

HIBBING PUBLIC UTILITIES

2018

Audited Financial Statements and Auditors Letters

June 25, 2019

Audited Financial Statements

- ▶ Independent Auditor's Report
- ▶ Management Discussion & Analysis (MD&A)
- ▶ Financial Statements - single year
- ▶ Supplementary Information
- ▶ Report on Internal Control
- ▶ Independent Auditor's Report on Supplementary Information
- ▶ Schedules of Department Revenue and Expenses

Independent Auditor's Report

- ▶ Sterle & Company LTD
- ▶ Management is responsible for financial statements
- ▶ Auditor's responsibility - express opinion
- ▶ Unmodified (clean) opinion - present fairly, in all material respects, the respective financial position of the business-type activities

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of the Hibbing Public Utilities Commission, as of December 31, 2018, and the respective changes in financial position and cash flows thereof, for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Independent Auditor's Report

- ▶ Emphasis of Matter - *GASB 75 Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*

Emphasis of Matter

As described in Note 15 of the notes to the basic financial statements, the Commission has implemented Governmental Accounting Standards Board (GASB) Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions* during the year ended December 31, 2018. Our opinion is not modified with respect to this matter.

- ▶ Required supplementary information
- ▶ Report on internal control over financial reporting and compliance with certain laws, regulations, contracts, grants, and other matters

Management Discussion and Analysis

- ▶ Not audited
- ▶ From management
- ▶ Net position of the Utility increased by 242% \$69.6 million
 - ❖ Investment in LEA increased by \$58.1 million
 - ❖ Federal grant of \$28 thousand
 - ❖ Capital Contribution from City of Hibbing of \$415 thousand
 - ❖ LEA termination payment of \$9 million
 - ❖ LEA wind-down payment of \$2.3 million
- ▶ Cash increased by \$3.5 million due to operating activities, LEA distributions, and limited capital investments
- ▶ Designated \$250,000 of Net Position for OPEB

Statement of Net Position

(Balance Sheet)

- ▶ Cash increase and designated cash for OPEB
- ▶ Investments increased
- ▶ Accounts Receivable increased
- ▶ Restricted cash decreased
- ▶ PP&E decreased
- ▶ Accounts Receivable - LEA decreased to \$14 thousand
- ▶ Equity in joint venture increased \$58.1 million
- ▶ Current liabilities decreased - amount owed to the City of Hibbing = 1 month
- ▶ Long-term debt decreased - paid off capital lease for dump truck and bank loan
- ▶ Unrestricted net position increased greatly - \$67.8 million

Statement of Revenues, Expenses and Changes in Net Position

(Income Statement)

- ▶ Operating Revenue increased \$1.288 million to a total \$28.4 million
 - ▶ Electric was greatest contributor to total operating revenue at 54% or \$15.3 million and increased 6% from 2017 revenue
 - ▶ Gas was next contributing 25% to total operating revenue or \$7 million and slightly decreased less than 1% in revenue from 2017
 - ▶ Steam contributed 12% to total operating revenue or \$3.46 million and increased 2% from 2017
 - ▶ Water contributed \$2.6 million or 9% of total operating revenue and increased 6% from 2017

Statement of Revenues, Expenses and Changes in Net Position

(Income Statement)

- ▶ Operating Revenue increased \$1.288 million to a total \$28.4 million

	<u>Electric</u>	<u>Steam</u>	<u>Gas</u>	<u>Water</u>	<u>Total</u>
Operating Revenues					
Sales and services	\$ 15,341,755	\$ 3,466,792	\$ 7,041,356	\$ 2,612,308	\$ 28,462,211
Operating Expenses					
Operation costs	10,072,792	1,586,303	3,514,040	839,656	16,012,791
Maintenance expense	292,316	100,729	20,214	77,320	490,579
Distribution expense	1,501,797	793,505	683,769	1,179,866	4,158,937
General overhead	5,166,120	1,782,216	1,024,539	455,919	8,428,794
Total Operating Expenses	<u>17,033,025</u>	<u>4,262,753</u>	<u>5,242,562</u>	<u>2,552,761</u>	<u>29,091,101</u>
Operating Income (Loss)	<u>\$ (1,691,270)</u>	<u>\$ (795,961)</u>	<u>\$ 1,798,794</u>	<u>\$ 59,547</u>	<u>\$ (628,890)</u>

Statement of Revenues, Expenses and Changes in Net Position

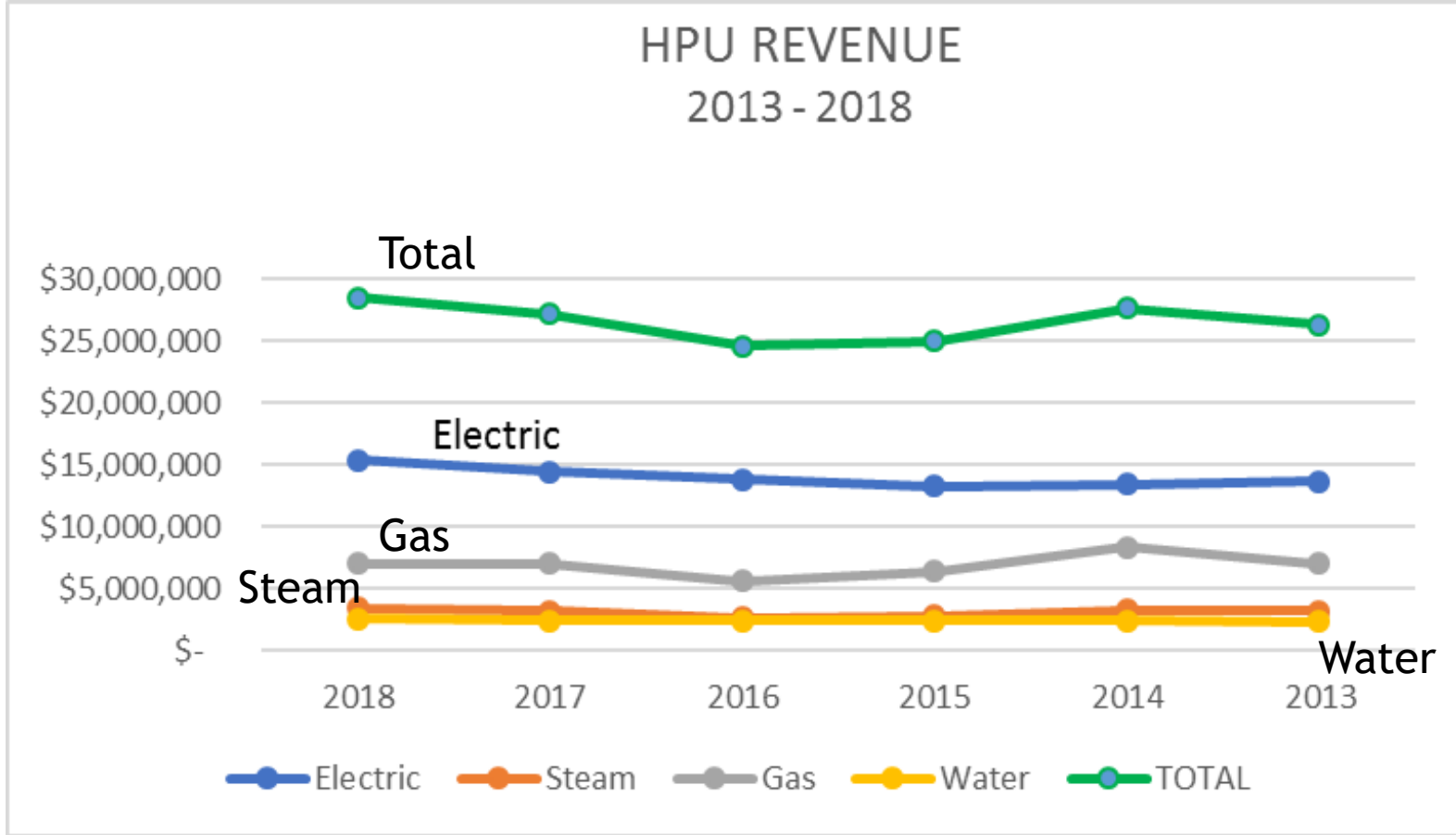
(Income Statement)

- ▶ Nonoperating Revenue (Expenses) increased \$66.8 million to a total \$69.8 million
 - ▶ Joint venture member distributions - LEA = \$11.4 million
 - ▶ Equity interest in joint venture - LEA = \$58.1 million
 - ▶ Capital grant = \$28 thousand
 - ▶ Capital asset transfer from City of Hibbing = \$415 thousand

Statement of Revenues, Expenses and Changes in Net Position

(Income Statement)

Operating Loss	<u>(628,890)</u>
Nonoperating Revenues (Expenses)	
Interest income	87,959
Late payment penalties	210,566
Other income	148,797
Joint venture member distributions	11,406,667
Equity interest in joint venture increase in net assets	58,111,022
Interest expense	(130,055)
Total Nonoperating Revenues (Expenses)	<u>69,834,956</u>
Income Before Capital Grant	69,206,066
Capital Grants	28,444
Capital Asset Transfer from City of Hibbing	<u>415,976</u>
Increase in Net Position	<u><u>\$ 69,650,486</u></u>

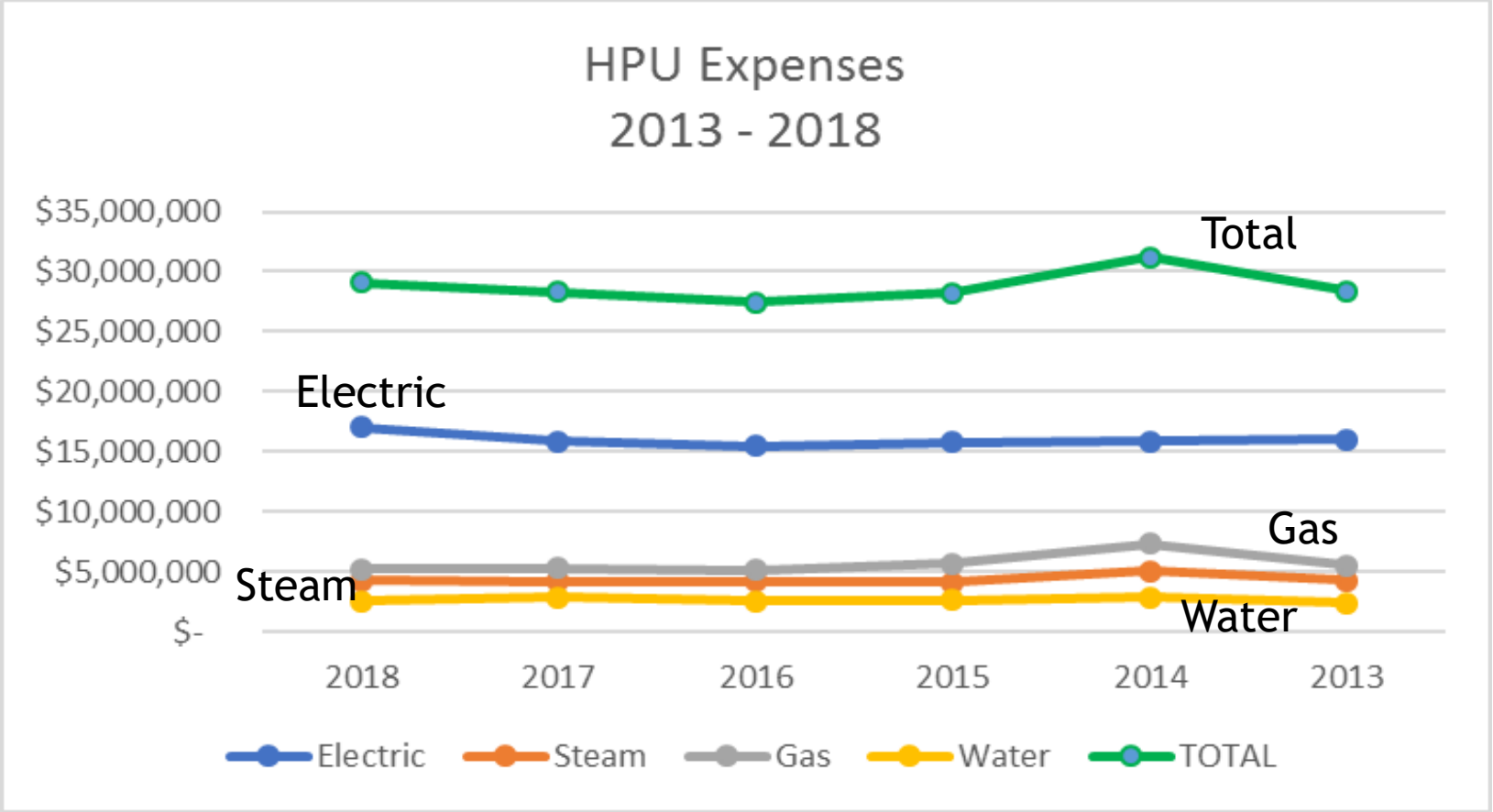


Based on audited financial statements

Statement of Revenues, Expenses and Changes in Net Position

(Income Statement)

- ▶ Operating Expenses increased \$809 thousand to a total \$29 million
 - ▶ Electric was greatest contributor to total operating expenses at 59% or \$17 million and increased 7% from 2017 expenses
 - ▶ Gas was next contributing 18% to total operating expenses or \$5.2 million and decreased 1% in expenses from 2017
 - ▶ Steam contributed 15% to total operating expenses or \$4.3 million and decreased 2% from 2017
 - ▶ Water contributed \$2.6 million or 9% of total operating expenses and decreased 13% from 2017



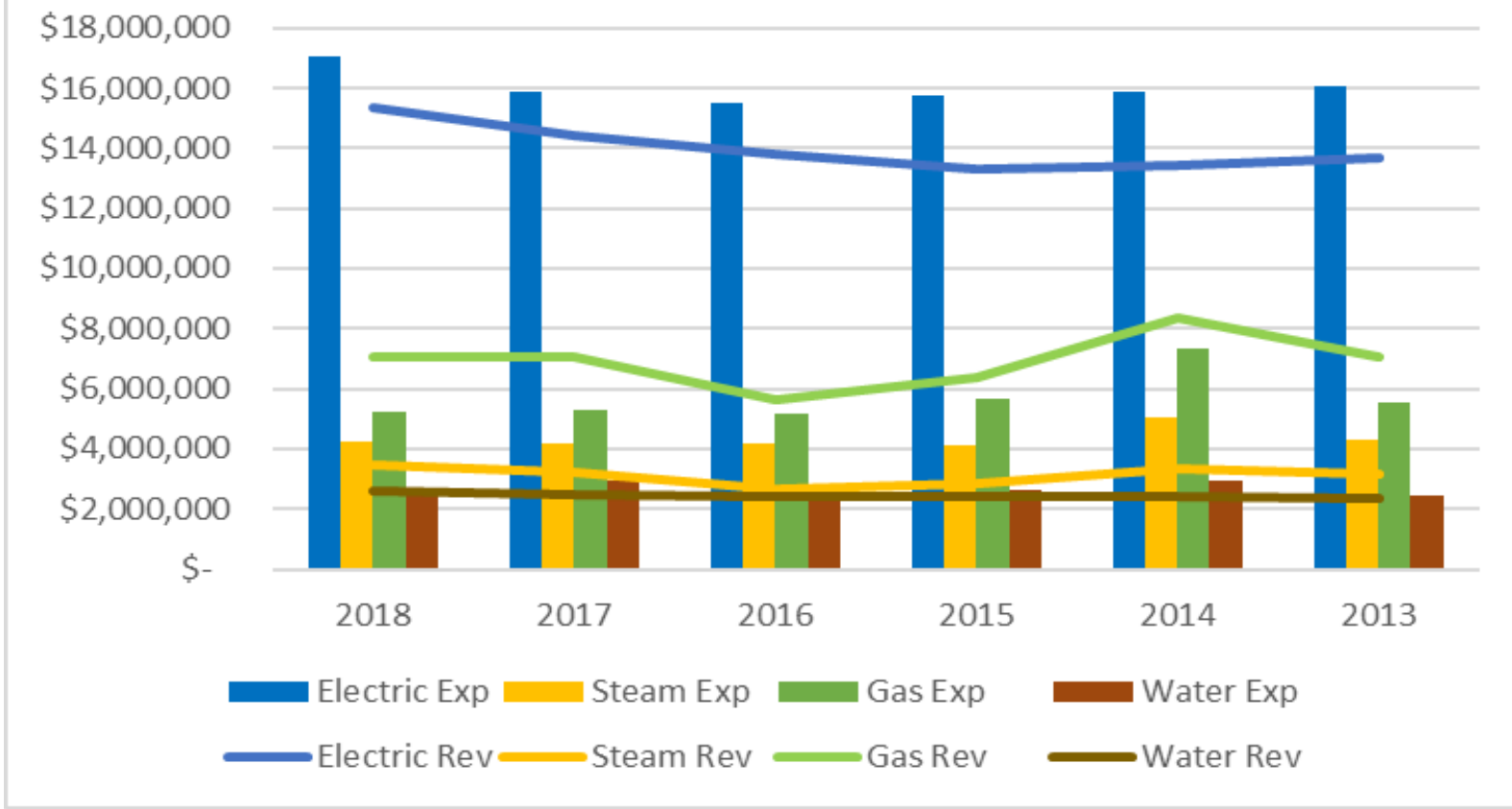
Statement of Revenues, Expenses and Changes in Net Position

(Income Statement)

- ▶ Operating Expenses increased \$809 thousand to a total \$29 million

	<u>Electric</u>	<u>Steam</u>	<u>Gas</u>	<u>Water</u>	<u>Total</u>
Operating Revenues					
Sales and services	\$ 15,341,755	\$ 3,466,792	\$ 7,041,356	\$ 2,612,308	\$ 28,462,211
Operating Expenses					
Operation costs	10,072,792	1,586,303	3,514,040	839,656	16,012,791
Maintenance expense	292,316	100,729	20,214	77,320	490,579
Distribution expense	1,501,797	793,505	683,769	1,179,866	4,158,937
General overhead	5,166,120	1,782,216	1,024,539	455,919	8,428,794
Total Operating Expenses	<u>17,033,025</u>	<u>4,262,753</u>	<u>5,242,562</u>	<u>2,552,761</u>	<u>29,091,101</u>
Operating Income (Loss)	<u>\$ (1,691,270)</u>	<u>\$ (795,961)</u>	<u>\$ 1,798,794</u>	<u>\$ 59,547</u>	<u>\$ (628,890)</u>

HPU Revenue vs Expenses 2013 - 2018



Statement of Revenues, Expenses and Changes in Net Position

(Income Statement)

- ▶ Net operating loss of \$629 thousand
- ▶ Gas had an operating income of \$1.8 million and a \$1.8 million operating income in 2017
- ▶ Electric had an operating loss of \$1.7 million and a \$1.5 million operating loss in 2017
- ▶ Steam had an operating loss of \$796 thousand and \$928 thousand operating loss in 2017
- ▶ Water had an operating income of \$59 thousand and \$459 thousand operating loss in 2017
- ▶ Operating and distribution costs decreased in 2018 from 2017 and maintenance and general overhead increased in 2018 from 2017

Statement of Revenues, Expenses and Changes in Net Position

(Income Statement)

- ▶ Net position - prior period adjustment = Note 15 (\$2.7) million

Net Position - Beginning of Year - As Previously Stated	\$ 31,498,156
Prior Period Adjustment (See Note 15)	(2,708,883)
Net Position - Beginning of Year - As Restated	<u>28,789,273</u>
Increase in Net Position	<u>69,650,486</u>
Net Position - End of Year	<u><u>\$ 98,439,759</u></u>

- ▶ Increase in net position = \$69.6 million
- ▶ EOY Net Position = \$98.4 million

Operating Loss		(628,890)
Nonoperating Revenues (Expenses)		
Interest income		87,959
Late payment penalties		210,566
Other income		148,797
Joint venture member distributions		11,406,667
Equity interest in joint venture increase in net assets		58,111,022
Interest expense		(130,055)
Total Nonoperating Revenues (Expenses)		<u>69,834,956</u>
Income Before Capital Grant		<u>69,206,066</u>
Capital Grants		28,444
Capital Asset Transfer from City of Hibbing	(\$311,623)	415,976
Increase in Net Position		<u>\$ 69,650,486</u>
Net Position - Beginning of Year - As Previously Stated		\$ 31,498,156
Prior Period Adjustment (See Note 15)		(2,708,883)
Net Position - Beginning of Year - As Restated		<u>28,789,273</u>
Increase in Net Position		69,650,486
Net Position - End of Year		<u>\$ 98,439,759</u>

Statement of Cash Flows

- ▶ Cash increased to \$3.5 million at end of 2018

NET INCREASE IN CASH

3,509,248

Cash - Beginning of Year

3,447,323

Cash - End of Year

\$ 6,956,571

- ▶ Cash flow provided from operating activities - \$2.8 million
- ▶ Cash flow provided from non-capital financing - \$359 thousand
- ▶ Cash flow used for capital and related financing - \$2.1 million
- ▶ Cash flow provided from investing activities - \$2.4 million

Notes to Financial Statements

- ▶ Summary of Significant Accounting Policies - Note 1
- ▶ Deposits and Investments - Note 2
- ▶ Long-term Debt - Note 8
- ▶ Defined Benefit Pension Plan - Statewide - PERA - Note 11
- ▶ Other Post Employment Benefits - Note 12
- ▶ Net Position - Designated for OPEB - Note 13
- ▶ Joint Venture - LEA - Note 14
- ▶ Change in Accounting Principle - Note 15

OPEB Discussion

Note 12 - Commission provides health care and dental insurance for retired Commission employees. Funding status and funding progress - currently has no assets that have been irrevocably deposited in a trust for future health benefits thus the entire amount is unfunded.

- ▶ Designation of Net Position
- ▶ Restrictions of Net Position
- ▶ Irrevocable Trust

Change in Accounting Principles

NOTE 15 CHANGE IN ACCOUNTING PRINCIPLE

For the year ended December 31, 2018, the Commission implemented GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*. This restatement resulted in an adjustment to the beginning net position on the Statement of Revenues, Expenses, and Changes in Net of Position of \$2,708,883, for changes in the recognition of the accumulated OPEB liability as of December 31, 2017.

Auditor's Report on Internal Control

- ▶ Lack of segregation of duties over financial processes

Finding 2018-001 – Lack of segregation of duties

The Commission has a lack of segregation of duties over the authorizing, recording, processing and reporting of the financial data due to the limited number of staff. In addition, one individual has complete control over the maintenance of the general ledger and can propose and post adjustments to the financial statements without additional approval.

Condition: Lack of segregation of duties over financial processes.

Auditor's Report on Compliance

Minnesota Legal Compliance

- ▶ None reported

Minnesota Legal Compliance

The *Minnesota Legal Compliance Audit Guide for Cities*, promulgated by the State Auditor pursuant to Minn. Stat. Section 6.65 contains seven categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, and miscellaneous provisions and tax increment financing. Our audit considered all of the listed categories except for tax increment funding since the Commission has not entered into any such activities.

In connection with our audit, nothing came to our attention that caused us to believe that the Commission failed to comply with the provisions of the *Minnesota Legal Compliance Audit Guide for Political Cities*. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the Commission's noncompliance with the above referenced provisions.

The Commission's responses to the internal control findings identified in our audit are described above. We did not audit the Commission's response, and, accordingly, we express no opinion on them.

Questions for the Auditor?

Questions for Director of Finance?

THANK YOU!

Thank you to all HPU employees without them following laws, policies, and procedures the over all financial statements would not be possible to prepare.

A special thank you to the audit team members - Jane Garrity, Chris Zubich, Jamie Chacich, Paul Plombon, and Penny Lange without their work and attention to details the audit would not have gone so smoothly.

Thank you Commission Members