

OFFICE OF AUDITOR OF STATE
STATE OF IOWA

Rob Sand
Auditor of State

State Capitol Building
Des Moines, Iowa 50319-0006

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NEWS RELEASE

FOR RELEASE

June 27, 2019

Contact: Marlys Gaston
515/281-5834

Auditor of State Rob Sand today released an audit report on the Hudson Municipal Electric Utility in Hudson, Iowa for the year ended June 30, 2018.

The Utility's receipts totaled \$1,716,505 for the year ended June 30, 2018, an 7.7% increase over the prior year. The receipts included \$1,703,730 of charges for service, \$10,861 of miscellaneous receipts and \$1,914 of interest on investments. Disbursements for the year ended June 30, 2018 totaled \$1,801,660, a 6.0% increase over the prior year, and included \$1,687,666 for operations, \$94,618 for debt service and \$19,376 for capital outlay.

The significant increase in disbursements is due primarily to an increase in the energy purchased as a result of an increase in demand. In addition, the Utility paid the remaining balance of \$93,199 on an outstanding promissory note. The increase also included approximately \$23,000 of additional development rebates paid in fiscal year 2018 over fiscal year 2017.

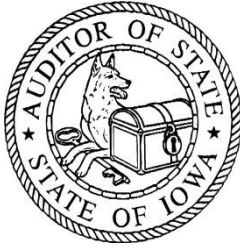
A copy of the audit report is available for review on the Auditor of State's web site at <https://auditor.iowa.gov/reports/audit-reports/>.

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HUDSON MUNICIPAL ELECTRIC UTILITY
INDEPENDENT AUDITOR'S REPORTS
FINANCIAL STATEMENT
SUPPLEMENTARY AND OTHER INFORMATION
SCHEDULE OF FINDINGS

JUNE 30, 2018

Hudson Municipal Electric Utility



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STATE OF IOWA

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June 20, 2019

Officials of Hudson Municipal Electric Utility
Hudson, Iowa

Dear Board Members:

I am pleased to submit to you the financial and compliance audit report for Hudson Municipal Electric Utility for the year ended June 30, 2018. The audit was performed pursuant to Chapter 11.6 of the Code of Iowa and in accordance with U.S. auditing standards and the standards applicable to financial audits contained in Government Auditing Standards.

I appreciate the cooperation and courtesy extended by the officials and employees of Hudson Municipal Electric Utility throughout the audit. If I or this office can be of any further assistance, please contact me or Marlys Gaston of my staff at 515-281-5834.

Sincerely,

A handwritten signature in black ink that reads "Rob Sand". The signature is stylized and cursive.

Rob Sand
Auditor of State

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Hudson Municipal Electric Utility

Officials

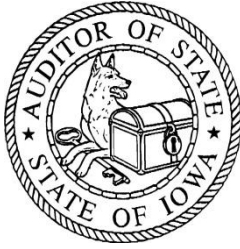
(Before January 2018)

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
Jereme Trotter	Chairperson	Jan 2018
Kenton Zelle	Vice Chairperson	Jan 2020
Doug Wyatt	Trustee	Jan 2021
Dan Brobst	Trustee	Jan 2022
Jeff Cory	Trustee	Jan 2023
Sue Theisen	Office Manager	Indefinite
Barb Guenther	Billing Clerk	Indefinite

(After January 2018)

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
Jereme Trotter	Chairperson	Jan 2024
Jeff Cory	Vice Chairperson	Jan 2023
Doug Wyatt	Trustee	(Resigned May 2018)
Kenton Zelle	Trustee	Jan 2020
Wanda Birdsong (Appointed June 2018)	Trustee	Jan 2021
Dan Brobst	Trustee	Jan 2022
Sue Theisen	Office Manager	Indefinite
Barb Guenther	Billing Clerk	Indefinite

Hudson Municipal Electric Utility



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Independent Auditor's Report

To the Board of Trustees of the Hudson Municipal Electric Utility:

Report on the Financial Statement

We have audited the accompanying financial statement of the Hudson Municipal Electric Utility as of and for the year ended June 30, 2018, and the related Notes to Financial Statement listed in the table of contents.

Management's Responsibility for the Financial Statement

Management is responsible for the preparation and fair presentation of the financial statement in accordance with the cash basis of accounting described in Note 1. This includes determining the cash basis of accounting is an acceptable basis for the preparation of the financial statement in the circumstances. This includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of a financial statement that is free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statement. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statement, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Utility's preparation and fair presentation of the financial statement 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 Utility'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 statement.

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

Opinion

In our opinion, the financial statement referred to above presents fairly, in all material respects, the cash basis financial position of the Hudson Municipal Electric Utility as of June 30, 2018 and the changes in its cash basis financial position for the years then ended in accordance with the basis of accounting described in Note 1.

Basis of Accounting

As discussed in Note 1, the financial statement was prepared on the basis of cash receipts and disbursements, which is a basis of accounting other than U.S. generally accepted accounting principles. Our opinion is not modified with respect to this matter.

Other Matters

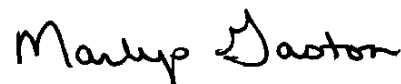
Supplementary and Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statement. The supplementary information included in Schedule 1 is for purposes of additional analysis and is not a required part of the basic financial statement. The supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statement. Such information has been subjected to the auditing procedures applied in the audit of the financial statement and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statement or to the financial statement itself, and other additional procedures in accordance with U.S. generally accepted auditing standards. In our opinion, the supplementary information is fairly stated in all material respects in relation to the financial statement taken as a whole.

The other information, Management's Discussion and Analysis, the Budgetary Comparison Information, the Schedule of the Utility's Proportionate Share of the Net Pension Liability and the Schedule of Utility Contributions on pages 7 through 9 and 21 through 26, has not been subjected to the auditing procedures applied in the audit of the financial statement and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by Government Auditing Standards

In accordance with Government Auditing Standards, we have also issued our report dated June 20, 2019 on our consideration of the Hudson Municipal Electric Utility's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the effectiveness of the Utility's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the Hudson Municipal Electric Utility's internal control over financial reporting and compliance.



Marlys K. Gaston, CPA
Deputy Auditor of State

June 20, 2019

MANAGEMENT'S DISCUSSION AND ANALYSIS

The Hudson Municipal Electric Utility provides this Management's Discussion and Analysis of its financial statement. This narrative overview and analysis of the financial activities is for the fiscal year ended June 30, 2018. We encourage readers to consider this information in conjunction with the Utility's financial statement, which follows.

2018 FINANCIAL HIGHLIGHTS

- The Utility's total receipts increased 7.7%, or approximately \$123,000, from fiscal year 2017 to fiscal year 2018. Charges for services increased approximately \$128,000, primarily due to an increase in demand and a 53% increase in the purchased power adjustment rate from \$0.01887 per kWhr to \$0.02887 per kWhr effective December of 2017.
- The Utility's total disbursements increased 6.0%, or approximately \$102,000, from fiscal year 2017 to fiscal year 2018.
- The Utility's total cash balance decreased 8.8%, or approximately \$85,000, from June 30, 2017 to June 30, 2018.

USING THIS ANNUAL REPORT

The annual report consists of a financial statement and other information, as follows:

Management's Discussion and Analysis introduces the financial statement and provides an analytical overview of the Utility's financial activities.

The Statement of Cash Receipts, Disbursements and Changes in Cash Balance presents information on the Utility's receipts and disbursements, non-operating receipts and disbursements and whether the Utility's cash basis financial position has improved or deteriorated as a result of the year's activities.

The Notes to Financial Statement provide additional information essential to a full understanding of the data provided in the financial statement.

Other Information further explains and supports the financial statement with a comparison of the Utility's budget for the year and the Utility's proportionate share of the net pension liability and related contributions.

Supplementary Information provides detailed information about the individual Enterprise Fund Accounts.

BASIS OF ACCOUNTING

The Hudson Municipal Electric Utility maintains its financial records on the basis of cash receipts and disbursements and the financial statement of the Utility is prepared on that basis. The cash basis of accounting does not give effect to accounts receivable, accounts payable and accrued items. Accordingly, the financial statement does not present financial position and results of operations of the funds in accordance with U.S. generally accepted accounting principles. Therefore, when reviewing the financial information and discussion within this annual report, readers should keep in mind the limitations resulting from the use of the cash basis of accounting.

FINANCIAL ANALYSIS OF THE HUDSON MUNICIPAL ELECTRIC UTILITY

Statement of Cash Receipts, Disbursements and Changes in Cash Balance

The purpose of the statement is to present the receipts received by the Utility and the disbursements paid by the Utility, both operating and non-operating. The statement also presents a fiscal snapshot of the Utility's cash balance at year-end. Over time, readers of the financial statement are able to determine the Utility's financial position by analyzing the increase or decrease in cash balance.

Receipts include metered electric sales, fees for upkeep and/or upgrade of individual service lines, electric turn on/off fees and miscellaneous fees. A summary of cash receipts, disbursements and changes in the cash balance for the years ended June 30, 2017 and June 30, 2018 is presented below:

	Changes in Cash Balance	
	Year ended June 30,	
	2018	2017
Receipts:		
Interest on investments	\$ 1,914	2,492
Charges for service	1,703,730	1,576,016
Miscellaneous	10,861	14,635
Total receipts	1,716,505	1,593,143
Disbursements:		
Business type	1,687,666	1,469,169
Debt service	94,618	23,175
Capital outlay	19,376	85,909
Total disbursements	1,801,660	1,578,253
Change in cash balance	(85,155)	14,890
Cash balance beginning of year	969,044	954,154
Cash balance end of year	\$ 883,889	969,044

The Utility's unrestricted cash balance is available for use in the routine operations and administrative areas of the electric utility and for the capital improvements to the infrastructure areas.

BUDGETARY HIGHLIGHTS

Over the course of the fiscal year ended June 30, 2018, the Utility did not amend its budget.

For the fiscal year ended June 30, 2018, the Utility's charges for service receipts were \$282,497 less than budgeted and miscellaneous receipts were \$10,476 more than budgeted. Charges for service receipts were significantly less than budgeted due to optimistic projections for development in the Upper Ridge subdivision.

For the fiscal year ended June 30, 2018, the Utility's disbursements were \$188,089 less than budgeted for the year. Business type disbursements were less than budgeted due to optimistic projections for development in the Upper Ridge subdivision.

DEBT ADMINISTRATION

At June 30, 2018, the Utility had no long-term debt outstanding.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

Current economic conditions beyond the Utility Trustees' control play a significant role in the daily operations of the distribution services. These conditions include, but are not limited to:

- The need to constantly maintain facilities, vehicles and machinery.
- The need to comply with federal and state regulations for the distribution of electricity.
- The need to maintain up-to-date technology at a reasonable cost.

CONTACTING THE UTILITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide the citizens, customers and creditors with a general overview of the Hudson Municipal Electric Utility's finances and to show the Utility's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Hudson Municipal Electric Utility, 615 Washington, PO Box 416, Hudson, Iowa 50643.

Basic Financial Statement

Hudson Municipal Electric Utility
Statement of Cash Receipts, Disbursements and
Changes in Cash Balance

As of and for the year ended June 30, 2018

	2018	2017
Operating receipts:		
Charges for service	\$ 1,703,730	1,576,016
Miscellaneous	10,861	14,635
Total operating receipts	1,714,591	1,590,651
Operating disbursements:		
Business type activities	1,687,666	1,469,169
Excess of operating receipts over operating disbursements	26,925	121,482
Non-operating receipts (disbursements):		
Interest on investments	1,914	2,492
Debt service	(94,618)	(23,175)
Capital outlay	(19,376)	(85,909)
Net non-operating receipts (disbursements)	(112,080)	(106,592)
Change in cash balance	(85,155)	14,890
Cash balance beginning of year	969,044	954,154
Cash balance end of year	\$ 883,889	969,044
Cash Basis Fund Balance		
Restricted for customer deposits	\$ 10,022	18,911
Restricted for capital improvements	201,630	128,466
Unrestricted	672,237	821,667
Total cash basis fund balance	\$ 883,889	969,044

See notes to financial statement.

Hudson Municipal Electric Utility

Hudson Municipal Electric Utility

Notes to Financial Statement

June 30, 2018

(1) Summary of Significant Accounting Policies

A. Reporting Entity

The Hudson Municipal Electric Utility is a component unit of the City of Hudson, Iowa, as determined by criteria specified by the Governmental Accounting Standards Board. The Utility is governed by a five-member Board of Trustees appointed by the Mayor of the City of Hudson, and then approved by the Board of Trustees, which exercises oversight responsibility under this criteria.

B. Basis of Presentation

The accounts of the Utility are organized as an Enterprise Fund. Enterprise Funds are utilized to finance and account for the acquisition, operation and maintenance of governmental facilities and services supported by user charges.

Enterprise Funds distinguish operating receipts and disbursements from non-operating items. Operating receipts and disbursements generally result from providing services and producing and delivering goods in connection with an Enterprise Fund's principal ongoing operations. All receipts and disbursements not meeting this definition are reported as non-operating receipts and disbursements.

C. Basis of Accounting

The Utility maintains its financial records on the basis of cash receipts and disbursements and the financial statement of the Utility is prepared on that basis. The cash basis of accounting does not give effect to accounts receivable, accounts payable and accrued items. Accordingly, the financial statement does not present financial position and results of operations of the funds in accordance with U.S. generally accepted accounting principles.

D. Restricted Cash Basis Fund Balance

Funds set aside for customer deposits and system upgrades are classified as restricted.

E. Budgets and Budgetary Accounting

The budgetary comparison and related disclosures are reported as Other Information.

(2) Cash and Pooled Investments

The Utility's deposits in banks at June 30, 2018 were entirely covered by federal depository insurance or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to ensure there will be no loss of public funds.

The Utility is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentalities; certificates of deposit or other evidences of deposit at federally insured depository institutions approved by the Board of Trustees; prime eligible bankers acceptances; certain high rated commercial paper; perfected repurchase agreements; certain registered open-end management investment companies; certain joint investment trusts; and warrants or improvement certificates of a drainage district.

The Utility had no investments meeting the disclosure requirements of Governmental Accounting Standards Board Statement No. 72.

(3) Pension Plan

Plan Description – IPERS membership is mandatory for employees of the Utility, except for those covered by another retirement system. Employees of the Utility are provided with pensions through a cost-sharing multiple employer defined benefit pension plan administered by the Iowa Public Employees' Retirement System (IPERS). IPERS issues a stand-alone financial report which is available to the public by mail at PO Box 9117, Des Moines, Iowa 50306-9117 or at www.ipers.org.

IPERS benefits are established under Iowa Code Chapter 97B and the administrative rules thereunder. Chapter 97B and the administrative rules are the official plan documents. The following brief description is provided for general informational purposes only. Refer to the plan documents for more information.

Pension Benefits – A Regular member may retire at normal retirement age and receive monthly benefits without an early-retirement reduction. Normal retirement age is age 65, any time after reaching age 62 with 20 or more years of covered employment or when the member's years of service plus the member's age at the last birthday equals or exceeds 88, whichever comes first. These qualifications must be met on the member's first month of entitlement to benefits. Members cannot begin receiving retirement benefits before age 55. The formula used to calculate a Regular member's monthly IPERS benefit includes:

- A multiplier based on years of service.
- The member's highest five-year average salary, except members with service before June 30, 2012 will use the highest three-year average salary as of that date if it is greater than the highest five-year average salary.

If a member retires before normal retirement age, the member's monthly retirement benefit will be permanently reduced by an early-retirement reduction. The early-retirement reduction is calculated differently for service earned before and after July 1, 2012. For service earned before July 1, 2012, the reduction is 0.25% for each month the member receives benefits before the member's earliest normal retirement age. For service earned on or after July 1, 2012, the reduction is 0.50% for each month the member receives benefits before age 65.

Generally, once a member selects a benefit option, a monthly benefit is calculated and remains the same for the rest of the member's lifetime. However, to combat the effects of inflation, retirees who began receiving benefits prior to July 1990 receive a guaranteed dividend with their regular November benefit payments.

Disability and Death Benefits – A vested member who is awarded federal Social Security disability or Railroad Retirement disability benefits is eligible to claim IPERS benefits regardless of age. Disability benefits are not reduced for early retirement. If a member dies before retirement, the member’s beneficiary will receive a lifetime annuity or a lump-sum payment equal to the present actuarial value of the member’s accrued benefit or calculated with a set formula, whichever is greater. When a member dies after retirement, death benefits depend on the benefit option the member selected at retirement.

Contributions – Contribution rates are established by IPERS following the annual actuarial valuation which applies IPERS’ Contribution Rate Funding Policy and Actuarial Amortization Method. State statute limits the amount rates can increase or decrease each year to 1 percentage point. IPERS Contribution Rate Funding Policy requires the actuarial contribution rate be determined using the “entry age normal” actuarial cost method and the actuarial assumptions and methods approved by the IPERS Investment Board. The actuarial contribution rate covers normal cost plus the unfunded actuarial liability payment based on a 30-year amortization period. The payment to amortize the unfunded actuarial liability is determined as a level percentage of payroll based on the Actuarial Amortization Method adopted by the Investment Board.

In fiscal year 2018, pursuant to the required rate, Regular members contributed 5.95% of covered payroll and the Utility contributed 8.93% of covered payroll, for a total rate of 14.88%.

The Utility’s contributions to IPERS for the years ended June 30, 2018 and 2017 were \$11,247 and \$10,944, respectively.

Net Pension Liability, Pension Expense, Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions – At June 30, 2018, the Utility had a liability of \$109,363 for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2017 and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The Utility’s proportion of the net pension liability was based on the Utility’s share of contributions to IPERS relative to the contributions of all IPERS participating employers. At June 30, 2017, the Utility’s proportion was 0.001642%, which was a decrease of 0.000049% from its proportion measured as of June 30, 2016.

For the year ended June 30, 2018, the Utility’s pension expense, deferred outflows of resources and deferred inflows of resources totaled \$15,043, \$39,863 and \$21,947, respectively.

There were no non-employer contributing entities to IPERS.

Actuarial Assumptions – The total pension liability in the June 30, 2017 actuarial valuation was determined using the following actuarial assumptions applied to all periods included in the measurement:

Rate of inflation (effective June 30, 2017)	2.60% per annum.
Rates of salary increase (effective June 30, 2017)	3.25 to 16.25% average, including inflation. Rates vary by membership group.
Long-term investment rate of return (effective June 30, 2017)	7.00% compounded annually, net of investment expense, including inflation.
Wage growth (effective June 30, 2017)	3.25% per annum, based on 2.60% inflation and 0.65% real wage inflation.

The actuarial assumptions used in the June 30, 2017 valuation were based on the results of actuarial experience study dated March 24, 2017.

Mortality rates were based on the RP-2000 Mortality Table for Males or Females, as appropriate, with adjustments for mortality improvements based on Scale AA.

The long-term expected rate of return on IPERS' investments was determined using a building-block method in which best-estimate ranges of expected future real rates (expected returns, net of investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

<u>Asset Class</u>	<u>Asset Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
Domestic equity	24.0%	6.25%
International equity	16.0	6.71
Core plus fixed income	27.0	2.25
Public credit	3.5	3.46
Public real assets	7.0	3.27
Cash	1.0	(0.31)
Private equity	11.0	11.15
Private real assets	7.5	4.18
Private credit	3.0	4.25
Total	<u>100.0%</u>	

Discount Rate – The discount rate used to measure the total pension liability was 7.00%. The projection of cash flows used to determine the discount rate assumed employee contributions will be made at the contractually required rate and contributions from the Utility will be made at contractually required rates, actuarially determined. Based on those assumptions, IPERS' fiduciary net position was projected to be available to make all projected future benefit payments to current active and inactive employees. Therefore, the long-term expected rate of return on IPERS' investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of the Utility's Proportionate Share of the Net Pension Liability to Changes in the Discount Rate – The following presents the Utility's proportionate share of the net pension liability for fiscal year 2018 calculated using the discount rate of 7.00%, as well as what the Utility's proportionate share of the net pension liability would be if it were calculated using a discount rate 1% lower (6.00%) or 1% higher (8.00%) than the current rate.

	1% Decrease (6.00%)	Discount Rate (7.00%)	1% Increase (8.00%)
Utility's proportionate share of the net pension liability	\$ 180,187	109,363	49,858

IPERS' Fiduciary Net Position – Detailed information about IPERS' fiduciary net position is available in the separately issued IPERS financial report which is available on IPERS' website at www.ipers.org.

(4) Promissory Notes

A summary of changes in long-term liabilities for the year ended June 30, 2018 is as follows:

	Balance Beginning of Year	Increases	Decreases	Balance End of Year	Due Within One Year
Promissory notes	\$ 93,199	-	93,199	-	-

On July 22, 2011, the Hudson Municipal Electric Utility issued a promissory note to Butler County Rural Electric Cooperative for \$100,000 to assist in completing construction on a warehouse and office facility. The note bears interest at 3.0% for a term of 10 years.

On December 15, 2011, the Hudson Municipal Electric Utility issued a second promissory note to Butler County Rural Electric Cooperative for \$100,000 to assist in completing construction on a warehouse and office facility. The note bears interest at 3.0% for a term of 10 years.

During the fiscal year ending June 30, 2018, the Hudson Municipal Electric Utility paid off the remaining balance on the two promissory notes.

(5) Compensated Absences

Utility employees accumulate a limited amount of earned but unused vacation, sick, and compensatory time leave hours for subsequent use or for payment upon termination, retirement or death. These accumulations are not recognized as disbursements by the Utility until used or paid. The Utility's approximate liability for earned vacation, sick leave and compensatory time payable to employees at June 30, 2018 is as follows:

<u>Type of Benefit</u>	<u>Amount</u>
Vacation	\$ 15,000
Sick leave	2,000
Compensatory time	<u>5,000</u>
Total	<u>\$ 22,000</u>

This liability has been computed based on rates of pay in effect at June 30, 2018.

(6) Risk Management

The Hudson Municipal Electric Utility is exposed to various risks of loss related to torts; theft, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. The Utility assumes liability for any deductibles and claims in excess of coverage limitations. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

Other Information

Hudson Municipal Electric Utility

Hudson Municipal Electric Utility

Budgetary Comparison Schedule
of Receipts, Disbursements and Changes in Balance -
Budget and Actual (Cash Basis)
Other Information

Year ended June 30, 2018

	Actual	Original/Final Budgeted Amounts	Final to Net Variance
Receipts:			
Use of money and property	\$ 1,914	3,137	(1,223)
Charges for service	1,703,730	1,986,227	(282,497)
Miscellaneous	10,861	385	10,476
Total receipts	1,716,505	1,989,749	(273,244)
Disbursements:			
Business type activities	1,801,660	1,989,749	188,089
Excess of receipts over disbursements	(85,155)	-	(85,155)
Other financing uses, net	-	-	-
Change in cash balance	(85,155)	-	(85,155)
Cash balance beginning of year	969,044	1,004,175	(35,131)
Cash balance end of year	\$ 883,889	1,004,175	(120,286)

See accompanying independent auditor's report.

Hudson Municipal Electric Utility

Notes to Other Information – Budgetary Reporting

June 30, 2018

The Hudson Municipal Electric Utility prepares a budget on the cash basis of accounting for all funds and submits it to the City Council. In accordance with the Code of Iowa, the City Council annually adopts a budget, which includes the Utility, on the cash basis following required public notice and hearing. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures.

Formal and legal budgetary control is based upon classes of disbursements known as functions, not by fund. The Utility's disbursements are budgeted in the business type activities function.

During the year ended June 30, 2018, disbursements did not exceed the amount budgeted.

Hudson Municipal Electric Utility

Schedule of the Utility's Proportionate Share of the Net Pension Liability

Iowa Public Employees' Retirement System
For the Last Four Years*
(In Thousands)

Other Information

	2018	2017	2016	2015
Utility's proportion of the net pension liability	0.001642%	0.001691%	0.001743%	0.001712%
Utility's proportionate share of the net pension liability	\$ 109	106	86	69
Utility's covered payroll	\$ 123	121	121	114
Utility's proportionate share of the net pension liability as a percentage of its covered payroll	88.62%	87.60%	71.07%	60.53%
IPERS' net position as a percentage of the total pension liability	82.21%	81.82%	85.19%	87.61%

* In accordance with GASB Statement No. 68, the amounts presented for each fiscal year were determined as of June 30 of the preceding fiscal year.

See accompanying independent auditor's report.

Hudson Municipal Electric Utility

Schedule of Utility Contributions

Iowa Public Employees' Retirement System
For the Last Ten Years
(In Thousands)

Other Information

	<u>2018</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>
Statutorily required contribution	\$ 11	11	11	11
Contributions in relation to the statutorily required contribution	<u>(11)</u>	<u>(11)</u>	<u>(11)</u>	<u>(11)</u>
Contribution deficiency (excess)	<u>\$ -</u>	<u>-</u>	<u>-</u>	<u>-</u>
Utility Department's covered payroll	\$ 126	123	121	121
Contributions as a percentage of covered payroll	8.73%	8.94%	9.09%	9.09%

See accompanying independent auditor's report.

2014	2013	2012	2011	2010	2009
10	9	8	6	6	5
(10)	(9)	(8)	(6)	(6)	(5)
-	-	-	-	-	-
114	109	103	93	89	77
8.77%	8.26%	7.77%	6.45%	6.74%	6.49%

Hudson Municipal Electric Utility

Notes to Other Information – Pension Liability

Year ended June 30, 2018

Changes of benefit terms:

Legislation enacted in 2010 modified benefit terms for Regular members. The definition of final average salary changed from the highest three to the highest five years of covered wages. The vesting requirement changed from four years of service to seven years. The early retirement reduction increased from 3% per year measured from the member's first unreduced retirement age to a 6% reduction for each year of retirement before age 65.

Changes of assumptions:

The 2017 valuation implemented the following refinements as a result of an experience study dated March 24, 2017:

- Decreased the inflation assumption from 3.00% to 2.60%.
- Decreased the assumed rate of interest on member accounts from 3.75% to 3.50% per year.
- Decreased the discount rate from 7.50% to 7.00%.
- Decreased the wage growth assumption from 4.00% to 3.25%.
- Decreased the payroll growth assumption from 4.00% to 3.25%.

The 2014 valuation implemented the following refinements as a result of a quadrennial experience study:

- Decreased the inflation assumption from 3.25% to 3.00%.
- Decreased the assumed rate of interest on member accounts from 4.00% to 3.75% per year.
- Adjusted male mortality rates for retirees in the Regular membership group.
- Reduced retirement rates for sheriffs and deputies between the ages of 55 and 64.
- Moved from an open 30-year amortization period to a closed 30-year amortization period for the UAL (unfunded actuarial liability) beginning June 30, 2015. Each year thereafter, changes in the UAL from plan experience will be amortized on a separate closed 20-year period.

The 2010 valuation implemented the following refinements as a result of a quadrennial experience study:

- Adjusted retiree mortality assumptions.
- Modified retirement rates to reflect fewer retirements.
- Lowered disability rates at most ages.
- Lowered employment termination rates.
- Generally increased the probability of terminating members receiving a deferred retirement benefit.
- Modified salary increase assumptions based on various service duration.

Supplementary Information

Hudson Municipal Electric Utility

Hudson Municipal Electric Utility

Combining Schedule of Cash Receipts, Disbursements
and Changes in Cash Balance

Enterprise Fund Accounts

As of and for the year ended June 30, 2018

	Electric Operating	Meter Deposit	System Upgrades	Total
Operating receipts:				
Charges for service	\$ 1,611,474	-	92,256	1,703,730
Miscellaneous	2,037	8,824	-	10,861
Total operating receipts	<u>1,613,511</u>	<u>8,824</u>	<u>92,256</u>	<u>1,714,591</u>
Operating disbursements:				
Business type activities	<u>1,680,986</u>	<u>6,680</u>	<u>-</u>	<u>1,687,666</u>
Excess (deficiency) of operating receipts over (under) operating disbursements	<u>(67,475)</u>	<u>2,144</u>	<u>92,256</u>	<u>26,925</u>
Non-operating receipts (disbursements):				
Interest on investments	1,914	-	-	1,914
Debt service	(94,618)	-	-	(94,618)
Capital outlay	(284)	-	(19,092)	(19,376)
Total non-operating receipts (disbursements)	<u>(92,988)</u>	<u>-</u>	<u>(19,092)</u>	<u>(112,080)</u>
Change in cash balance	(160,463)	2,144	73,164	(85,155)
Cash balance beginning of year	<u>821,667</u>	<u>18,911</u>	<u>128,466</u>	<u>969,044</u>
Cash balance end of year	<u>\$ 661,204</u>	<u>21,055</u>	<u>201,630</u>	<u>883,889</u>

See accompanying independent auditor's report.

Hudson Municipal Electric Utility



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Independent Auditor's Report on Internal Control
over Financial Reporting and on Compliance and Other Matters
Based on an Audit of a Financial Statement Performed in Accordance with
Government Auditing Standards

To the Board of Trustees of the Hudson Municipal Electric Utility:

We have audited in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States, the financial statement of the Hudson Municipal Electric Utility as of and for the year ended June 30, 2018, and the related Notes to Financial Statement, and have issued our report thereon dated June 20, 2019. Our report expressed an unmodified opinion on the financial statement which was prepared on the basis of cash receipts and disbursements, a basis of accounting other than U.S. generally accepted accounting principles.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statement, we considered the Hudson Municipal Electric Utility's internal control over financial reporting to determine the audit procedures appropriate in the circumstances for the purpose of expressing our opinion on the financial statement, but not for the purpose of expressing an opinion on the effectiveness of the Hudson Municipal Electric Utility's internal control. Accordingly, we do not express an opinion on the effectiveness of the Hudson Municipal Electric Utility's internal control.

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

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility a material misstatement of the Hudson Municipal Electric Utility's financial statement will not be prevented or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings as items (A) through (C) to be material weaknesses.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control which is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying Schedule of Findings as items (D) through (G) to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Hudson Municipal Electric Utility's financial statement is free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, non-compliance 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 no instances of non-compliance or other matters that are required to be reported under Government Auditing Standards. However, we noted certain immaterial instances of non-compliance or other matters which are described in the accompanying Schedule of Findings.

Comments involving statutory and other legal matters about the Utility's operations for the year ended June 30, 2018 are based exclusively on knowledge obtained from procedures performed during our audit of the financial statement of the Utility. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

The Hudson Municipal Electric Utility's Responses to the Findings

The Hudson Municipal Electric Utility's responses to the findings identified in our audit are described in the accompanying Schedule of Findings. The Hudson Municipal Electric Utility's responses were not subjected to the auditing procedures applied in the audit of the financial statement and, accordingly, we express no opinion on them.

Purpose of this Report

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

We would like to acknowledge the many courtesies and assistance extended to us by personnel of the Hudson Municipal Electric Utility during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.


Marlys K. Gaston, CPA
Deputy Auditor of State

June 20, 2019

Hudson Municipal Electric Utility

Schedule of Findings

Year ended June 30, 2018

Finding Related to the Financial Statements:

INTERNAL CONTROL DEFICIENCY:

(A) Segregation of Duties

Criteria – Management is responsible for establishing and maintaining internal control. A good system of internal control provides for adequate segregation of duties so no one individual handles a transaction from its inception to completion. In order to maintain proper internal control, duties should be segregated so the authorization, custody and recording of transactions are not under the control of the same employee. This segregation of duties helps prevent losses from employee error or dishonesty and maximizes the accuracy of the Utility's financial statement.

Condition – Generally, one or two individuals have control over each of the following areas for the Utility:

- (1) Accounting system – performing all general accounting functions, including journal entries and controlling all data input and output.
- (2) Cash – handling cash, reconciling bank accounts and initiating and recording cash receipt and disbursement transactions.
- (3) Investments – investing and recording.
- (4) Bank reconciliation – preparing bank account reconciliations, handling cash receipt and disbursement functions and handling and recording cash. There is no independent review of the bank reconciliations.
- (5) Receipts – opening mail, collecting, depositing, posting and reconciling.
- (6) Disbursements and payroll – purchasing, preparing checks, recording, reconciling, distributing.
- (7) Long term debt – recordkeeping, compliance and debt payment processing.
- (8) Journal entries – preparing and recording. In addition, there is no independent review of journal entries.

Cause – The Utility has a limited number of employees and procedures have not been designed to adequately segregate duties or provide compensating controls through additional oversight of transactions and processes.

Effect – Inadequate segregation of duties could adversely affect the Utility's ability to prevent or detect and correct misstatements, errors or misappropriation on a timely basis by employees in the normal course of performing their assigned functions.

Recommendation – We realize segregation of duties is difficult with a limited number of office employees. However, the Utility should review its operating procedures to obtain the maximum internal control possible under the circumstances utilizing currently available personnel, including officials. Independent reviews of reconciliations, compensated absences records and utility rates entered into the computer system should be documented by the signature or initials of the independent reviewer and the date of the review.

Hudson Municipal Electric Utility

Schedule of Findings

Year ended June 30, 2018

Response – Due to the size of our utility office, segregation of duties is difficult. We will follow the recommendations and continue to look for additional ways to segregate duties.

Conclusion – Response accepted.

(B) Bank Reconciliations

Criteria – An effective internal control system provides for internal controls related to ensuring proper accounting for all funds by reconciling bank and book balances and review by an independent person.

Condition – Monthly bank reconciliations were not reviewed by an independent person.

Cause – Procedures have not been designed and implemented to ensure bank reconciliations have been reviewed by an independent person.

Effect – Lack of independent review of may result in the potential for errors to not be detected.

Recommendation – To improve financial accountability and control, monthly bank reconciliations should be reviewed by an independent person and the review should be documented by the signature or initials of the reviewer and the date of the review.

Response – The Utility Office is now considering removing two Board Trustees from the bank signature cards and requiring them to review, sign, and date bank reconciliations after they have been reviewed.

Conclusion – Response accepted.

(C) Reconciliation of Utility Billings, Collections and Delinquent Accounts

Criteria – An effective internal control system provides for internal controls related to maintaining delinquent account listings, reconciling utility billings, collections and delinquent accounts and comparing utility collections to deposits to ensure proper recording of utility receipts, the propriety of adjustments and write-offs and the propriety of delinquent account balances.

Condition – Monthly utility reconciliations were not reviewed by an independent person.

Cause – Procedures have not been designed and implemented to ensure utility reconciliations have been reviewed by an independent person.

Effect – Lack of independent review of may result in the potential for errors to not be detected.

Hudson Municipal Electric Utility

Schedule of Findings

Year ended June 30, 2018

Recommendation – The Utility board or a designated independent person should review the reconciliations and monitor delinquencies. The review of the reconciliations should be documented by the signature or initials of the reviewer and the date of review.

Response – The Utility Office is now considering removing two Board Trustees from the bank signature cards and requiring them to review, sign, and date utility reconciliations after they have been reviewed.

Conclusion – Response accepted.

(D) Computer System

Criteria – Properly designed policies and procedures pertaining to control activities over the Utility’s computer system and implementation of the policies and procedures help provide reasonable assurance financial information is safeguarded and reliable, and helps ensure the reliability of financial reporting, the effectiveness and efficiency of operations and compliance with applicable laws and regulations.

Condition – The Utility does not have written policies for requiring password changes because the Utility’s software does not require the user to change log-ins/passwords periodically.

Cause – Management has not required written policies for the above computer based controls.

Effect – Lack of written policies for computer based system and implementation of those policies could result in a loss of data or compromised data, resulting in unreliable financial information.

Recommendation – The Utility should develop written policies addressing the above items to improve the Utility’s control over its computer system.

Response – The Board will consider revising the employee Computer Use Policy to include additional password protections.

Conclusion – Response accepted.

(E) Timesheets

Criteria – An effective internal control system provides for internal controls related to the processing and approval of payroll for employees of the Utility. Proper review of timesheets can help ensure proper payment of payroll expenses.

Condition – There is no evidence of independent review of time sheets for the Office Manager.

Cause – Management and the Board have not required review of timesheets for the Office Manager allowing potential errors to perpetuate without being corrected.

Hudson Municipal Electric Utility

Schedule of Findings

Year ended June 30, 2018

Effect – Payroll and compensated absences errors or misstatements could occur without being corrected in a timely manner.

Recommendation – All time sheets should be reviewed by an independent person for accuracy.

Response – The Utility Office is now considering removing two Board Trustees from the bank signature cards and requiring them to review, sign, and date authorized payroll rates entered into the system, time sheets for the Office Manager and compensated absences for full-time employees at the Utility after they have been reviewed.

Conclusion – Response accepted.

(F) Compensated Absences

Criteria – An effective internal control system provides for internal controls related to the processing and approval of payroll for employees in accordance with adopted policies of the City. Approved policies regarding compensated absence records can help ensure proper payment of payroll expenses.

Condition – Although the City has an established policy for paid vacation time, the City has not enforced the vacation time allowed by the policy, resulting in excessive carryover of balances. Also, compensated absence balances are not reviewed by an independent person.

Cause – Established vacation accrual policies have not been enforced.

Effect – The lack of enforcing the policy regarding compensated absences could result in inaccurate payouts.

Recommendation – The City should review policies regarding vacation accruals and payout of compensated absences upon resignation and establish procedures to ensure the policies are enforced. In addition, the City Council should review compensated absence balances to determine their accuracy.

Response – The Utility has now implemented having a Board member act as an auditor who will review the limits for accrual of compensated absences.

Conclusion – Response accepted.

(G) Payroll Rates

Criteria – An effective internal control system provides for controls relating to payroll including proper approval of pay rates.

Condition – Annual salary increases were approved based upon a percentage and the actual approved wages were not documented in the Utility Board minutes.

Cause – The Utility has not implemented procedures to ensure payroll is approved and documented at an actual wage rate.

Hudson Municipal Electric Utility

Schedule of Findings

Year ended June 30, 2018

Effect – Using a percentage rather than per hour rate may cause errors or misstatements in the actual rate applied which could result in unauthorized, unapproved or incorrect increases in pay.

Recommendation – Salaries and wages of employees should be stated in the Utility Board minutes as payroll rates, not percentage increases.

Response – The will be done in the future.

Conclusion – Response accepted.

INSTANCES OF NON-COMPLIANCE:

No matters were noted.

Hudson Municipal Electric Utility

Schedule of Findings

Year ended June 30, 2018

Other Findings Related to Required Statutory Reporting:

- (1) Certified Budget – The budget certified by the City of Hudson includes an amount for the Hudson Municipal Electric Utility. Disbursements during the years ended June 30, 2018 did not exceed the amount budgeted.
- (2) Questionable Disbursements – No disbursements we believe may not meet the requirements of public purpose as defined in an Attorney General’s opinion dated April 25, 1979 were noted.
- (3) Travel Expense – No disbursements of Utility money for travel expenses of spouses of Utility officials or employees were noted.
- (4) Business Transactions – No business transactions between the Utility and Utility officials or employees were noted.
- (5) Bond Coverage – Surety bond coverage of Hudson Municipal Electric Utility officials and employees is carried by the City of Hudson in accordance with statutory provisions. The amount of coverage should be reviewed annually to ensure the coverage is adequate for current operations.
- (6) Board Minutes – No transactions were found that we believe should have been approved in the Board minutes but were not.
- (7) Deposits and Investments – Except as noted, no instances of non-compliance with the deposit and investment provisions of Chapters 12B and 12C of the Code of Iowa and the Utility’s investment policy were noted.

A resolution naming official depositories has been adopted by the Utility. However, the maximum deposit amount was not included on the depository resolution as required by Chapter 12C.2 of the Code of Iowa.

Recommendation – The Utility should adopt a new depository resolution which establishes a maximum deposit amount as required by Chapter 12C.2 of the Code of Iowa.

Response – The Utility will adopt a new depository resolution as required by Chapter 12C.2 of the Code of Iowa.

Conclusion – Response accepted.

- (8) Electronic Check Retention – Chapter 554D.114 of the Code of Iowa allows the Utility to retain cancelled checks in an electronic format and requires retention in this manner to include an image of both the front and back of each cancelled check. The Utility does not retain electronic images of the back of cancelled checks.

Recommendation – The Utility should retain an image of both the front and back of each cancelled check as required.

Response – We will work with our bank to obtain front and back of check images.

Conclusion – Response accepted.

Hudson Municipal Electric Utility

Schedule of Findings

Year ended June 30, 2018

- (9) Payroll Overpayment – During fiscal year ended June 30, 2018, the hourly rate calculated for one employee was greater than the intended authorized rate. Due to this incorrect calculation, the Utility paid the employee at the rate of \$28.74 per hour while the approved wage was \$26.67 per hour. This incorrect calculation resulted in an overpayment by the Utility of \$4,332.20 in wages, \$331.41 in FICA contributions and \$386.87 in IPERS contributions for a total overpayment of \$5,050.48 for fiscal year 2018.

In addition, the incorrect calculations continued through February of 2019 resulting in an overpayment by the Utility of \$3,067.20 in wages, \$234.64 in FICA contributions and \$289.54 in IPERS contributions for a total overpayment of \$3,591.38 for fiscal year 2019.

Recommendation – The Utility should seek reimbursement for the overpayments of wages and related FICA and IPERS contributions identified above. In addition, the Utility should ensure payroll registers are independently reviewed for the accuracy of rates in the future.

Response – The Board will discuss repayment options.

Conclusion – Response acknowledged. The Utility should also ensure payroll registers are independently reviewed for the accuracy of rates.

- (10) Health Insurance Premiums – During the fiscal year ended June 30, 2018, health insurance premiums were not updated in the Utility’s payroll system for the new higher rate. In addition, the portion of the premium paid by the Utility was not consistent with the health insurance policy documented in the approved employee manual. Due to these errors, the Utility under paid their portion of the premium for one individual by \$711.60 in fiscal year ended 2018 and \$56.66 in fiscal year 2019 through the pay period ending March 27, 2019.

Recommendation – The Utility should refund the underpaid portion of the health insurance premiums to the respective employee. In addition, the Utility should ensure payroll registers are independently reviewed to ensure the utility portion of insurance premiums are accurate in the future.

Response – Hudson Municipal Electric Utility will repay the affected employee. Further, a Board member has been named as “auditor” per the recommendation and the payroll items will be audited for accuracy.

Conclusion – Response accepted.

Hudson Municipal Electric Utility

Staff

This audit was performed by:

Marlys K. Gaston, CPA, Deputy
Suzanne R. Dahlstrom, CPA, Manager
Marcus B. Johnson, Senior Auditor
Amanda M. Anderson, Assistant Auditor