

**City of Hernando, Mississippi
Audited Financial Statements
For the Year Ended September 30, 2013**



City of Hernando, Mississippi
Audited Financial Statements
For the Year Ended September 30, 2013

TABLE OF CONTENTS

Independent Auditors' Report	1
Management's Discussion and Analysis	i-viii
Financial Statements	3
Statement of Net Position	4
Statement of Activities.....	5
Balance Sheet – Governmental Funds	6
Reconciliation of the Governmental Funds Balance Sheet to the Statement of Net Position	7
Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Funds.....	8
Reconciliation of Revenues, Expenditures, and Changes in Fund Balances of Governmental Funds to the Statement of Activities	9
Statement of Net Position – Proprietary Fund	10
Statement of Revenues, Expenses and Changes in Net Position – Proprietary Fund.....	11
Statement of Cash Flows – Proprietary Fund	12
Notes to Financial Statements	13
Required Supplementary Information	25
Budgetary Comparison Schedule – General Fund	27
Notes to the Required supplementary Information.....	28
Other Information	29
Surety Bond Coverage	31
Special Reports	33
Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	35
Independent Auditors' Report on Compliance with State Laws and Regulations.....	37
Schedule of Findings and Responses.....	39



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INDEPENDENT AUDITORS' REPORT

Mayor and Board of Aldermen
City of Hernando
Hernando, Mississippi

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hernando, Mississippi ("the City") as of and for the year ended September 30, 2013, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hernando, as of September 30, 2013, 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.

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 on pages i-viii and 27 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.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's basic financial statements. The schedule of surety bonds of municipal officials has not been subjected to 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 Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated June 27, 2014, on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, 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. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's internal control over financial reporting and compliance.

Williams, Pitts & Beard, PLLC

Williams, Pitts & Beard, PLLC
Hernando, Mississippi
June 27, 2014

MANAGEMENT'S DISCUSSION AND ANALYSIS

City of Hernando, Mississippi
Management's Discussion and Analysis
For the Year Ended September 30, 2013
Unaudited

This Discussion and Analysis of the City of Hernando's financial performance provides an overall review of the City's financial activities for the year ended September 30, 2013. The intent of this discussion and analysis is to look at the City's financial performance as a whole. Readers should also review the basic financial statements to enhance their understanding of the City's financial performance.

This discussion complies with the "Required Supplementary Information" specified in the Governmental Accounting Standards Board's (GASB) Statement No. 34 – Basic Financial Statements – and Management's Discussion and Analysis (MD&A) for State and Local Governments issued in June 1999, in order to give the reader a clear understanding of the financial activities that occurred during the fiscal year.

The statements presented in this audit consist of two types:

- Government-wide financial statements are prepared using the modified accrual basis of accounting and include all assets and liabilities of the City of Hernando as a whole. These statements provide an overall view of Hernando's finances. The Statement of Net Position is found on page 4 of the audit report.
- In the Statement of Activities, the City's activities are reported as (1) Governmental Activities; which includes: administration, ambulance, fire, park, planning, police, and street departments, (2) Business-type Activities; which includes: water, sewer, and sanitation. This statement shows the revenues, expenses, and net position. The Statement of Activities is found on page 5.

Fund Financial Statements – A fund is a self-balancing set of accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City of Hernando, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City can be divided into two categories – Governmental Funds and Proprietary Funds.

Governmental Funds – Governmental funds are used to account for essentially the functions reported as governmental activities in the governmental –wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on current sources and uses of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Non-financial assets such as governmental buildings, roads, parkland and long-term liabilities such as bonds payable or long-term liabilities that will not be paid with current assets are excluded. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental funds balance sheet and the governmental funds statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

City of Hernando, Mississippi
Management's Discussion and Analysis
For the Year Ended September 30, 2013
Unaudited

The City maintains several governmental funds. Information is presented separately in the Governmental Funds Balance Sheet (page 6) and in the Governmental Funds Statement of Revenues, Expenditures, and Changes in Fund Balances for the General Fund and Debt Service Fund which are considered to be major funds. All other Governmental Funds are combined into a single amount listed as Other Governmental Funds. The basic governmental funds financial statements can be found on pages 6-9.

Proprietary Funds – The City maintains one proprietary fund, which is an enterprise fund. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The City of Hernando uses enterprise funds to account for its Water, Sewer, and Sanitation operations.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statement provides separate revenue information for the Water, Sewer, and Sanitation funds. The proprietary fund financial statements can be found on pages 10-12 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 government-wide and fund financial statements. The notes to the financial statements can be found on pages 13-24 of this report.

BRIEF DISCUSSION OF BASIC FINANCIAL STATEMENTS

Net position and net position by category may serve over time as a useful indicator of a government's financial position. The assets of the City of Hernando, Mississippi exceeded its liabilities at September 30, 2013 by \$12,757,631. The Majority of the City's net position is net investment in capital assets and unrestricted net position and may be used to meet the government's ongoing obligations to citizens and creditors in accordance with the City's fund designation and fiscal policies. The remaining \$892,390 is restricted for specific purposes. Unrestricted net position decreased by \$950,097, restricted net position decreased in the amount of \$66,213, and net investment in capital assets increased by \$164,424.

As of the close of the current fiscal year the City of Hernando's governmental funds reported combined ending fund balances of \$1,391,567 and a total liabilities and fund balances combined of \$5,685,986.

City of Hernando, Mississippi
Management's Discussion and Analysis
For the Year Ended September 30, 2013
Unaudited

CONDENSED COMPARATIVE FINANCIAL STATEMENTS

The City's combined net position in 2013 decreased 6% from a year ago. The combined net position decreased from \$13,609,517 in 2012 to \$12,757,631 in 2013, which is a decrease of \$851,886.

NET POSITION						
	2012		2012	2013		
	Governmental Activities (All other funds)	2013 Governmental Activities (All other funds)	Business Type Activities (Utility Fund)	Business Type Activities (Utility Fund)	2012 Total	2013 Total
<u>ASSETS</u>						
Current and Other Assets	\$6,620,133	\$ 5,783,776	\$1,517,412	\$ 1,561,714	\$ 8,137,545	\$ 7,345,490
Capital Assets, Net	12,354,683	12,447,425	9,254,899	10,571,508	21,609,582	23,018,933
TOTAL ASSETS	18,974,816	18,231,201	10,772,311	12,133,222	29,747,127	30,364,423
<u>LIABILITIES</u>						
Current and Other Liabilities	4,374,159	4,273,912	527,158	996,392	4,901,317	5,270,304
Long Term Liabilities:						
Due Within One Year	455,000	255,515	172,050	124,185	627,050	379,700
Due in More than One Year	7,846,089	7,907,010	2,763,154	4,049,778	10,609,243	11,956,788
TOTAL LIABILITIES	12,675,248	12,436,437	3,462,362	5,170,355	16,137,610	17,606,792
<u>NET POSITION</u>						
Invest in Capital Assets Net of Debt	4,313,209	4,456,930	6,398,272	6,418,975	10,711,481	10,875,905
Restricted:						
Capital Projects	845,245	847,755	-	-	845,245	847,755
Special Revenue	31,749	35,199	-	-	31,749	35,199
Debt Services	81,609	9,436	-	-	81,609	9,436
Unrestricted	1,027,756	445,444	911,677	543,892	1,939,433	989,336
TOTAL NET POSITION	\$6,299,568	\$ 5,794,764	\$7,309,949	\$ 6,962,867	\$13,609,517	\$12,757,631

Net Position of the City's governmental activities has decreased by 8% (\$6,299,568 in 2012, compared to \$5,794,764 in 2013). Unrestricted net position – the part of net position that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation, or other legal requirements - changed from \$1,027,756 at September 30, 2012 to \$445,444 at the end of this year which is a decrease of 56%.

Net Position of the City's business type activities (utility fund) decreased by 5% (\$7,309,949 compared to \$6,962,867). Unrestricted net position changed from \$911,677 at September 30, 2012 to \$543,892 at the end of this year, which is a decrease of 40%.

City of Hernando, Mississippi
Management's Discussion and Analysis
For the Year Ended September 30, 2013
Unaudited

ANALYSIS OF FINANCIAL POSITION AND RESULTS OF OPERATION

The City's revenues have increased in sales tax, and in building permits. In order to continue to furnish quality services to the citizens, Hernando has been fortunate to receive grants and loans for projects such as water improvements, parks, and drainage improvements.

ANALYSIS OF BALANCES AND TRANSACTIONS OF INDIVIDUAL FUNDS

The largest portion of the City of Hernando's assets can be found in fixed assets such as land, buildings, equipment, and infrastructure. Capital assets used in governmental activities are not financial resources but are used to provide services.

The Statement of Net Position looks at the City as a whole. The following table provides a summary and comparison of the City's net assets for Governmental Activities, Business Type Activities and the two combined per year.

	2013	2012	2013	2012	2013	2012
	Governmental	Governmental	Business-	Business-	2013	2012
	Activities	Activities	Type	Type	Total	Total
	Activities	Activities	Activities	Activities	Total	Total
Revenues						
Taxes - Property	\$4,071,342	\$ 3,964,844	\$ -	\$ -	\$ 4,071,342	\$ 3,964,844
Sales and Use	2,835,915	2,726,591	-	-	2,835,915	2,726,591
Other Taxes	372,841	355,707	-	-	372,841	355,707
Forfeitures	126,317	329,207	-	-	126,317	329,207
Intergovernmental	224,381	224,166	-	-	224,381	224,166
Charges for services	1,094,571	929,451	3,562,976	3,631,203	4,657,547	4,560,654
Interest	6,294	5,800	1,398	1,425	7,692	7,225
Grants	108,743	528,970	239,458	30,898	348,201	559,868
Interfund transfers	(57,300)	(123,262)	57,300	123,262	-	-
Miscellaneous	151,542	215,911	12,024	9,284	163,566	225,195
Sale of assets	33,550	(26,618)	9,619	6,920	43,169	(19,698)
Total revenues	8,968,196	9,130,767	3,882,775	3,802,992	12,850,971	12,933,759
Total expenses	(9,473,000)	(8,501,150)	(4,229,857)	(3,546,271)	(13,702,857)	(12,047,421)
Change in net position	(504,804)	629,617	(347,082)	256,721	(851,886)	886,338
Net position-beginning of year	6,299,568	5,669,951	7,309,949	7,053,228	13,609,517	12,723,179
Net position-end of year	\$5,794,764	\$6,299,568	\$6,962,867	\$ 7,309,949	\$12,757,631	\$ 13,609,517

City of Hernando, Mississippi
Management's Discussion and Analysis
For the Year Ended September 30, 2013
Unaudited

BUDGETARY ANALYSIS

The City of Hernando's budget is prepared according to Mississippi law and is based on accounting for certain transactions on a basis of cash receipts, disbursements, and encumbrances. The most significant budgeted fund is the General Fund. The Budgetary Analysis can be found on page 27.

During the fiscal year ending September 30, 2013, the City amended its budget twice. The total dollar amount of the budget for all funds was increased in the amount of \$1,471,446.00, which was in the General Fund, Culture and Recreation Fund, and Utility Fund. The amendment was necessary in the General Fund for revenues due to subdivision bonds recalled, a Tax Anticipation Loan, loans to purchase a Fire truck, Police cars and equipment, and repairs to City Hall due to a busted pipe. Expenses in the General Fund were increased and some decreased to account for repaying the Tax Anticipation Loan, purchasing the Fire truck, Police cars and equipment, for the Subdivision Bond recalled money being spent to repair subdivisions, repair to City Hall, repairs to the rental area, and legal expenses. The Culture and Recreation Fund was amended to move budgeted amounts from salaries to Temporary Staffing, also other expenses were increased and decreased to cover for supplies, maintenance to building and vehicles, and legal services. In the Utility Fund, revenue and expenses were increased to cover for the lagoon reclamation project, and expenses were increased and decreased to cover for repairs to storm drains, sewer and vehicles.

All budget amendments must be approved by the Mayor and Board of Aldermen. If the amendment exceeds 10% of the original budget then the amendment must be published in a local newspaper.

The fund balance at the beginning of the year was \$1,512,133 for the General Fund and at the end of the year (GAAP basis) was \$1,137,867, which was a decrease of \$374,266.00. The most significant revenues in the General Fund are derived from ad-valorem taxes, sales taxes, franchise taxes, building permit fees, police fines, and ambulance fees.

The revenue budgeted for the Business-Type Fund (Utility Fund) is derived from the sale of water and for services provided such as sanitary sewer and sanitation.

**City of Hernando, Mississippi
Management's Discussion and Analysis
For the Year Ended September 30, 2013
Unaudited**

CAPITAL ASSETS AND LONG TERM DEBT ACTIVITY

Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds. A comparison of these assets are shown as follows:

Description	FYE 9-30-13	FYE 9-30-12	Difference
Land	\$ 581,339	\$ 581,339	\$ 0
Buildings and improvements	5,627,896	5,627,896	0
Equipment	2,355,647	1,920,991	434,656
Vehicles	1,061,605	983,469	78,136
Infrastructure	8,832,713	8,832,713	0
Construction in progress	9,293	58,043	(48,750)
Improvements other than buildings	463,979	463,979	0
Accumulated depreciation	(6,485,047)	(6,113,747)	(371,300)
	<u>\$12,447,425</u>	<u>\$ 12,354,683</u>	<u>\$ 92,742</u>

Changes in General Fixed Assets can be found on page 19 and 20. In the category of Governmental Activities capital assets, net, increased from \$12,354,683 at September 30, 2012 to \$12,447,425 at September 30, 2013. This is an increase of \$92,742 after depreciation. In the category of Business-type Activities capital assets, net, increased from \$9,254,899 at September 30, 2012 to \$10,571,508 at September 30, 2013. This is an increase of \$1,316,609 after depreciation.

General Long-Term Debt is located on pages 21-22. As of September 30, 2013, the City had \$8,270,000 in outstanding General Obligation Bonds, which is \$370,000 more than last year, and \$3,170,745 in notes payable, which is \$320,754.00 more than last year. The long-term debt is low interest loans from the State of Mississippi for water and sewer improvements.

INFRASTRUCTURE ACTIVITY

Over the past few years, the City has applied for state funding to improve the City water system and sanitary sewer system. The DWSIRLF loan application included major water projects for the city that would be completed in five phases. At this time, Hernando has received four DWSIRLF loans. The water improvements have included a new well, water tank, and larger water mains.

CURRENTLY KNOWN FACTS

Hernando has been growing at a very rapid pace; according to the Census in 1990, the population was 3,200, in 2000 the population was 6,812, and currently the population according to the 2012 US Census Population estimate is 14,763. In 2013, the City assessed value of property increased 3% and the sales tax revenue has gone up 4% over the last year. Residential and commercial building permits are seeing a rise again. People are continuing to move to Hernando as shown by the increased number of utility customers. Over the past year the City has added 103 sewer customers and 20 water customers. Since FYE 9-30-2000 the City has added 2,894 sewer customers, and 1,838 water customers. We have two rural water systems that also provide water inside the corporate limits of Hernando which is the reason there are more sewer customers than water. Over the last few years, the Mississippi Department of Environmental quality

City of Hernando, Mississippi
Management's Discussion and Analysis
For the Year Ended September 30, 2013
Unaudited

has mandated that Hernando and the other cities in DeSoto County improve the level of sewage treatment. This mandate is in place to protect our environment and our groundwater. In order to satisfy this mandate more cost effectively, the cities joined with the county to create the DeSoto County Regional Utility Authority (DCRUA).

Each year we try to improve our facilities as funds become available either from tax revenues, grants, or donations. We have a community garden at the Gale Center that is open to the public and a farmers market on the square where the public can purchase locally grown produce. Our farmers market was named fifth favorite in the nation among large markets, and best market in the State. Our park facilities include community center, tennis courts, basketball courts, football fields, and soccer fields, exercise equipment, walking trails, pavilions and playgrounds. We have made an effort to have facilities and programs to accommodate all ages. The City of Hernando has been given the "Playful City USA" designation for the sixth year as of 2013. Hernando was also previously given the "Healthiest Hometown" Award from Blue Cross Blue Shield and the City has been designated a "Tree City USA" for three years now. Hernando has been promoting a healthier city by improving and extending the sidewalks, and adding walking and biking trails on the streets. We are a "Let's Move" and "Excel By 5" Community. The City of Hernando has been featured on CNN Small Hometown series and the ABC "Everyday Health" program.

Hernando has kept the property taxes at a reasonable rate, while continuing to provide the needed services. In 2011 CNN named us in Money Magazine as one of the top 100 places to live. From 1988 to 1990, the millage for ad-valorem tax was 28.5, and in 1990, the millage was increased to 29.5. In the budget year 2001-2002, the millage for ad-valorem taxes was increased from 29.5 mills to 31.75 and this year the millage has remained the same. The taxes are distributed to the General Fund, Municipal Bond and Interest Fund, Library Fund, and the Park Fund. The General Fund is the main fund of the city, which provides for Administration, Fire, Police, Planning, Ambulance, and Court. The Municipal Bond and Interest Fund is to pay General Obligation Bond payments and fees. Library Fund provides funding for the Hernando Library. The Park Fund is used to pay for improvements in the park, cemetery maintenance, and beautification of the City.

CONTACT:

This financial report is designed to provide our citizens, taxpayers, creditors, and investors with a general overview of the City's finances and to show the City's accountability for the money it receives. If you have any questions about this report or need additional financial information contact the City Clerk, at 475 West Commerce Street, Hernando, MS 38632 or by telephone at 662-429-9092.

FINANCIAL STATEMENTS

City of Hernando, Mississippi
Statement of Net Position
September 30, 2013

	Governmental Activities	Business-Type Activities	Total
Assets			
Cash and cash equivalents	\$ 1,266,518	\$ 645,775	\$ 1,912,293
Accounts receivable, net of allowance for uncollectibles of \$1,211,787	81,733	498,889	580,622
Property tax receivable	3,806,534	-	3,806,534
Intergovernmental receivable	328,194	-	328,194
Loan receivable	-	453,116	453,116
Prepaid expense	96,175	22,539	118,714
Internal balances	58,605	(58,605)	-
Deferred charges - bond issuance costs	146,017	-	146,017
Capital assets:			
Land and construction in progress	590,632	2,779,371	3,370,003
Other capital assets, net	11,856,793	7,792,137	19,648,930
Total Assets	18,231,201	12,133,222	30,364,423
Liabilities			
Accounts payable	301,406	553,593	854,999
Retainage payable	-	72,187	72,187
Accrued expenses	165,972	20,817	186,789
Customer deposits	-	349,795	349,795
Unearned revenue	3,806,534	-	3,806,534
Long-term liabilities			
Due within one year:			
Capital debt	255,515	124,185	379,700
Due in more than one year:			
Capital debt	7,734,980	4,028,348	11,763,328
Non-capital debt	172,030	21,430	193,460
Total Liabilities	12,436,437	5,170,355	17,606,792
Net Position			
Net investment in capital assets	4,456,930	6,418,975	10,875,905
Restricted for:			
Capital projects	847,755	-	847,755
Debt service	9,436	-	9,436
Special revenue	35,199	-	35,199
Unrestricted	445,444	543,892	989,336
Total Net Position	\$ 5,794,764	\$ 6,962,867	\$ 12,757,631

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

City of Hernando, Mississippi
Statement of Activities
For the Year Ended September 30, 2013

	Program Revenues				Net (Expenses) Revenue and Changes in Net Position		
	Expenses	Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-Type Activities	Total
Governmental Activities							
General government	\$ 1,929,656	\$ 224,692	\$ 12,260	\$ -	\$ (1,692,704)	\$ -	\$ (1,692,704)
Public safety	5,650,794	294,433	21,567	-	(5,334,794)	-	(5,334,794)
Public works	606,089	-	-	74,916	(531,173)	-	(531,173)
Culture and recreation	745,556	237,933	-	-	(507,623)	-	(507,623)
Health and welfare	144,517	337,513	-	-	192,996	-	192,996
Interest on long-term debt	396,388	-	-	-	(396,388)	-	(396,388)
Total Governmental Activities	<u>9,473,000</u>	<u>1,094,571</u>	<u>33,827</u>	<u>74,916</u>	<u>(8,269,686)</u>	<u>-</u>	<u>(8,269,686)</u>
Business-Type Activities							
Utility	4,163,688	3,562,976	-	239,458	-	(361,254)	(361,254)
Interest on long-term debt	66,169	-	-	-	-	(66,169)	(66,169)
Total Business-Type Activities	<u>4,229,857</u>	<u>3,562,976</u>	<u>-</u>	<u>239,458</u>	<u>-</u>	<u>(427,423)</u>	<u>(427,423)</u>
Total Government	<u>\$ 13,702,857</u>	<u>\$ 4,657,547</u>	<u>\$ 33,827</u>	<u>\$ 314,374</u>	<u>\$ (8,269,686)</u>	<u>\$ (427,423)</u>	<u>\$ (8,697,109)</u>
General Revenues							
					4,071,342	-	4,071,342
					224,381	-	224,381
					2,835,915	-	2,835,915
					372,841	-	372,841
					126,317	-	126,317
					6,294	1,398	7,692
					151,542	12,024	163,566
					(57,300)	57,300	-
					33,550	9,619	43,169
					<u>7,764,882</u>	<u>80,341</u>	<u>7,845,223</u>
					(504,804)	(347,082)	(851,886)
					<u>6,299,568</u>	<u>7,309,949</u>	<u>13,609,517</u>
					<u>\$ 5,794,764</u>	<u>\$ 6,962,867</u>	<u>\$ 12,757,631</u>

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

City of Hernando, Mississippi
Balance Sheet - Governmental Funds
September 30, 2013

	<u>General Fund</u>	<u>Debt Service Fund</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Assets				
Cash and cash equivalents	\$ 963,625	\$ 96,098	\$ 206,795	\$ 1,266,518
Property tax receivable	2,706,668	764,406	335,460	3,806,534
Intergovernmental receivable	316,854	-	11,340	328,194
Other receivables	41,894	-	1,000	42,894
Prepaid expenses	93,496	-	2,679	96,175
Due from other funds	121,235	-	24,436	145,671
Total Assets	<u>\$ 4,243,772</u>	<u>\$ 860,504</u>	<u>\$ 581,710</u>	<u>\$ 5,685,986</u>
Liabilities				
Accounts payable	\$ 267,065	\$ -	\$ 34,341	\$ 301,406
Accrued expenses	94,076	-	5,337	99,413
Due to other funds	38,096	20,103	28,867	87,066
Deferred revenue	2,706,668	764,406	335,460	3,806,534
Total Liabilities	<u>3,105,905</u>	<u>784,509</u>	<u>404,005</u>	<u>4,294,419</u>
Fund Balances				
Nonspendable:				
Prepaid expenses	93,496	-	2,679	96,175
Restricted:				
Capital projects	-	-	60,801	60,801
Debt service	-	75,995	-	75,995
Special revenue	-	-	35,199	35,199
Assigned:				
General fund	792,438	-	-	792,438
Culture and recreation	-	-	56,658	56,658
Forfeiture	-	-	22,368	22,368
Unassigned	251,933	-	-	251,933
Total Fund Balances	<u>1,137,867</u>	<u>75,995</u>	<u>177,705</u>	<u>1,391,567</u>
Total Liabilities and Fund Balances	<u>\$ 4,243,772</u>	<u>\$ 860,504</u>	<u>\$ 581,710</u>	<u>\$ 5,685,986</u>

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

City of Hernando, Mississippi
Reconciliation of the Governmental Funds Balance Sheet
to the Statement of Net Position
September 30, 2013

Total Fund Balance - Governmental Funds \$ 1,391,567

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

Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds. These assets consist of:

Land	581,339	
Buildings and improvements	5,627,896	
Equipment	2,355,647	
Vehicles	1,061,605	
Infrastructure	8,832,713	
Construction in progress	9,293	
Improvements other than buildings	463,979	
Accumulated depreciation	<u>(6,485,047)</u>	
		12,447,425

Bonds issued by the City have associated costs that are paid from current available financial resources in the funds. However, these costs are deferred on the Statement of Net Position. 146,017

Other assets are not available to pay for current period expenditures and, therefore, are deferred in the funds. 38,839

Some liabilities are not due and payable in the current period and therefore are not reported in the funds. Those liabilities consist of:

Notes payable	(61,551)	
Leases payable	(600,276)	
General obligation and revenue bonds	(7,328,668)	
Compensated absences	(172,030)	
Accrued interest	<u>(66,559)</u>	
		<u>(8,229,084)</u>

Net Position of Governmental Activities \$ 5,794,764

City of Hernando, Mississippi
Statement of Revenues, Expenditures and
Changes in Fund Balances – Governmental Funds
For the Year Ended September 30, 2013

	<u>General Fund</u>	<u>Debt Service Fund</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Revenues				
General property taxes	\$ 2,917,215	\$ 803,320	\$ 350,808	\$ 4,071,343
Intergovernmental	224,381	-	-	224,381
Sales tax	2,835,915	-	-	2,835,915
Franchise taxes	365,839	-	7,002	372,841
Charges for services	853,746	-	240,825	1,094,571
Forfeitures	126,317	-	-	126,317
Interest	5,044	342	908	6,294
Miscellaneous	124,988	-	26,554	151,542
Total Revenues	<u>7,453,445</u>	<u>803,662</u>	<u>626,097</u>	<u>8,883,204</u>
Expenditures				
General government	1,283,117	-	-	1,283,117
Public safety	5,608,384	-	224	5,608,608
Public works	311,841	-	-	311,841
Culture and recreation	-	-	719,273	719,273
Health and welfare	115,106	3,963	25,448	144,517
Capital outlay	1,134,130	-	196,927	1,331,057
Debt service:				
Principal	505,812	622,500	7,626	1,135,938
Interest	7,899	385,003	702	393,604
Bond issue cost	-	74,191	-	74,191
Total Expenditures	<u>8,966,289</u>	<u>1,085,657</u>	<u>950,200</u>	<u>11,002,146</u>
Excess (Deficiency) of Revenues Over (Under) Expenditures	<u>(1,512,844)</u>	<u>(281,995)</u>	<u>(324,103)</u>	<u>(2,118,942)</u>
Other Financing Sources (Uses)				
Grant revenue	33,827	-	74,916	108,743
Sale of assets	250	-	33,300	33,550
Interfund transfers	-	-	(57,300)	(57,300)
Loan proceeds	1,104,500	-	68,000	1,172,500
Refunding bonds issued	-	3,496,168	-	3,496,168
Payment to bond refunding escrow agent	-	(3,450,906)	-	(3,450,906)
Total Other Financing Sources	<u>1,138,577</u>	<u>45,262</u>	<u>118,916</u>	<u>1,302,755</u>
Net Change in Fund Balances	(374,267)	(236,733)	(205,187)	(816,187)
Fund Balance - Beginning of Year	<u>1,512,134</u>	<u>312,728</u>	<u>382,892</u>	<u>2,207,754</u>
Fund Balance - End of Year	<u>\$ 1,137,867</u>	<u>\$ 75,995</u>	<u>\$ 177,705</u>	<u>\$ 1,391,567</u>

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

City of Hernando, Mississippi
Reconciliation of Revenues, Expenditures and Changes in
Fund Balances of Governmental Funds to the Statement of Activities
For the Year Ended September 30, 2013

Net Change in Fund Balances - Total Governmental Funds	\$ (816,187)
<p>Amounts reported for governmental activities in the Statement of Activities are different because:</p>	
<p>Governmental funds report capital outlays as expenditures. However, in the Statements of Activities, the cost of those material assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which capital outlays of \$745,848 exceeded depreciation expense of \$653,106 in the current period.</p>	92,742
<p>Debt proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the Statement of Net Position. Repayment of debt principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the Statement of Net Position. This is the amount by which repayments of \$4,586,844 are exceed by amortization expense of \$77,700 and proceeds of \$4,668,668.</p>	(159,524)
<p>Some expenses reported in the Statement of Activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds. Those amounts by which the (increase) decrease consist of are as follows:</p>	
Accrued interest payable	74,915
Compensated absences payable	229,059
Bond issue costs	74,191
	74,191
Change in Net Position of Governmental Activities	\$ (504,804)

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

City of Hernando, Mississippi
Statement of Net Position – Proprietary Fund
September 30, 2013

	Utility Fund
Assets	
Current Assets	
Cash and cash equivalents	\$ 645,775
Accounts receivable , net of allowance for uncollectibles of \$225,052	498,889
Loan receivable	453,116
Prepaid expenses	22,539
Due from other funds	4,800
Total Current Assets	1,625,119
Noncurrent Assets	
Capital assets:	
Land and construction in progress	2,779,371
Other capital assets, net	7,792,137
Total Noncurrent Assets	10,571,508
Total Assets	\$ 12,196,627
Liabilities and Net Position	
Current Liabilities	
Accounts payable	\$ 553,593
Retainage payable	72,187
Accrued expenses	20,817
Due to other funds	63,405
Total Current Liabilities	710,002
Current Liabilities Payable From Restricted Assets:	
Customer deposits	349,795
Long-term liabilities due within one year:	
Capital debt	124,185
Total Current Liabilities Payable From Restricted Assets	473,980
Long-Term Liabilities Due in More Than One Year:	
Capital debt	4,028,348
Non-capital debt	21,430
Total Long-Term Liabilities	4,049,778
Total Liabilities	5,233,760
Net Position	
Invested in capital assets, net of related debt	6,418,975
Unrestricted	543,892
Total Net Position	6,962,867
Total Liabilities and Net Position	\$ 12,196,627

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

City of Hernando, Mississippi
Statement of Revenues, Expenses and
Changes in Net Position – Proprietary Fund
For the Year Ended September 30, 2013

	<u>Utility Fund</u>
Operating Revenues	
Sewer sales	\$ 1,980,280
Water sales	797,749
Sanitation sales	784,947
Miscellaneous	<u>12,024</u>
Total Operating Revenues	<u>3,575,000</u>
Operating Expenses	
Cost of sales	1,861,509
Personnel	1,062,193
Depreciation and amortization	482,344
Material and supplies	191,762
Repairs and maintenance	260,490
Other	<u>305,390</u>
Total Operating Expenses	<u>4,163,688</u>
Operating Income	<u>(588,688)</u>
Non-operating Revenues (Expenses)	
Grant proceeds	239,458
Interest income	1,398
Interest expense	(66,169)
Interfund transfers	57,300
Sales of asset	<u>9,619</u>
Total Non-operating Revenues (Expenses)	<u>241,606</u>
Change in Net Position	(347,082)
Net Position - Beginning of Year	<u>7,309,949</u>
Net Position - End of Year	<u>\$ 6,962,867</u>

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

City of Hernando, Mississippi
Statement of Cash Flows – Proprietary Fund
For the Year Ended September 30, 2013

	Utility Fund
Cash Flows From Operating Activities	
Cash received from customers	\$ 3,627,968
Cash payments for goods and services	(2,134,873)
Cash payments to employees	(1,119,340)
Net Cash Provided By (Used In) Operating Activities	373,755
Cash Flows From Non-Capital Financing Activities	
Interfund transfers	114,937
Net Cash Provided By (Used In) Non-Capital Financing Activities	114,937
Cash Flows From Capital and Related Financing Activities	
Payments for capital acquisitions	(1,798,955)
Proceeds from sale of assets	9,619
Customer deposits	3,718
Grant proceeds	114,293
Proceeds from debt issuance	2,629,585
Principal payments on debt	(1,333,679)
Interest payments on debt	(66,169)
Net Cash Provided By (Used In) Capital and Related Financing Activities	(441,588)
Cash Flows From Investing Activities	
Interest on investments	1,398
Net Cash Provided By (Used In) Investing Activities	1,398
Net Increase (Decrease) in Cash and Cash Equivalents	48,502
Cash and Cash Equivalents - Beginning of Year	597,273
Cash and Cash Equivalents - End of Year	\$ 645,775
Reconciliation of Operating Income to Net Cash	
Provided By (Used In) Operating Activities	
Operating Income	\$ (588,688)
Adjustments to reconcile operating income to net cash provided by (used in) operating activities:	
Depreciation and amortization	482,344
(Increase) decrease in customer receivables	52,968
(Increase) decrease in prepaid items	18,760
Increase (decrease) in accounts payable	394,225
Increase (decrease) in accrued expenses	(894)
Increase (decrease) in accrued compensated absences	(57,147)
Total adjustments	962,443
Net Cash Provided By (Used In) Operating Activities	\$ 373,755

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

City of Hernando, Mississippi
Notes to Financial Statements
For the Year Ended September 30, 2013

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General Statement

The City of Hernando (“the City”) was incorporated in 1866. The City operates under the Board of Aldermen-Mayor form of government and provides the following services; public safety, public works, culture and recreation, public improvements, planning and zoning, and general administrative services.

The financial statements of the City have been prepared in conformity with generally accepted accounting principles (“GAAP”) as applied to governmental units. The Governmental Accounting Standards Board (“GASB”) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The following is a summary of the more significant polices.

Financial Reporting Entity

These financial statements present all the accounts of the City. There are no component units as defined by GASB Statement 14, *The Financial Reporting Entity*.

Basis of Presentation

The government-wide financial statements (Statement of Net Position and the Statement of Activities) report information on all the activities of the City. The effect of interfund activity, within the governmental and business-type activities columns, has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The Statement of Activities demonstrates the degree to which the direct expenses of a given program are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific program. Program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services or privileges provided by a given program and 2) operating or capital grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Taxes and other items not properly included among program revenues are reported instead as general revenues. Indirect expenses are allocated to general government.

Fund Financial Statements

The City segregated transactions related to certain functions or activities into separate funds in order to aid financial management and to demonstrate legal compliance. Separate statements are presented for governmental and proprietary activities. These statements present each major fund as a separate column on the fund financial statements; all non-major funds are aggregated and presented in a single column.

Governmental funds are those funds through which most governmental functions typically are financed. The measurement focus of governmental funds is on the sources, uses and balance of current financial resources. The City has presented the following major governmental funds:

City of Hernando, Mississippi
Notes to Financial Statements
For the Year Ended September 30, 2013

General Fund:

The General Fund is the main operating fund of the City. This fund is used to account for all financial resources not accounted for in other funds. All general tax revenues and other receipts that are not restricted by law or contractual agreement to some other fund are accounted for in this fund. General operating expenditures, fixed charges and capital improvement costs that are not paid through other funds are paid from the General Fund.

Debt Service Fund:

The Debt Service Fund is used to account for the accumulation of resources for, and the payment of general long-term debt principal, interest, and related costs. The primary revenue source is local property taxes levied specifically for Debt Service.

Proprietary Funds

All proprietary funds are accounted for using the economic resources measurement focus and the accrual basis of accounting. The accounting objectives are determinations of net income, financial position, and cash flow. All assets and liabilities are included on the Statement of Net Position. The City has presented the following major proprietary fund:

Utility Fund:

The Utility Fund is used to account for the provision of water, sewer and sanitation services to the residents of the City. Activities of the fund include administration, operations and maintenance of the water and sewer system and sanitation services, as well as billing and collection activities. The fund also accounts for the accumulation of resources for, and the payment of, long-term debt principal and interest for water, sewer and sanitation debt. All costs are financed through charges to utility customers with rates reviewed regularly and adjusted if necessary to ensure integrity of the funds.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Operating expenses for the proprietary funds include the cost of personal and contractual services, supplies and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Measurement Focus/Basis of Accounting

Measurement focus refers to what is being measured; basis of accounting refers to when revenues and expenditure are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurement made, regardless of the measurement focus applied.

The government-wide statements and fund financial statements for proprietary funds are reported using the economic resources measurement focus and the accrual basis of accounting. The economic resources measurement focus means all assets and liabilities (whether current or non-current) are included on the Statement of Net Position and the operating statements present increases (revenues) and decreases (expenses) in net total position. Under the accrual basis of accounting, revenues are recognized when earned, including unbilled water, sewer and sanitation services which are accrued. Expenses are recognized at the time the liability is incurred.

City of Hernando, Mississippi
Notes to Financial Statements
For the Year Ended September 30, 2013

Governmental fund financial statements are reported using the current financial resources measurement focus and are accounted for using the modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues are recognized when susceptible to accrual; i.e., when they both become measurable and available. "Measurable" means the amount of the transaction can be determined and "available" means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. The City considers property taxes as available if they are collected within 60 days after year-end. A one-year availability period is used for recognition of all other governmental fund revenues. Expenditures are recognized when the related fund liability is incurred. However, debt service expenditures, except for interest payable accrued at the debt issuance date for which cash is received with the debt proceeds, as well as expenditures related to compensated absences are recorded only when payment has matured and will be payable shortly after year-end.

The revenues susceptible to accrual are property taxes, franchise fees, licenses, charges for services, interest income and intergovernmental revenues. Sales taxes collected and held by the state at year-end on behalf of the government are also recognized as revenue. All other governmental fund revenues are recognized when received, as they are deemed immaterial.

Budgets and Budgetary Accounting

The City follows these procedures in establishing the budgetary data reflected in the financial statements:

The City Charter establishes the fiscal year as the twelve-month period beginning October 1. The departments submit to the City Clerk a budget of estimated expenditures for the ensuing fiscal year after which the City Clerk submits a budget of estimated expenditure and revenues to the Mayor and Board of Aldermen by August 1.

Upon receipt of the budget estimates, the Board of Aldermen holds a public hearing on the proposed budget. Information about the budget ordinance is then published in the official newspaper of the City.

At the September board meeting, the budget is legally enacted through passage of ordinance. The City Clerk is authorized to transfer budgeted amounts between departments within any fund; however, any revisions that alter the total expenditures of any fund must be approved by the Board of Aldermen.

The actual receipts and disbursements are accumulated each month and compared to the budgeted amounts and reviewed by the Mayor and Board of Aldermen. Any revisions on the budget during the year are approved by the Board of Aldermen.

Cash and Cash Equivalents

For the purpose of the Statement of Net Position, "Cash and cash equivalents" includes all demand, savings accounts, and certificates of deposits of the City. For the purpose of the proprietary fund Statement of Cash Flows, "Cash and cash equivalents" include all demand and savings accounts, and certificates of deposit or short-term investments with an original maturity of three months or less.

Prepaid Expenses

Prepaid balances are for payments made by the City in the current year to provide services occurring in the subsequent fiscal year, and the reserve for prepaid expenses in the governmental funds has been recorded to signify that a portion of fund balance is not available for other subsequent expenditures.

City of Hernando, Mississippi
Notes to Financial Statements
For the Year Ended September 30, 2013

Loan Receivable

Loan Receivable consists of funds that have been requested prior to year-end and not yet received or a portion of expenses occurring before year-end allowable to be drawn down from available loan funds per the loan agreement.

Interfund Transactions and Balances

Transactions between funds that are representative of short-term lending/borrowing arrangements and transactions that have not resulted in the actual transfer of cash at the end of the fiscal year are referred to as "Due to/from other funds." Noncurrent portions of interfund receivables and payables are reported as "Advances to/from other funds." Advances between funds, when reported in the fund financial statements, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources. Interfund receivables and payable between funds within governmental activities are eliminated in the Statement of Net Position. Any outstanding balances between the governmental activities and business type activities are reported in the government-wide financial statements as "Internal balances."

Restricted Assets

Proprietary fund assets required to be held and/or used as specified in bond indentures, bond resolutions, trustee agreements, board resolutions and donor specifications have been reported as restricted assets. When both restricted and non-restricted assets are available for use, the policy is to use restricted assets first.

Capital Assets and Depreciation

Capital assets, which include property, plant, equipment, and infrastructure assets, are reported in the applicable governmental or business-type activities columns in the government-wide financial statements and in the fund financial statements for proprietary funds. All capital assets are valued at historical cost or estimated historical cost if actual historical cost is not available. Donated capital assets are capitalized at estimated fair market value on the date donated.

Depreciation of capital assets is computed and recorded by the straight-line method. Estimated useful lives of the various classes of depreciable capital assets are as follows:

- Buildings/improvements 20 to 40 years
- Infrastructure 20 to 50 years
- Equipment 3 to 10 years

Compensated Absences

The City has adopted a policy of compensation for accumulated unpaid employee personal leave. No payment is authorized for accrued major medical leave. Accounting principles generally accepted in the United States of America require accrual of accumulated unpaid employee benefits as long-term liabilities in the government-wide financial statements and proprietary fund financial statements. In fund financial statements, governmental funds report the compensated absence liability payable only if the payable has matured, for example an employee resigns or retires.

Fund Balances

In the governmental fund financial statements, fund balances are classified as follows:

- **Nonspendable** – Amounts that cannot be spent either because they are in a nonspendable form or because they are legally or contractually required to be maintained intact.

City of Hernando, Mississippi
Notes to Financial Statements
For the Year Ended September 30, 2013

- **Restricted** – Amounts that can be spent only for specific purposes because of the City Charter, the City Code, state or federal laws, or externally imposed conditions by grantors or creditors.
- **Committed** – Amounts that can be used only for specific purposes determined by a formal action by the Board of Aldermen ordinance or resolution.
- **Assigned** – Amounts that are designated by the Mayor for a particular purpose but are not spendable until a budget ordinance is passed or there is a majority vote approval (for capital projects or debt service) by the Board of Aldermen.
- **Unassigned** – All amounts not included in other spendable classifications.

When an expenditure/expense is incurred for purposes for which both restricted and unrestricted (committed, assigned, or unassigned) resources are available, it is the City's general policy to use restricted resources first. When expenditures/expenses are incurred for purposes for which unrestricted (committed, assigned, and unassigned) resources are available, and amounts in any of these unrestricted classifications could be used, it is the City's general policy to spend committed resources first, followed by assigned amounts, and then unassigned amounts.

Net Position

Net Position in the government-wide and proprietary fund financial statements is displayed in three components. "Net investment in capital assets" are capital assets, less accumulated depreciation and any outstanding debt related to the acquisition, construction or improvement of those assets. "Restricted net position" consists of net position with constraints placed on the use either by external groups such as creditors, grantors, contributors, or laws and regulations of other governments; or law through constitutional provisions enabling legislation. "Unrestricted net position" consists of all other net position not meeting the definition of "restricted" or "net investment in capital assets."

Property Tax Revenues

Restrictions associated with property tax levies vary with the statutory authority. The amount of increase in certain property taxes is limited by state law. Generally, this restriction provides that these tax levies shall produce no more than 110% of the amount which resulted from the assessments of the previous year.

The Board of Alderman, each year at a meeting in September, levies property taxes for the ensuing fiscal year which begins on October 1. Real property taxes become a lien on January 1 of the current year, and personal property taxes become a lien on March 1 of the current year. Taxes on both real and personal property, however, are due on or before February 1 of the next succeeding year. Taxes on motor vehicles and mobile homes become a lien are due in the month that coincides with the month of the original purchase.

Accounting principles generally accepted in the United States of America require property taxes to be recognized at the levy date if measurable and available. All property taxes are recognized as revenue in the year for which they are levied. Motor vehicle and mobile home taxes do not meet the measurability and collectability criteria for property tax recognition because the lien and due date cannot be established until the date of the original purchase occurs.

Changes in Accounting Standards

The City adopted GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, during the fiscal year changing the source of guidance for accounting and financial reporting. They also adopted GASB Statement No. 63, *Financial Reporting of Deferred Outflows*

City of Hernando, Mississippi
Notes to Financial Statements
For the Year Ended September 30, 2013

of Resources, Deferred Inflows of Resources, and Net Position during the year ended September 30, 2013. Statement No. 63 added new classifications on the statements of position and changed net assets to net position. These statements did not significantly impact any amounts reported in the financial statements.

NOTE B – CASH AND CASH EQUIVALENTS

The collateral for public entities’ deposits in financial institutions are held in the name of the State Treasurer under a program established by the Mississippi State Legislature and is governed by Section 27-105-5, Miss. Code Ann. (1972). Under this program, the entity’s funds are protected through a collateral pool administered by the State Treasurer. Financial institutions holding deposits of public funds must pledge securities as collateral against those deposits. In the event of failure of a financial institution, securities pledged by that institution would be liquidated by the State Treasurer to replace the public deposits not covered by the Federal Deposit Insurance Corporation (“FDIC”).

Custodial credit risk is the risk that, in the event of a financial institutions failure, the City’s deposits might not be recovered. The City does not have a deposit policy for custodial credit risk. As of September 30, 2013, the City’s bank balance was not exposed to custodial credit risk.

As of September 30, 2013, the carrying amount of the City’s deposits was \$1,912,293 and the bank balances totaled \$1,940,240. Of the bank balances, \$250,000 was insured by federal deposit insurance and \$1,690,240 was covered by pooled and/or pledged collateral with the State Treasurer.

NOTE C - INTERGOVERNMENTAL RECEIVABLES

Intergovernmental receivables consist of sales tax and franchise tax.

	<u>General Fund</u>
Ad valorem	\$ 11,359
Franchise and sales tax	316,835
Total	<u>\$ 328,194</u>

City of Hernando, Mississippi
Notes to Financial Statements
For the Year Ended September 30, 2013

NOTE D – CAPITAL ASSETS

	<u>Balance at 9/30/2012</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance at 9/30/2013</u>
Governmental Activities				
Capital assets, not being depreciated:				
Land	\$ 581,339	\$ -	\$ -	\$ 581,339
Construction in progress	58,043	1,250	(50,000)	9,293
Total capital assets, not being depreciated:	<u>639,382</u>	<u>1,250</u>	<u>(50,000)</u>	<u>590,632</u>
Capital assets, being depreciated:				
Buildings and improvements	5,627,896	-	-	5,627,896
Infrastructure	8,832,713	-	-	8,832,713
Equipment	1,920,991	716,462	(281,806)	2,355,647
Vehicles	983,469	78,136	-	1,061,605
Improvements other than buildings	463,979	-	-	463,979
Total capital assets, being depreciated:	<u>17,829,048</u>	<u>794,598</u>	<u>(281,806)</u>	<u>18,341,840</u>
Less accumulated depreciation for:				
Buildings and improvements	(1,464,190)	(112,162)	-	(1,576,352)
Infrastructure	(2,053,063)	(312,429)	-	(2,365,492)
Equipment	(1,618,285)	(160,638)	281,806	(1,497,117)
Vehicles	(907,252)	(49,523)	-	(956,775)
Improvements other than buildings	(70,957)	(18,354)	-	(89,311)
Total Accumulated Depreciation	<u>(6,113,747)</u>	<u>(653,106)</u>	<u>281,806</u>	<u>(6,485,047)</u>
Total Capital Assets, Being Depreciated, Net	<u>11,715,301</u>	<u>141,492</u>	<u>-</u>	<u>11,856,793</u>
Governmental Activities Capital Assets, Net	<u>\$ 12,354,683</u>	<u>\$ 142,742</u>	<u>\$ (50,000)</u>	<u>\$ 12,447,425</u>
Business-Type Activities				
Capital assets, not being depreciated:				
Land	\$ 52,930	\$ -	\$ -	\$ 52,930
Construction in progress	1,097,498	1,628,943	-	2,726,441
Total Capital Assets, Not Being Depreciated:	<u>1,150,428</u>	<u>1,628,943</u>	<u>-</u>	<u>2,779,371</u>
Capital assets, being depreciated:				
Infrastructure	13,344,319	-	-	13,344,319
Equipment	1,154,646	134,107	(30,157)	1,258,596
Vehicles	403,426	35,903	-	439,329
Total Capital Assets, Being Depreciated:	<u>14,902,391</u>	<u>170,010</u>	<u>(30,157)</u>	<u>15,042,244</u>
Less accumulated depreciation for:				
Infrastructure	(5,411,372)	(404,486)	-	(5,815,858)
Equipment	(1,033,014)	(34,645)	30,157	(1,037,502)
Vehicles	(353,534)	(43,213)	-	(396,747)
Total Accumulated Depreciation	<u>(6,797,920)</u>	<u>(482,344)</u>	<u>30,157</u>	<u>(7,250,107)</u>
Total Capital Assets, Being Depreciated, Net	<u>8,104,471</u>	<u>(312,334)</u>	<u>-</u>	<u>7,792,137</u>
Business-Type Activities Capital Assets, Net	<u>\$ 9,254,899</u>	<u>\$ 1,316,609</u>	<u>\$ -</u>	<u>\$ 10,571,508</u>

No interest was capitalized during the year due to immateriality.

City of Hernando, Mississippi
Notes to Financial Statements
For the Year Ended September 30, 2013

A summary of depreciation expense by function is as follows:

Governmental Activities:	
General government	\$ 63,597
Public safety	249,448
Public works	294,248
Culture and recreation	45,813
Total Governmental Activities Depreciation Expense	\$ 653,106
Business-Type Activities:	
Utility	\$ 482,344
Total Business-Type Activities Depreciation Expense	\$ 482,344

Commitments under construction at September 30, 2013 are summarized as follows:

<u>Project</u>	<u>Contract Amount</u>	<u>Remaining Balance</u>	<u>Fund</u>
Lagoon Project			
Contract #1	\$ 190,000	\$ 15,400	Utility
Contract #2	1,775,629	843,159	Utility

NOTE E - INTERFUND TRANSACTIONS

Interfund transactions are for the payment of monthly claims, and to provide funds for debt service and capital outlay. All transfers were routine and consistent with the activities of the fund, and all interfund balances are expected to be repaid within a year. The following is a summary of interfund transactions and balances as of September 30, 2013:

	<u>Due From</u>	<u>Due To</u>
Major Funds:		
General fund	\$ 121,235	\$ 38,096
Nonmajor funds	24,436	28,867
Utility fund	4,800	63,405
Total Funds	\$ 150,471	\$ 150,471
	<u>Transfer In</u>	<u>Transfer Out</u>
Major Funds:		
Nonmajor funds	\$ -	\$ 57,300
Utility fund	57,300	-
Total Funds	\$ 57,300	\$ 57,300

City of Hernando, Mississippi
Notes to Financial Statements
For the Year Ended September 30, 2013

NOTE F - LONG-TERM DEBT

Long-term debt activity for the year ended September 30, 2013 was as follows:

	<u>Balance at 9/30/2012</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance at 9/30/2013</u>	<u>Amounts Due Within One Year</u>
Governmental Activities:					
General obligation bonds payable	\$ 7,900,000	\$ 3,496,168	\$ 4,067,500	\$ 7,328,668	\$ 210,000
Notes payable	-	68,000	6,449	61,551	13,252
Loan payable	-	500,000	500,000	-	-
Leases payable	-	604,500	4,224	600,276	32,263
Compensated absences payable	401,089	-	229,059	172,030	-
Governmental Activities Long-Term Liabilities	<u>\$ 8,301,089</u>	<u>\$ 4,668,668</u>	<u>\$ 4,807,232</u>	<u>\$ 8,162,525</u>	<u>\$ 255,515</u>
Business-Type Activities:					
General obligation bonds payable	\$ -	\$ 968,832	\$ 27,500	\$ 941,332	\$ -
Notes payable	2,849,991	1,541,545	1,282,342	3,109,194	100,884
Leases payable	6,636	119,208	23,837	102,007	23,301
Compensated absences payable	78,577	-	57,147	21,430	-
Business-Type Activities Long-Term Liabilities	<u>\$ 2,935,204</u>	<u>\$ 2,629,585</u>	<u>\$ 1,390,826</u>	<u>\$ 4,173,963</u>	<u>\$ 124,185</u>

General obligation bonds are direct obligations and pledge the full faith and credit of the City. General obligation bonds outstanding as of September 30, 2013 are as follows:

<u>Description</u>	<u>Interest Rate</u>	<u>Issue Date</u>	<u>Maturity Date</u>	<u>Amount</u>	
				<u>Issued</u>	<u>Outstanding</u>
2007	Various	5/31/2007	5/1/2027	\$ 5,000,000	\$ 3,930,000
2012	Various	11/8/2012	10/1/2023	4,465,000	4,340,000
Total General Obligation Bonds				<u>\$ 9,465,000</u>	<u>\$ 8,270,000</u>

Notes payable as of September 30, 2013 are as follows:

<u>Description</u>	<u>Interest Rate</u>	<u>Issue Date</u>	<u>Maturity Date</u>	<u>Amount</u>	
				<u>Issued</u>	<u>Outstanding</u>
First Security Note - Parks Equipment	1.85%	3/17/2013	3/15/2018	\$ 68,109	\$ 61,551
Subtotal Governmental Activities				<u>68,109</u>	<u>61,551</u>
Dept. of Econ. and Community Dev. - Sewer Cap Loan	3.00%	10/31/2002	10/31/2021	288,000	137,880
Dept. of Environ. Quality - Water Pollution Control	1.75%	6/1/2003	1/1/2023	508,741	264,199
Dept. of Econ. and Community Dev. - Sewer Cap Loan	2.00%	2/1/2005	2/1/2025	237,400	146,702
Dept. of Econ. and Community Dev. - Sewer Cap Loan	3.00%	11/1/2005	11/1/2025	191,116	135,589
State of Mississippi - DWSIRLF	1.95%	11/5/2012	10/15/2032	1,141,966	893,262
Dept. of Environmental Quality - Water Pollution Control				1,531,562	1,531,562
Subtotal Business-Type Activities				<u>3,898,785</u>	<u>3,109,194</u>
Total Business-Type Activities				<u>\$ 3,966,894</u>	<u>\$ 3,170,745</u>

City of Hernando, Mississippi
Notes to Financial Statements
For the Year Ended September 30, 2013

The aggregate maturities of general obligation bonds and notes for the years subsequent to September 30, 2013 are as follows:

Year ending September 30	Governmental Activities Fund		Business-Type Activities Fund	
	Principal	Interest	Principal	Interest
2014	\$ 223,252	\$ 193,371	\$ 100,884	\$ 42,298
2015	540,499	214,379	272,405	75,462
2016	558,551	197,558	278,285	70,000
2017	576,607	182,247	284,241	64,418
2018	592,462	166,428	290,277	58,714
2019-2023	3,182,800	573,473	1,478,125	204,189
2024-2028	1,716,048	142,643	873,551	81,383
2029-2033	-	-	472,758	14,580
2034	-	-	-	-
Total	\$ 7,390,219	\$ 1,670,099	\$ 4,050,526	\$ 611,044

Future minimum capital lease payments and the net present value of these future minimum lease payments as of September 30, 2013 were as follows:

Year Ending September 30	Governmental Activities		Business-type Activities	
	Principal	Interest	Principal	Interest
2014	\$ 32,263	18,446	\$ 23,301	\$ 1,654
2015	33,294	17,415	23,726	1,228
2016	34,358	16,351	24,159	795
2017	35,456	15,252	24,600	354
2018	36,589	14,119	6,221	19
2019-2023	201,250	52,291	-	-
2024-2028	227,066	18,021	-	-
Total	\$ 600,276	151,895	\$ 102,007	\$ 4,050

Current and Advance Refunding – On November 8, 2012, the City issued \$4,465,000 in General Obligation Refunding Bonds, Series 2012, with an interest rate of 2.00% - 2.50% for the current refunding of three Drinking Water Improvement Loans and for the advance refunding of certain outstanding maturities of the \$3,500,000 General Obligation Bonds, Series 2003 and the advance refunding of certain outstanding maturities of the \$2,000,000 General Obligation Bonds, Series 2003.

The three Drinking Water Improvement Loans currently refunded are as follows:

Issue	Average Interest Rate	Outstanding Amount Refunded
2002 DWSIRLF Loan	3.00%	\$ 399,236
2003 DWSIRLF Loan	3.00%	226,565
2006 DWSIRLF Loan	2.50%	330,266
Total		\$ 956,067

City of Hernando, Mississippi
Notes to Financial Statements
For the Year Ended September 30, 2013

The \$3,500,000 General Obligation Bonds, Series 2003 had an outstanding balance of \$2,295,000 at the time of refunding, but only \$2,130,000, of the bond was refunded, leaving a remaining principal balance of \$165,000 of which the City paid September 2013.

The \$2,000,000 General Obligation Bonds, Series 2003 had an outstanding balance of \$1,315,000 at the time of refunding, but only \$1,220,000 of the bond was refunded, leaving a remaining principal balance of \$95,000 which the City paid in April 2013 to pay off the bond.

The remaining net proceeds of \$3,450,906 (after payment of underwriting fees and other issuance costs) were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the bonds. As a result, those bonds are considered to be defeased, and the liability for those bonds has been removed from the Statement of Net Position.

The City refunded the above bonds to reduce its total debt service payments over the next 11 years by almost \$239,143 and to obtain an economic gain (difference between the present value and the debt service payments on the old and new debt) of \$227,813.

Legal debt margin. The City is subject to the limitations of indebtedness prescribed by Section 21-33-303, Miss. Code Ann. (1972). No municipality may issue bonds secured by a pledge of its full faith and credit in an amount which, when added to the then outstanding bond indebtedness of such municipality, would exceed the 15% and 20% tests prescribed in Section 21-33-303. These percentages are applied to the assessed value of the taxable property within such municipality, with certain types of bond issues being excluded from the authorized debt limit tests. Presented in the schedule below are the calculations of the applicable statutory debt limitations and the resulting margin for further debt in the amount of \$13,543,061 (the smaller of the two computed margins) as of September 30, 2013.

	<u>15% Test</u>	<u>20% Test</u>
Assessed value as of September 30, 2013:		
\$139,144,859 times applicable percentage	\$ 20,871,729	\$ 27,828,972
Less present debt subject to debt limits as of September 30, 2013:		
Total bonds outstanding (excluding proprietary)	<u>(7,328,668)</u>	<u>(7,328,668)</u>
Margin for additional debt	<u>\$ 13,543,061</u>	<u>\$ 20,500,304</u>

In December 2007, the City entered into an agreement with the City of Southaven, Mississippi whereby the City of Southaven will design and construct a sewer system ("the Hurricane Creek Project") by which it will collect and transport wastewater through the City of Hernando to the DeSoto County Regional Utility Authority's sewer system for treatment and disposal. Upon completion, the City of Hernando will operate and maintain the sewer line. Further, the City has agreed to pay the City of Southaven \$1,000,000 over seven years to reimburse the City of Southaven for its portion of the construction costs.

The City will make the first annual payment to the City of Southaven within sixty days of completion of the project, and then annually on October 1. The project is scheduled to be finished in June 2015 and debt payments should begin in October 2015.

City of Hernando, Mississippi
Notes to Financial Statements
For the Year Ended September 30, 2013

NOTE G – DEFINED BENEFIT PENSION PLAN

Plan Description. The City contributes to the Public Employees' Retirement System of Mississippi ("PERS"), a cost-sharing multiple-employer defined benefit pension plan. PERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit provisions are established by state law and may be amended only by the State of Mississippi Legislature. PERS issues a publicly available financial report that includes financial statements and required supplementary information. That information may be obtained by writing to Public Employee Retirement System, PERS Building, 429 Mississippi Street, Jackson, MS 39201-1005 or by calling (601) 359-3589 or 1-800-444 PERS.

Funding Policy. At September 30, 2013, PERS members were required to contribute 9% of their annual covered salary and the City is required to contribute at an actuarially determined rate. The rate at September 30, 2013 was 15.75% of annual covered payroll. The contribution requirements of PERS members are established and may be amended only by the State of Mississippi Legislature. The City's contributions (employer share only) to PERS for the years ending September 30, 2013, 2012 and 2011 were \$761,087, \$661,818, and \$606,362 respectively, equal to the required contributions for each year.

NOTE H – RISK MANAGEMENT

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters. This exposure is covered by purchase of commercial insurance.

NOTE I – LITIGATION

The City is subject to various legal proceedings in various stages of litigation, the outcome of which is not determinable at this time. Management of the City and its legal counsel do not anticipate that there will be a material effect on the financial statements as a result of the cases presently in progress.

NOTE J – SUBSEQUENT EVENTS

Management has evaluated subsequent events through June 27, 2014, which is the date the financial statements were available to be issued.

In December 2013, the City signed a Series 2013 Tax Anticipation Note in the amount of \$1,000,000 with an interest rate of .96%. The City actually borrowed \$450,000 and paid back the amount in full in February 2014.

REQUIRED SUPPLEMENTARY INFORMATION

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City of Hernando, Mississippi
Budgetary Comparison Schedule – General Fund
For the Year Ended September 30, 2013

	Budgeted Amounts		Actual Amounts Budgetary Basis	Variance with Final Budget
	Original	Final		
Revenues				
General property taxes	\$ 2,696,440	\$ 2,696,440	\$ 2,970,847	\$ 274,407
Franchise taxes	385,000	385,000	360,820	(24,180)
Intergovernmental	3,240,400	4,611,846	3,060,296	(1,551,550)
Licenses and permits	550,500	550,500	224,692	(325,808)
Charges for services	350,000	450,000	337,513	(112,487)
Fines and forfeitures	301,200	301,200	417,848	116,648
Interest	-	-	5,044	5,044
Miscellaneous	129,000	129,000	124,988	(4,012)
Total Revenues	7,652,540	9,123,986	7,502,048	(1,621,938)
Expenditures				
General government	1,050,608	1,089,332	1,283,117	(193,785)
Public safety	6,093,742	6,079,565	5,608,384	471,181
Public works	300,440	300,440	311,841	(11,401)
Health and welfare	-	-	115,106	(115,106)
Capital outlay	745,000	2,079,222	1,134,130	945,092
Debt service	400,750	513,427	513,711	(284)
Total Expenditures	8,590,540	10,061,986	8,966,289	1,095,697
Excess (deficiency) of revenues over (under) expenditures	(938,000)	(938,000)	(1,464,241)	(526,241)
Other Financing Sources (Uses)				
Grant revenue	180,000	180,000	62,038	(117,962)
Loan proceeds	-	-	1,104,500	1,104,500
Interfund transfers	758,000	758,000	-	(758,000)
Sale of assets	-	-	250	250
Total Other Financing Sources (Uses)	938,000	938,000	1,166,788	228,788
Net Change in Fund Balances	\$ -	\$ -	(297,453)	\$ (297,453)
Fund Balance - Beginning of Year			1,512,133	
Fund Balance - End of Year			1,214,680	
Adjustments to Conform with GAAP:				
Revenues			(76,813)	
Expenditures			-	
Fund Balance - End of Year (GAAP Basis)			\$ 1,137,867	

City of Hernando, Mississippi
Notes to the Required supplementary Information
For the Year Ended September 30, 2013

Notes to the Required Supplementary Information

(A) Budgetary Information.

Statutory requirements dictate how and when the City's budget is to be prepared as noted in Note A. The completed budget for the fiscal year includes for each fund every source of revenue, each general item of expenditure, and the unencumbered cash and investment balances. When during the fiscal year it appears to the Board of Aldermen that budgetary estimates will not be met, they may make revisions to the budget.

The City's budget is prepared principally on the cash basis of accounting. All appropriations lapse at year end, and there are no encumbrances to budget because state law does not require that funds be available when goods or services are ordered, only when payment is made.

(B) Basis of Presentation.

The Statement of Revenues, Expenditures and Changes in Fund Balance - Budget and Actual presents the original legally adopted budget, the final legally adopted budget, actual amounts on a budgetary (Non-GAAP Basis) and variances between the final budget and the actual amounts. The schedule is presented for the General Fund and each major Special Revenue Fund. The Statement of Revenues, Expenditures and Changes in Fund Balance – Budget and Actual is a part of required supplemental information.

(C) Budget/GAAP Reconciliation.

The major differences between the budgetary basis and the GAAP basis are:

1. Revenues are recorded when received in cash (budgetary) as opposed to when susceptible to accrual (GAAP).
2. Expenditures are recorded when paid in cash (budgetary) as opposed to when susceptible to accrual (GAAP).

(D) Excess of Actual Expenditures over Budget in Individual Funds.

Section 21-35-17, Miss. Code Ann. (1972)

The City exceeded the final adopted budget for general government expenditures, public works, health and welfare, and debt service.

OTHER INFORMATION

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City of Hernando, Mississippi
Surety Bond Coverage
September 30, 2013

Surety bonds in force at September 30, 2013 were as follows:

<u>Name</u>	<u>Position</u>	<u>Insurance Company</u>	<u>Bond</u>
Willis W. Johnson	Mayor	Travelers Casualty and Surety Co.	\$100,000
Sonny Bryant	Alderman	Brierfield Insurance Co.	\$100,000
Gary N. Higdon	Alderman	Brierfield Insurance Co.	\$100,000
Jeff Hobbs	Alderman	Brierfield Insurance Co.	\$100,000
Sam Lauderdale	Alderman	Brierfield Insurance Co.	\$100,000
Cathy Brooks	Alderman	Brierfield Insurance Co.	\$100,000
Andrew Miller	Alderman	Brierfield Insurance Co.	\$100,000
Michael McLendon	Alderman	Brierfield Insurance Co.	\$100,000
Katie Subia	City Clerk	Travelers Casualty and Surety Co.	\$50,000
Carla Leigh Scallorn	Deputy Clerk	Travelers Casualty and Surety Co.	\$50,000
Cassandra E. Perry	Court Clerk	Travelers Casualty and Surety Co.	\$50,000
Robin Luttrell	Deputy Court Clerk	Travelers Casualty and Surety Co.	\$50,000
Donna Riles	Deputy Court Clerk	Travelers Casualty and Surety Co.	\$50,000
Kristin Duggan	Planning Clerk	Travelers Casualty and Surety Co.	\$50,000
Julie Harris	Deputy Clerk	Travelers Casualty and Surety Co.	\$50,000
Dot Hughes	Deputy Clerk	Travelers Casualty and Surety Co.	\$50,000
Shelly Johnstone	Deputy Clerk	Travelers Casualty and Surety Co.	\$50,000
Casey Nicole Kee	Deputy Clerk	Travelers Casualty and Surety Co.	\$50,000
Debra Tipton	Deputy Clerk	Travelers Casualty and Surety Co.	\$50,000
Tiffany Brown	Deputy Clerk	Travelers Casualty and Surety Co.	\$50,000
Susan Renee Holloway	Deputy Clerk	Travelers Casualty and Surety Co.	\$50,000
James M. Riley	Police Chief	Travelers Casualty and Surety Co.	\$50,000
Shane Ellis	Asst. Police Chief	Travelers Casualty and Surety Co.	\$50,000
Tarra Davis	Police Officer	Travelers Casualty and Surety Co.	\$50,000
Dewayne Williams	Park Director	Travelers Casulity and Surety Co.	\$50,000
Daniel Carson	Asst. Parks Director	Travelers Casulity and Surety Co.	\$50,000
Amidah Jordan	Parks Receptionist	Travelers Casulity and Surety Co.	\$50,000
Marshall Shane Dyson	Program Coordinator	Travelers Casulity and Surety Co.	\$50,000
Jared Darby	Director of Planning	Travelers Casulity and Surety Co.	\$50,000
Jacob A. Hisaw	Animal Control Officer	Travelers Casulity and Surety Co.	\$50,000

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SPECIAL REPORTS

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

Mayor and Board of Aldermen
City of Hernando
Hernando, Mississippi

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hernando, Mississippi ("the City"), as of and for the year ended September 30, 2013, and the related notes to the financial statements, which collectively comprise the City's basic financial statements, and have issued our report thereon dated June 27, 2014.

Internal Control Over Financial Reporting

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

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings and Responses as items 13-1, 13-2, 13-3, 13-4, and 13-5 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Findings and Responses as item 13-3.

We also noted certain matters which we have reported to the management of the City in the Independent Auditors' Report on Compliance with State Laws and Regulations dated June 27, 2014, included with this document.

City of Hernando, Mississippi's Responses to Findings

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

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Williams, Pitts & Beard, PLLC

Williams, Pitts and Beard, PLLC

Hernando, Mississippi

June 27, 2014

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH STATE LAWS AND REGULATIONS

Mayor and Board of Aldermen
City of Hernando, Mississippi

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Hernando, Mississippi ("the City") as of and for the year ended September 30, 2013 and have issued our report thereon dated June 27, 2014. We have conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*.

As required by the state legal compliance audit program prescribed by the Office of the State Auditor, we have also performed procedures to test compliance with certain state laws and regulations. However, providing an opinion on compliance with state laws and regulations was not an objective of our audit and, accordingly, we do not express such an opinion.

The results of those procedures and our audit of the general purpose financial statements disclosed the following material instance of noncompliance with state laws and regulations. Our finding and recommendation and your response is as follows:

1. **Finding-** Section 21-35-17, Miss. Code Ann. (1972) requires that the governing authorities shall not approve any claim and the city clerk shall not issue warrant for any expenditure in excess of said detailed budget appropriations as finally adopted, or as revised under the provisions of this chapter, except upon an order of a court competent jurisdiction or for an emergency, as provided in this chapter. See the budgetary comparison schedule on page 27 for expenditures in excess of budgeted appropriations.

Recommendation- The governing authorities and City Clerk should ensure no expenditures exceed the final adopted budget as required in Section 21-35-17, Miss. Code Ann. (1972).

Response- We are working on changing our budget process to keep track of and record revenues and expenses that were not budgeted for.

2. **Finding-** The City is not completing a thorough inventory of all fixed assets owned by the municipality at the end of the fiscal year in accordance with the Mississippi Municipal Audit and Accounting Guide.

Recommendation- The City should follow the yearly inventory procedures as outlined in the Mississippi Municipal Audit and Accounting Guide.

Response- We will change our process to make sure that the yearly inventory and fixed assets are completed and recorded properly.

3. **Finding-** Unclaimed checks over five years old have not been transferred to the State Treasurer as prescribed by Miss. Code Ann. (1972), Section 89-12-14.

Recommendation- The City should periodically (at least annually) review outstanding checks, and transfer those amounts greater than five years old to the State Treasurer.

Response- We are working on changing our process to make sure this is done in order to comply with Miss. Code Ann. (1972), Section 89-12-14.

The Office of the State Auditor or a public accounting firm will review, on a subsequent year's audit engagement, the findings in this report to ensure that corrective action has been taken.

The City's responses to the findings included in this report were not audited, and accordingly, we express no opinion on them.

This report is intended for the information of the City's management and the Office of the State Auditor and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Williams, Pitts & Beard, PLLC

Williams, Pitts & Beard, PLLC
Hernando, Mississippi
June 27, 2014

City of Hernando, Mississippi
Schedule of Findings and Responses
September 30, 2013

Section 1: Summary of Auditor's Results

Financial Statements:

1.	Type of auditor's report issued on the financial statements	Unmodified
2.	Material noncompliance relating to the financial statements	Yes
3.	Internal control over financial reporting:	
	a. Material weakness(es) identified?	Yes
	b. Significant deficiency(ies) identified that are not considered to be material weaknesses?	None Reported

Section 2: Financial Statements Findings

Material Weakness

13-1 Criteria: Part of effective internal controls over financial reporting is the ability to properly produce financial statements in accordance with generally accepted accounting principles ("GAAP"). Management is responsible for ensuring that all items are reported correctly on the City's financial statements.

Condition: The City relies on external auditors for assistance with the preparation of external financial statements and related note disclosures in conformity with GAAP. Under auditing standards generally accepted in the United States of America, outside auditors cannot be considered part of the City's internal control structure. The City does not have documented procedures in place that prevent or detect material misstatements in the external financial statements. However, the City's management reviewed and approved all adjustments.

Effect: Due to this oversight, the external auditors discovered and proposed material adjusting journal entries to the financial statements. Also, the lack of effective internal control over financial statements could result in misstatements of accounts on the City's financial statements.

Cause: The City has not designated internal control procedures or provided staffing to prepare external financial statements and, consequently, relies on its external auditors for this function.

Recommendation: Management should ensure that the financial statements are being prepared in accordance with GAAP.

Response: We are making changes in our process to prevent needing these adjustments at the end of the year.

City of Hernando, Mississippi
Schedule of Findings and Responses
September 30, 2013

13-2 Criteria: Part of effective internal controls over financial reporting is the ability to reconcile bank accounts to their corresponding accounts in the general ledger and ensure that it is performed in a timely manner.

Condition: The City was not timely reconciling all their bank statements to the general ledger.

Effect: Material transactions may not be recorded and the cash balance could be misstated.

Cause: Staff did not have the skills or proper training to reconcile the bank statements and the process was not being monitored by management to ensure it was performed in a timely manner.

Recommendation: All bank statements should be reconciled to the general ledger each month and the process should be complete within a week of receiving the bank statements. Management should review the monthly reconciliations for errors, omissions, unusual reconciling items and for the timeliness of the procedure. The reviewer should sign and date the reconciliation to note the date of the review.

Response: There was a bank statement for one fund that was not reconciled for months, when our new employee started, she had to go back to reconcile months of the one fund. The bank statements are now caught up and this should not happen again.

13-3 Criteria: The City is required to develop and maintain a complete and accurate accounting of fixed assets. Subsidiary ledgers should be used to track and record all inventory and fixed assets for the City. This ending balance per the subsidiary ledger should be reconciled to the general ledger on a monthly basis. Also the additions to the subsidiary ledger should be reconciled to the City's capital outlay accounts at year end noting the reason for amounts in capital outlay that do not tie to current year additions.

Condition: The City was not reconciling their subsidiary fixed asset ledger to the general ledger and not ensuring that all items that should be capitalized were added to the ledger.

Effect: The City had improper items that were added to the ledger causing the ledger to be materially misstated. At year end a thorough inventory of all fixed assets was not taken in accordance with the Mississippi Municipal Audit and Accounting Guide.

Cause: Staff did not have the skills or proper training to keep and reconcile the fixed asset ledger, and the process was not being monitored by management to ensure it was properly performed.

Recommendation: Complete and accurate records and subsidiary ledgers should be maintained for all inventory and fixed assets in accordance with the Mississippi Municipal Audit and Accounting Guide. At the end of each fiscal year a thorough inventory of all fixed assets owned by the municipality must be made according to the guidelines set forth in the Mississippi Municipal Audit and Accounting Guide.

Response: We are changing our process to make sure that the fixed assets are reconciled and added to the ledger correctly.

13-4 Criteria: Part of effective controls over financial reporting is the proper classification of revenues and expenses in accordance with GAAP. Revenues should be recorded separately from expenses and be reported separately on the financial statement.

Condition: The external auditors discovered certain grant revenues recorded in expense accounts and sales tax revenue was recorded at the net amount, excluding amounts withheld for debt service, instead of at the gross amount of revenue.

City of Hernando, Mississippi
Schedule of Findings and Responses
September 30, 2013

Effect: Material sales tax revenues and grant revenues as well as debt service and public safety expenditures could be materially understated in the financial statements.

Cause: The City has not designed internal control procedures to appropriately monitor the recording of revenue and to ensure that all revenue transactions are properly classified.

Recommendation: Management should develop internal control procedures to ensure that all revenue transactions are properly recorded and classified.

Response: We are changing our process to make sure that items are keyed to the correct account, and will be monitoring to make sure all transactions are properly classified.

13-5 Criteria: Effective internal control over financial reporting includes robust oversight and monitoring, proper documentation of transactions and adequate segregation of duties.

Condition: Audit procedures identified lack of management oversight including insufficient monitoring, and improper segregation of duties. The City bookkeeper makes adjusting journal entries and reconciles the bank statements without proper approval and documentation of approval on adjustments.

Effect: Improper material adjustments could go undetected causing the financial statements to be materially misstated.

Cause: The City has not designed internal control procedures to appropriately monitor the adjusting journal entries.

Recommendation: Management should make changes to the City's internal control structure over adjusting entries. Management should review and approve all adjusting journal entries and note their approval by signing and dating all adjusting journal entries.

Response: We are changing our procedures to make sure that proper approval and documentation are made on future adjustments and bank statement reconciliations.