lives of the related capital assets. Major additions that are substantially a new asset are capitalized over the useful lives of that asset category as determined by the City's management.

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED

Year ended June 30, 2015

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Major outlays for capital assets and improvements are capitalized as the projects are constructed and put into use. Capital assets are depreciated using the straight-line method over the following estimated useful lives:

Buildings and improvements	50 years
Machinery and equipment	5 years
Infrastructure	25 years

Capital assets transferred between funds or functions are transferred at their net book value (cost less accumulated depreciation), as of the date of transfer.

I. Lease obligations

The City may have various assets under capital lease agreements. In the government wide financial statements, capital leases and the related lease obligations are reported as liabilities in the governmental activities of the statement of net assets.

J. Debt costs

Debt costs are expensed as incurred.

K. Unearned revenues

Unearned revenues arise in governmental funds when revenue does not meet both the “measurable” and “available” criteria for recognition in the current period. Deferred revenue may also arise, in both governmental and proprietary funds, when resources are received by the government before it has a legal claim to them, as when grant monies are received prior to incurring qualifying expenditures (unearned). In subsequent periods, when both revenue recognition criteria are met, or when the government has a legal claim to the resources, revenue is recognized. The City assumes all delinquent taxes to be uncollectible at the end of the year and does not present accounts receivable or deferred revenue in connection with taxes receivable. However, the City does attempt to collect all delinquent taxes.

L. Compensated absences

The City’s policy allows employees to accumulate a maximum of 288 hours of unused sick leave and 192 hours of vacation leave. Employees are compensated for excess leave hours at the regular rate of pay each year in December.

M. Pension plans

Full-time City employees are members of the State of Kentucky County Employees’ Retirement System (CERS). The City’s policy is to fund all pension costs accrued; such costs to be funded are determined annually as of June 30 of the prior fiscal year by the System’s actuary. Former employees are also members of the Police and Fireman’s pension fund. The City funds the Police and Fireman’s Pension Fund as deemed necessary.

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED

Year ended June 30, 2015

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

N. Fund balances:

The Board has elected to adopt GASB Statement Number 54 for the current and subsequent reporting periods. This statement substantially changes the terminology used to describe different component of the fund balance. Under this statement, the fund balance is separated into five categories as follows:

Nonspendable:	Funds permanently nonspendable by decree of donor, such as an endowment or items which may not be used for another purpose, such as amounts used to prepay future expenses or already purchased inventory on hand.
Restricted:	Funds legally restricted under federal and state law, bond authority or grantor contract.
Committed:	Commitments passed by the Board for specific expenditures.
Assigned:	Funds assigned to management priority including issued encumbrances.
Unassigned:	Funds available for future operations

It is the Board's practice to liquidate funds when conditions have been met releasing these funds from legal, Board, or managerial obligations, using restricted funds first, followed by committed funds, assigned funds, then unassigned funds.

The City does not use encumbrance accounting.

O. Budgets and Budgetary accounting

The City follows procedures pursuant to KRS 91A.030 in establishing the budgetary data reflected in the financial statements as follows:

1. Prior to May 1 of each year, the Mayor submits to the Middlesboro City Council a proposed operating budget for the fiscal year commencing the following July 1. The operating budget includes proposed expenditures and the means of financing them.
2. Public hearings are conducted to obtain taxpayer comments.
3. Prior to July 1, the budget is legally enacted through passage of an ordinance.
4. The Mayor is authorized to transfer budgeted amounts between categories within each department; however, any revisions that alter the total expenditures of any fund must be approved by the Middlesboro City Council.
5. Formal budgetary integration is employed as a management control device during the year for the general fund. Formal budgetary integration is not employed for debt service funds because effective budgetary control is alternatively achieved through general obligation bond indenture provisions. Operating transfers required for debt service is accounted for in the budget of the City's general fund.

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED

Year ended June 30, 2015

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

6. Budgets for governmental funds are adopted on a basis consistent with generally accepted accounting principles (GAAP). Actual expenditures may not exceed the legally adopted budget for any given fund.
7. The budget for the fiscal year ending June 30, 2015 was amended during the year as in accordance with the law. The amendment was approved in the same manner as the original budget was adopted.

P. Property taxes

Delinquent property taxes attach as an enforceable lien on property as of January 1. Taxes are levied on October 1, and are payable in full by December 31. The County bills the property taxes and the City collects the taxes. City property tax revenues are recorded as receivables and deferred revenue at the time the tax levy is billed. Current year revenues recognized are those collected within the current period, or soon enough thereafter to pay current liabilities, generally within sixty days after the year-end. The City does not realize prior year delinquencies in the following year soon enough to make them available to meet current year expenditures, and fully reserves the uncollected balance at year's end as uncollectible. Since the net is zero they are not presented on the financial statements

Q. Use of estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of certain assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenditures/expenses during the reporting period. As such, actual results could differ from those estimates.

R. Inventory

Inventory is reported at cost and pertains only to the sewer fund. It represents supplies that will be utilized in the repair and maintenance of lines. The inventory value at June 30, 2014 was \$5,799.

S. Deferred Inflows and Deferred Outflows of Resources

The City adopted GASB 63 in the prior year and GASB 65 in the current year, which combined requires the recording of deferred outflows and deferred inflows of resources in the government-wide financial statements. The City did not have any items to present in these categories for the current audit period.

NOTE 2 – CASH AND INVESTMENTS

Custodial credit risk for deposits is the risk that in the event of a bank failure, the City's deposits may not be returned to it. As of June 30, 2015, the carrying amount of the City's cash and cash equivalents was \$1,341,207. The bank balance was \$1,435,026. The City also held \$1,201,643 in agency for the Middlesboro Police and Firemen's Pension Fund. Of the total cash balance, \$801,182 was covered by federal depository insurance with the remaining balance, excluding petty cash of \$1,000, covered by collateral agreements and collateral held by the pledging bank's trust department

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED

Year ended June 30, 2015

in the City's name. By state statute, and City policy, the City may deposit funds in state

NOTE 2 – CASH AND INVESTMENTS - CONTINUED

and nationally chartered banks which provide FDIC insurance and sufficient collateral to secure deposits in excess of FDIC coverage. Cash equivalents are considered to be demand deposits, certificates of deposit and highly liquid, short-term security investments that are readily convertible to known amounts of cash and mature within three months of the date they are acquired. Of the total cash balance exclusive of the Police & Firemen's Pension Fund, \$90,875 is considered restricted or committed. All Pension Fund cash is considered restricted. Restricted and committed cash is restricted by grant agreements, enabling legislation, or Council action. The remaining balance is unrestricted.

NOTE 3 - INVESTMENTS

City funds are considered to be public funds and, therefore, their investment is limited by statute to certain obligations of the United States or similar government agencies, cash instruments, and certain pooled investment funds as provided by KRS 66.480. At June 30, 2015, the City holds only demand deposits and certificates of deposit considered to be cash equivalents. The City holds three long term certificates of deposit in agency for the City of Middlesboro Police and Firemen's Pension Fund that do not bear material interest rate risk. Consequently, the City does not bear material investment related credit risk or interest rate risk. The City has not adopted a formal investment policy.

NOTE 4 – CONTINGENCIES

A. Pending and Threatened Litigation

A number of claims and suits are pending against the City for alleged damages to persons and/or property and for other alleged liabilities arising out of matters usually incident to the operation of a city such as Middlesboro. In the opinion of City management, the City has strong defenses against such claims, and thus the ultimate loss, if any, relating to these claims and suits not covered by insurance, will not materially affect the financial position of the City.

B. Short-term Line of Credit/ Short Term Loan

The City of Middlesboro maintains a short-term line of credit of \$250,000 with a local bank. The purpose of the loan is to meet short-term commitments as needed. There is no balance owed on the line of credit at June 30, 2015.

C. Grants

Amounts received or receivable from grant agencies are subject to audit and adjustment by grantor agencies. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount, if any, of expenditures that may be disallowed by the grantor cannot be determined at this time, although the City expects such amounts, if any, to be immaterial.

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED

Year ended June 30, 2015

NOTE 5 – CAPITAL ASSETS

Capital asset activity for the fiscal year ended June 30, 2015 was as follows:

<u>Governmental Activities</u>	<u>July 1, 2014</u>	<u>Additions</u>	<u>Deductions</u>	<u>June 30, 2015</u>
Land	\$ 1,599,747	\$ -	-	\$ 1,599,747
Infrastructure	90,713	5,000	-	95,713
Buildings	4,746,055	-	-	4,746,055
Equipment	1,175,114	266,965	-	1,442,079
Vehicles	<u>2,249,135</u>	<u>-</u>	<u>-</u>	<u>2,249,135</u>
Total historical cost	\$ 9,860,764	\$ 271,965	-	\$ 10,132,729
Less: Accumulated depreciation	<u>1,460,467</u>	<u>116,220</u>	<u>-</u>	<u>1,576,687</u>
Governmental Activities Capital Assets -net	<u>\$ 8,400,297</u>	<u>\$ 155,745</u>	<u>\$ -</u>	<u>\$ 8,556,042</u>
 Business-Type Activities				
Land	\$ 345,173	\$ -	\$ -	\$ 345,173
Buildings	137,620	-	-	137,620
Sewer plant	14,537,398	-	-	14,537,398
Equipment	2,035,164	74,098	-	2,109,262
Vehicles	<u>577,148</u>	<u>186,426</u>	<u>-</u>	<u>763,574</u>
Total historical cost	17,632,503	260,524	-	17,893,027
Less: Accumulated depreciation	<u>10,723,594</u>	<u>449,406</u>	<u>-</u>	<u>11,173,000</u>
Business-Type Activities Capital Assets -net	<u>\$ 6,908,909</u>	<u>\$ (188,882)</u>	<u>\$ -</u>	<u>\$ 6,720,027</u>

Depreciation expense for governmental activities is charged to functions as follows:

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED

Year ended June 30, 2015

General government	\$ 52,883
Public safety	41,411
Highways and streets	18,876
Culture and recreation	<u>3,050</u>
	<u>\$ 116,220</u>

NOTE – 6 LONG-TERM LIABILITIES

A. Compensated absences

The government-wide statement of net position and the proprietary fund financial statements record non-current accrued vacation and sick-leave as a long-term liability of the City.

B. Bonds Payable

Kentucky Bond Corporation Financing Program Revenue Bonds

The City issued \$255,000 in revenue bonds in March 2012 to finance a repayment of compensation of firefighters for overtime wages. This determination was made by a Kentucky Labor Cabinet audit and subsequent ruling. The bonds carry an interest rate of 2.5% - 3.5% and are payable in annual installments of \$20,000 over a ten-year period. Interest is paid semi-annually.

Kentucky League of Cities (KLC) Funding Trust General Obligation Refunding and Taxable Funding Bonds, Series 2003A and 2003B

In August 1988, the City elected to have its employees participate in the Commonwealth of Kentucky's County Employee Retirement System (CERS). In conjunction with this election, the City entered in an agreement with CERS whereby the City would fund the prior service credit of its employees over a thirty-year period at 8% interest. In August 1994, the City issued \$1,115,000 KLC floating Indebtness Funding Bonds to refinance the existing debt with CERS.

The following table presents future principal and interest payments due for the bonds payable at June 30, 2015:

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED
 Year ended June 30, 2015

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2016	\$ 99,000	14,405	\$ 113,405
2017	103,000	10,376	113,376
2018	106,000	6,098	112,098
2019	25,000	3,525	28,525
2020	30,000	2,775	32,775
2021	30,000	1,875	31,875
2022	<u>30,000</u>	<u>975</u>	<u>30,975</u>
	<u>\$ 423,000</u>	<u>\$ 40,029</u>	<u>\$ 463,029</u>

NOTE – 6 LONG-TERM LIABILITIES-CONTINUED

C. Note Payable – Street Sweeper

Note Payable

On October 7, 2014, the City acquired a street sweeper to replace one destroyed in a fire. To obtain the unit the City used insurance proceeds and a \$130,000 note from Branch Banking and Trust. The note carries an interest rate of 2.225% and is payable in annual installments over five years. The balance of the lease at June 30, 2015 was \$130,000. Future principal and interest rates as of June 30, 2015 are:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2016	\$ 24,871	2,886	\$ 27,757
2017	25,423	2,334	27,757
2018	25,988	1,769	27,757
2019	26,564	1,193	27,757
2020	<u>27,154</u>	<u>603</u>	<u>27,757</u>
	<u>\$ 130,000</u>	<u>\$ 8,785</u>	<u>\$ 138,785</u>

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED

Year ended June 30, 2015

D. Capital Lease Obligations

Lease Payable

On November 8, 2011, the City acquired two ambulances with a fair market value of \$188,562. The lease purchase agreement carries an interest rate of 4.25% and is payable in annual installments over five years. The balance of the lease at June 30, 2015 was \$56,853. Future principal and anticipated interest rates as of June 30, 2015 are:

<u>Period</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2015-16	\$ 40,780	\$ 16,073	\$ 56,853
	Less: amount representing interest		<u>(16,073)</u>
	Net capital lease liability		<u>\$ 40,780</u>

NOTE – 6 LONG-TERM LIABILITIES-CONTINUED

Changes in long-term liability for the year ended June 30, 2015 were as follows:

	<u>Balance July 1, 2014</u>	<u>Issues or Additions</u>	<u>Payments or Expenditures</u>	<u>Balance June 30, 2015</u>
Governmental Activities				
General obligation bonds	\$ 304,000	\$ -	\$ 71,000	\$ 233,000
Revenue bonds	215,000	-	25,000	190,000
Note payable	-	130,000	-	130,000
Compensated absences	<u>156,395</u>	<u>9,315</u>	<u>-</u>	<u>165,710</u>
	<u>\$ 675,395</u>	<u>\$ 139,315</u>	<u>\$ 96,000</u>	<u>\$ 718,710</u>
Business-Type Activities				
Lease Purchase	<u>\$ 79,666</u>	<u>\$ -</u>	<u>\$ 38,886</u>	<u>\$ 40,780</u>

NOTE 7 – PENSION PLANS

A. County Employee’s Retirement System (CERS)

The City contributes to the Kentucky County Employees Retirement System (CERS), which is a cost-sharing multiple-employer public employer retirement system (PERS) administered by the Kentucky retirement system. All full-time employees are eligible and must participate in the State PERS. The

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED

Year ended June 30, 2015

pension plan provides pension benefits, deferred allowances, and death and disability benefits to plan members and their beneficiaries. A member may retire after reaching the age of 55 or accumulating 27 years (20 years for hazardous-pay employees) of service with the City or another entity covered by the State PERS. Employees who retire at or after age 55 with 27 (20 years for hazardous-pay employees) or more years of service are entitled to pension payments for the remainder of their lives equal to a percentage of their final salary which depends on the number of years they were employed by a participant in the state PERS. Ten-year historical trend information showing CERS's progress in accumulating sufficient assets to pay benefits when due is presented in their comprehensive annual financial statements and required supplementary information. The report may be obtained by writing to Kentucky Retirement Systems, 1260 Louisville Road, Frankfort, Kentucky 40601

Funding Policy: Employees of the City are required to pay 5-6% (7.98% for hazardous-pay employees) of their gross earnings to the pension plan. The City makes annual contributions to pension plan equal to the amount required by state statutes. During the year the City was required to contribute 17.67% (34.31% for hazardous-pay employees) of its gross payroll to the plan. Covered payroll was \$3,526,249. Total contributions for the year ending June 30, 2015 were \$1,207,078 of which the City contributed \$966,516 and the employees contributed \$237,728. The City's contributions to the County Employee's Retirement systems for the years ending June 30, 2015, 2014 and 2013 were \$956,516, \$970,104, and \$886,615, respectively. The City's contributions were equal to the contractually required contributions as set by state statutes.

NOTE 7 – PENSION PLANS (CONTINUED)

Based on state statutes, all full-time employees must participate in city or municipality pension plans. Under the provisions of the City's pension plan, pension benefits vest after twenty years of full-time employment. An employee may retire after twenty years of service and receive annual pension benefits equal to on-half of the employee's salary, including incentive pay, earned during the last year of employment. Also, the pension plan provides for death and disability benefits. All pension, death, and disability benefits are determined by state statutes. The Fund is closed to new participants, and there are no active employees in the plan.

B. Police and Fireman's Pension Fund

The City contributes to a defined benefit plan, the Middlesboro Police and Fireman's Fund, which is a single-employer pension employee retirement system (PERS). In August 1988, the City froze admission of new entrants who now join the statewide County Employees Retirement System. Members who had already retired at August 1988 remained in the plan and continue to receive monthly benefits. It is the responsibility of the Middlesboro PERS to function as an investment and administrative agent for the City of Middlesboro with respect to the pension plan. The plan is included in the accompanying financial statements as the P&F Pension Fund.

The Plan uses the accrual basis of accounting. Investment income is recognized when incurred and contributions are recognized when due. Benefits and refunds are recognized when due and payable under the terms of the Plan. The Plan does not issue stand-alone financial statements; however, it is presented in the City's financial statements as the P&F Pension Fund. Three investments represented more than 5% of the net assets available for benefits. Long term certificates of deposit in the amounts of \$683,029, and \$364,936 represented 56.84%, and 30.37% of total holdings respectively.

The remaining assets are held in an interest-bearing checking account. The checking account

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED

Year ended June 30, 2015

represents 12.79% of total holdings. The cost of administering the plan is financed by the P&F Pension Fund. There are no related party transactions. According to KRS 95.629, if there are insufficient funds, the City will be held responsible for the monthly payment of the pensions after the entire proceeds of the pension fund have been transferred to the general fund of the City. City contributions are determined by the City council. For the year ended June 30, 2015, the City did not contribute any funds to the pension fund. Membership in the plan as of June 30, 2015 is seven participants. The population is made up of retired or terminated participants with deferred vested interest in the pension fund. The plan is closed to additional members

The fund has a cash and investment balance of \$1,201,642. The fund earned \$12,663 in interest income and paid out \$231,677 in benefits for the year ended June 30, 2015.

NOTE – 8 OTHER POST EMPLOYMENT BENEFITS

The City does not offer other post-employment benefits to its employees.

NOTE – 9 LEASES

The City receives rental income principally for real property from various agencies. Future minimum rental commitments under these leases are insignificant. Rental income from these sources totaled approximately \$7,500 for the year ended June 30, 2015.

NOTE – 10 MUNICIPAL AID FUNDS

The City receives municipal aid funding from the State of Kentucky. These funds are restricted for the specific purposes and are accounted for the Municipal Road Aid Fund. Municipal Aid funds received for the year amounted to \$231,466

NOTE – 11 LOCAL GOVERNMENT ECONOMIC ASSISTANCE

The City receives LGEA funding from the State of Kentucky. The funds are restricted for specific purposes, and, the City accounts for these funds under the LGEA fund. Local Government Economic Assistance funds received for the year amounted to \$95,657.

NOTE – 12 RISK MANAGEMENT

The City is exposed to various risks of loss related to torts; theft of, damage of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. To obtain insurance for workers' compensation, errors and omissions, and general liability coverage, the City participates in the Kentucky League of Cities Insurance Services. The City pays an annual premium to each fund for coverage. Workers' Compensation premiums are based on premium rates established by such fund in conjunction with the excess insurance carrier, subject to claims experience modifications.

In accordance with KRS 65.067, the City bonds officials or employees who handle public funds in an amount covering the maximum amount they may have under their control at any given time. This statute applies to all officers, officials, and employees of all local governments who handle public funds in an execution of their duties. In order to comply with the regulation, the City purchases insurance bonds through various agencies.

There has been no reduction in insurance coverage from the previous year in any of the City's policies. In addition, there have been no settlements in excess of the City's coverage in the past three

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO BASIC FINANCIAL STATEMENTS – CONTINUED

Year ended June 30, 2015

years.

NOTE – 13 RESTRICTED FUND BALANCE

At June 30, 2015, the City of Middlesboro had \$90,875 in restricted fund balances representing escrow held for bond payments and grant payments.

NOTE – 14 RESTRICTED NET ASSETS

Restricted net assets are those with constraints placed on their use by either: 1) externally imposed by creditors (such as through debt covenants), or 2) imposed by law through constitutional provisions or enabling legislation. All net assets not otherwise classified as restricted, committed, or assigned are shown as unrestricted. Restricted assets included \$13,495 in escrow deposits and \$77,875 in grant revenue restricted for specific purposes.

NOTE – 15 IMPLEMENTATION OF GASB STATEMENT NUMBER 63 AND GASB STATEMENT NO. 65

The City has implemented GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, for the year ended June 30, 2013 and GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*, for the year ended June 30, 2014. These standards established guidance for reporting deferred outflows of resources, deferred inflow of resources, and net position in a statement of financial position.

NOTE – 16 INTERFUND TRANSFERS

Interfund transfers during the year ended June 30, 2015 were as follows:

<u>From</u> <u>Fund</u>	<u>To</u> <u>Fund</u>	<u>Purpose</u>	<u>Amount</u>
MRA	General	Operating	\$ 55,000
LGEA	General	Operating	105,000
Ambulance	General	Operating	505,000
Sewer	General	Operating	<u>393,440</u>
			<u>\$ 1,058,440</u>

NOTE – 17 SUBSEQUENT EVENTS

The City's management has evaluated subsequent events through July 6, 2018, the date which the financial statements were available to be issued. Management has noted no issues that affect the current financial statements.

City of Middlesboro, Kentucky
 Required Supplemental Budgetary Comparison - General Fund
 Year Ended June 30, 2015

	Final Budget	Actual	Variance Favorable (Unfavorable)
Revenues	\$ 6,163,050	\$ 4,842,179	\$ (1,320,871)
Expenditures			
General government	1,071,085	1,063,230	7,855
Public Safety	3,625,750	3,600,369	25,381
Highways and streets	1,172,000	1,141,815	30,185
Debt service	121,800	115,054	6,746
Capital outlay	271,765	271,765	-
Total Expenditures	<u>6,262,400</u>	<u>6,192,233</u>	<u>70,167</u>
Other sources and uses			
Refinancing proceeds from loan	-	130,000	130,000
Refinancing payment of debt	-	-	-
Transfers in (out)	1,250,000	1,058,440	(191,560)
Total other sources and uses	<u>1,250,000</u>	<u>1,188,440</u>	<u>(61,560)</u>
Net Changes in Fund Balances	1,150,650	(161,614)	989,036
Fund Balance July 1, 2014	<u>563,445</u>	<u>232,689</u>	<u>330,756</u>
Fund Balance June 30, 2015	<u>\$ 1,714,095</u>	<u>\$ 71,075</u>	<u>\$ (1,643,020)</u>

CITY OF MIDDLESBORO, KENTUCKY

NOTES TO REQUIRED SUPPLEMENTARY INFORMATION

Year ended June 30, 2015

Note A - Budgets and Budgetary accounting

The City follows procedures pursuant to KRS 91A.030 in establishing the budgetary data reflected in the financial statements as follows:

1. Prior to May 1 of each year, the Mayor submits to the Middlesboro City Council a proposed operating budget for the fiscal year commencing the following July 1. The operating budget includes proposed expenditures and the means of financing them.
2. Public hearings are conducted to obtain taxpayer comments.
3. Prior to July 1, the budget is legally enacted through passage of an ordinance.
4. The City Mayor is authorized to transfer budgeted amounts between categories within each department; however, any revisions that alter the total expenditures of any fund must be approved by the Middlesboro City Council.
5. Formal budgetary integration is employed as a management control device during the year for the general fund. Formal budgetary integration is not employed for debt service funds because effective budgetary control is alternatively achieved through general obligation bond indenture provisions. Operating transfers required for debt service are accounted for in the budget of the City's general fund.
6. Budgets for governmental funds are adopted on a basis consistent with generally accepted accounting principles (GAAP). Actual expenditures may not exceed the legally adopted budget for any given fund.
7. The budget for the fiscal year ending June 30, 2015 was amended during the year as allowed by law. The amendment was approved in the same manner as the original budget was adopted.

REQUIRED SUPPLEMENTARY INFORMATION

City of Middlesboro, Kentucky
 Schedule of the City's Proportionate Share of the
 Net Pension Liability
 County Employees Retirement System (Hazardous)
 June 30, 2013

	<u>City's proportion of net pension liability (asset)</u>	<u>City's proportionate share of the net pension liability (asset)</u>	<u>City's covered-employee payroll</u>	<u>City's proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll</u>	<u>Plan fiduciary net position as a percentage of the total pension liability</u>
2016	0.07810%	\$ 1,198,924	\$ 409,661	292.66%	59.97%
2015	0.07358%	\$ 854,000	\$ 417,748	204.43%	63.46%

* The amounts presented for each fiscal year were determined as of 6/30/.

This schedule is presented to illustrate the requirement to show information for 10 years. More information will be added as it becomes available.

City of Middlesboro, Kentucky
 Schedule of the City's Contributions
 County Employees Retirement System (Hazardous)
 June 30, 2013

	<u>Contractually required contribution</u>	<u>Contributions in relation to contractually required contribution</u>	<u>Contribution deficiency (excess)</u>	<u>City's covered-employee payroll</u>	<u>Contributions as a percentage of covered-employee payroll</u>
2016	\$ 134,983	\$ 134,983	\$ -	\$ 409,661	32.95%
2015	\$ 110,035	\$ 110,035	\$ -	\$ 417,748	26.34%

This schedule is presented to illustrate the requirement to show information for 10 years. More information will be added as it becomes available.

City of Middlesboro, Kentucky
Balance Sheet - Non-Major Governmental Funds
June 30, 2015

	LGEA Fund	Municipal Road Aid Fund	Total Governmental Funds
Assets			
Cash	\$ -	\$ -	\$ -
Restricted cash	13,937	63,728	77,665
Accounts receivable, net			
Tax and license	-	-	-
Other	-	-	-
	-	-	-
Total Assets	\$ 13,937	\$ 63,728	\$ 77,665
Liabilities and Fund Balances			
Liabilities			
Accounts payable	-	-	-
Accrued liabilities	-	-	-
	-	-	-
Total Liabilities	-	-	-
Fund Balances			
Restricted	13,937	63,728	77,665
Unassigned	-	-	-
	-	-	-
Total Fund Balances	13,937	63,728	77,665
Total Liabilities and Fund Balances	\$ 13,937	\$ 63,728	\$ 77,665

City of Middlesboro, Kentucky
 Schedule of the City's Proportionate Share of the
 Net Pension Liability
 County Employees Retirement System (Non-Hazardous)
 June 30, 2013

	<u>City's proportion of net pension liability (asset)</u>	<u>City's proportionate share of the net pension liability (asset)</u>	<u>City's covered-employee payroll</u>	<u>City's proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll</u>	<u>Plan fiduciary net position as a percentage of the total pension liability</u>
2016	0.039982%	\$ 1,719,045	\$ 1,034,038	166.25%	59.97%
2015	0.037870%	\$ 1,229,000	\$ 1,020,428	142.07%	66.80%

* The amounts presented for each fiscal year were determined as of 6/30/.

This schedule is presented to illustrate the requirement to show information for 10 years. More information will be added as it becomes available.

City of Middlesboro, Kentucky
Statement of Revenues, Expenditures and Changes In
Fund Balances - Non-Major Governmental Funds
For the Year Ended June 30, 2015

	LGEA Fund	Municipal Road Aid Fund	Total Governmental Funds
Revenue			
Taxes	\$ -	\$ -	\$ -
Licenses and permits	-	-	-
Fines and forfeits	-	-	-
Interest income	40	81	121
Rental income	-	-	-
Intergovernmental programs	100,658	231,466	332,124
Miscellaneous income	-	-	-
Total revenue	<u>100,698</u>	<u>231,547</u>	<u>332,245</u>
Expenditures			
General government	22,880	-	22,880
Public safety	-	-	-
Highways and streets	-	142,887	142,887
Debt service	-	-	-
Capital outlay	-	-	-
Total Expenditures	<u>22,880</u>	<u>142,887</u>	<u>165,767</u>
Excess of Revenues			
Over (Under) Expenditures	77,818	88,660	166,478
Other Financing Sources (Uses)			
Refinancing proceeds from loan	-	-	-
Proceed from sale of fixed assets	-	-	-
Operating transfers in (out)	<u>(105,000)</u>	<u>(55,000)</u>	<u>(160,000)</u>
Total Other Financing Sources (Uses)	<u>(105,000)</u>	<u>(55,000)</u>	<u>(160,000)</u>
Net Change in Fund Balance	(27,182)	33,660	6,478
Fund Balance July 1, 2013	<u>41,119</u>	<u>30,068</u>	<u>71,187</u>
PPA - Reclass	-	-	-
Fund Balance June 30, 2014	<u>\$ 13,937</u>	<u>\$ 63,728</u>	<u>\$ 77,665</u>

City of Middlesboro, Kentucky
 Schedule of the City's Contributions
 County Employees Retirement System (Non-Hazardous)
 June 30, 2013

	Contractually required contribution	Contributions in relation to contractually required contribution	Contribution deficiency (excess)	City's City's covered-employee payroll	Contributions as a percentage of covered-employee payroll
2016	\$ 160,365	\$ 160,365	\$ -	\$ 1,034,038	15.51%
2015	\$ 198,127	\$ 198,127	\$ -	\$ 1,020,428	19.42%

This schedule is presented to illustrate the requirement to show information for 10 years. More information will be added as it becomes available.

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

Independent Auditor's Report

Mayor and Councilors
City of Middlesboro
Middlesboro, Kentucky

We have audited, in accordance with the 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, the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of City of Middlesboro, Kentucky, as of and for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise City of Middlesboro, Kentucky's basic financial statements, and have issued our report thereon dated July 6, 2018.

Internal Control over Financial Reporting

Management of City of Middlesboro, Kentucky is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit of the financial statements, we considered City of Middlesboro, Kentucky'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 City of Middlesboro, Kentucky's internal control. Accordingly, we do not express an opinion on the effectiveness of City of Middlesboro, Kentucky's internal control.

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. 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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. We did identify deficiencies in internal control that we considered to be material weaknesses. These material weaknesses are presented in the attached Comments and Recommendations letter dated July 6, 2018. However, other material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether City of Middlesboro, Kentucky'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 three instances of noncompliance or other matters that are required to be reported under *Government Auditing Standard*. These noncompliance findings are presented in the attached Comments and Recommendations letter dated July 6, 2018.

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.

Cloyd & Associates, PSC

Middlesboro, Kentucky
July 6, 2018

Mayor and Councilors
City of Middlesboro
Middlesboro, Kentucky

In planning and performing our audit of the basic financial statements of the City of Middlesboro, Kentucky for the year ended June 30, 2015, we considered the District's internal control structure to determine our auditing procedures for the purpose of expressing an opinion on the basic financial statements and not to provide assurance on the internal control structure.

During our audit we note matters that are opportunities for strengthening internal controls and operating efficiency. The memorandum that accompanies this letter summarizes our comments and suggestions regarding those matters, if any. This letter does not affect our report thereon dated July 6, 2018, on the basic financial statements of City of Middlesboro, Kentucky.

We will review the status of these comments during our next audit engagement. We have already discussed these comments and suggestions with various City management personnel, and we will be pleased to discuss them in further detail at your convenience, to perform any additional study of these matters, or to assist you in implementing the recommendations.

Respectfully,

Cloyd & Associates, PSC

Middlesboro, Kentucky
July 6, 2018

**Comments and Recommendations
City of Middlesboro, Kentucky
June 30, 2015**

City of Middlesboro, Kentucky
Combining Statement of Net Position - Nonmajor Proprietary Funds
June 30, 2013

	Golf Course	Community Center	Total Proprietary Funds
Assets			
Current Assets			
Cash	\$ 21,500	\$ 10,632	\$ 32,132
Accounts receivable	876	-	876
Total Current Assets	<u>22,376</u>	<u>10,632</u>	<u>33,008</u>
Noncurrent Assets			
Restricted cash	341	-	341
Capital assets, net of accumulated depreciation	385,771	114,000	499,771
Total Noncurrent Assets	<u>386,112</u>	<u>114,000</u>	<u>500,112</u>
Total Assets	<u>408,488</u>	<u>124,632</u>	<u>533,120</u>
Deferred outflows			
	23,842	-	23,842
Liabilities			
Current Liabilities			
Bonds and notes payable	17,674	-	17,674
Capital Leases payable	4,236	-	4,236
Accounts payable	3,741	11	3,752
Compensated absences	2,592	-	2,592
Total Current Liabilities	<u>28,243</u>	<u>11</u>	<u>28,254</u>
Noncurrent Liabilities			
Bonds and notes payable	10,574	-	10,574
Capital Leases payable	4,785	-	4,785
Net pension liability	159,105	-	159,105
Total Noncurrent Liabilities	<u>174,464</u>	<u>-</u>	<u>174,464</u>
Total Liabilities	<u>202,707</u>	<u>11</u>	<u>202,718</u>
Deferred inflows			
	-	-	-
Net Position			
Invested in capital assets, net of related debt	357,523	114,000	471,523
Restricted	341	-	341
Unrestricted	(128,241)	10,621	(117,620)
Total Net Position	<u>\$ 229,623</u>	<u>\$ 124,621</u>	<u>\$ 354,244</u>

Material Weaknesses in Internal Control

1. Financial audits are not conducted timely.
2. The Police and Firemen's Pension Fund is not properly monitored.
3. There is no segregation of bank accounts for police forfeitures.
4. Police forfeitures and accounting records are not properly submitted to the City Clerk to ensure proper accounting.
5. Accounts receivable are not properly recorded.
6. There is no indication that fixed assets are accounted for in accordance with GAAP.

Non-Compliance

We noted the following deficiencies that we consider to be material weaknesses. All material weaknesses are also considered significant deficiencies.

1. There is a failure of City Management to have the actuarial study and actuarial evaluation of the Police and Firemen's Pension Fund to be conducted timely in accordance with KRS 67A.560
2. There is a failure of City Management to timely ensure the performance and submission of financial audits per KRS 91A.040. City audits for the years 2015, 2016, 2017, and 2018 are delinquent.
3. The Police Asset Forfeiture Account has not been reported to the proper authorities in accordance with 218A.040.

Management responses:

1. The City will conduct a study of cost and feasibility to get this noncompliance corrected as soon as possible.
2. The City has engaged auditors who are currently auditing all years that are delinquent.
3. The City will review policies and procedures for forfeitures to be properly reported to proper authorities.

City of Middlesboro, Kentucky
Combining Statement of Revenues, Expenses, and Changes
in Net Position - Nonmajor Proprietary Funds
For the Year Ended June 30, 2013

	Golf Course	Community Center	Total Other Proprietary Funds
Operating Revenues			
Charges for services	\$ 118,424	\$ 21,508	\$ 139,932
Other income	-	-	-
Total Operating Revenues	<u>118,424</u>	<u>21,508</u>	<u>139,932</u>
Operating Expenses			
Salaries	90,697	21,834	112,531
Purchase of resale items	22,620	65	22,685
Depreciation	15,722	6,736	22,458
Maintenance	1,050	-	1,050
Utilities	7,089	6,539	13,628
Chemicals	7,157	-	7,157
Employee benefits	13,073	2,394	15,467
Pension expense	94,968	-	94,968
Insurance	67	-	67
Supplies	21,182	4,486	25,668
Professional fees	3,425	-	3,425
Licenses & permits	160	225	385
Processing fees	2,369	999	3,368
Equipment rental	12,434	-	12,434
Fuel	6,416	-	6,416
Dues and subscriptions	701	-	701
Uniforms	-	-	-
Taxes	688	480	1,168
Other operating expenses	2,668	704	3,372
Other general expenses	4,719	-	4,719
Total Operating Expenses	<u>307,205</u>	<u>44,462</u>	<u>351,667</u>
Operating Loss	(188,781)	(22,954)	(211,735)
Other Revenues (Expenses)			
Interest revenue	-	-	-
Interest expense	(8)	-	(8)
Total other Revenues (Expenses)	<u>(8)</u>	<u>-</u>	<u>(8)</u>
Loss before transfers	(188,789)	(22,954)	(211,743)
Transfers from governmental activities	<u>112,000</u>	<u>27,000</u>	<u>139,000</u>
Net gain (loss)	(76,789)	4,046	(72,743)
Net Position July 1, 2015	<u>306,412</u>	<u>120,575</u>	<u>426,987</u>
Net Position June 30, 2016	<u>\$ 229,623</u>	<u>\$ 124,621</u>	<u>\$ 354,244</u>