

CITY OF BATTLE CREEK DIRECT
INVESTMENT FUNDS ADMINISTERED BY
BATTLE CREEK UNLIMITED, INC.

Year Ended
June 30, 2018

Financial
Statements

CITY OF BATTLE CREEK DIRECT INVESTMENT FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.

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INDEPENDENT AUDITORS' REPORT

December 26, 2018

To the Honorable Mayor and City Commissioners
of the City of Battle Creek and Direct Investment Fund Committee
of Battle Creek Unlimited, Inc.
City of Battle Creek, Michigan

Report on the Financial Statements

We have audited the accompanying financial statements of the enterprise funds of the *City of Battle Creek Direct Investment Funds Administered by Battle Creek Unlimited, Inc.* (the "Direct Investment Funds") (which consists of an enterprise fund of the City of Battle Creek, Michigan and an enterprise fund of the Battle Creek Downtown Development Authority, a component unit of the City of Battle Creek, Michigan) as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the Direct Investment Funds' 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.

Independent Auditor's Responsibility

Our responsibility is to express an opinion 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 of 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 Direct Investment Fund'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 opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the enterprise funds of the City of Battle Creek Direct Investment Funds Administered by Battle Creek Unlimited, Inc., as of June 30, 2018, and the respective changes in financial position and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Reporting Entity

As discussed in Note 1, the financial statements present only the City of Battle Creek Direct Investment Funds Administered by Battle Creek Unlimited, Inc. and do not purport to, and do not present fairly, the financial position of either the City of Battle Creek, Michigan or the Battle Creek Downtown Development Authority, and the changes in their financial position and their cash flows for the year ended June 30, 2018, in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

A handwritten signature in black ink that reads "Lehmann Johnson LLC". The signature is written in a cursive, flowing style.

BASIC FINANCIAL STATEMENTS

**CITY OF BATTLE CREEK DIRECT INVESTMENT FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.**

Statement of Net Position

June 30, 2018

	Economic Development Fund	Downtown Development Authority Revolving Loan Fund
Assets		
Current assets:		
Cash and cash equivalents	\$ 348,818	\$ 49,206
Investments	4,256,837	1,076,789
Loans receivable, current portion, net	3,133,352	21,943
Accrued interest receivable on loans	16,058	-
Other receivables	11,503	1,844
Due from Battle Creek Unlimited, Inc.	2,894	56,389
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Total current assets	7,769,462	1,206,171
Noncurrent assets:		
Loans receivable, less current portion, net	1,538,705	240,575
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Total assets	9,308,167	1,446,746
	<hr/>	<hr/>
Liabilities - current		
Due to Battle Creek DDA	-	199,996
	<hr/>	<hr/>
Net position		
Unrestricted	9,308,167	-
Restricted for loan commitments and lending activity	-	1,246,750
	<hr/>	<hr/>
Total net position	\$ 9,308,167	\$ 1,246,750
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The accompanying notes are an integral part of these financial statements.

**CITY OF BATTLE CREEK DIRECT INVESTMENT FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.**

Statement of Revenues, Expenses and Changes in Fund Net Position

For the Year Ended June 30, 2018

	Economic Development Fund	Downtown Development Authority Revolving Loan Fund
Operating revenues		
Income on loans	\$ 13,159	\$ 3,482
Loan loss recovery	-	16,003
	<hr/>	<hr/>
Total operating revenues	13,159	19,485
	<hr/>	<hr/>
Operating expenses		
Administration	97,500	32,500
Legal and consulting	103,703	2,867
Other operating costs	876	256
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Total operating expenses	202,079	35,623
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Operating loss	(188,920)	(16,138)
	<hr/>	<hr/>
Nonoperating revenues		
Investment earnings	34,972	7,876
Other revenue	34,600	-
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Total nonoperating revenues	69,572	7,876
	<hr/>	<hr/>
Change in net position	(119,348)	(8,262)
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Net position, beginning of year	9,427,515	1,255,012
	<hr/>	<hr/>
Net position, end of year	\$ 9,308,167	\$ 1,246,750
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The accompanying notes are an integral part of these financial statements.

**CITY OF BATTLE CREEK DIRECT INVESTMENT FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.**

Statement of Cash Flows

For the Year Ended June 30, 2018

	Economic Development Fund	Downtown Development Authority Revolving Loan Fund
Cash flows provided by (used in) operating activities		
Loans collected from borrowers	\$ 67,500	\$ 20,733
Interest and fees on loans	5,336	5,214
Payment received from Battle Creek Unlimited, Inc.	-	2,895
Loans made to borrowers	(1,688,115)	-
Administrative and other expenses paid	(230,087)	(37,014)
Net cash used in operating activities	(1,845,366)	(8,172)
Cash flows provided by (used in) investing activities		
Purchase of investments	(370,994)	(128,523)
Proceeds from sale of investments	2,465,383	150,799
Investment and other income received	69,572	7,876
Net cash provided by investing activities	2,163,961	30,152
Net change in cash and cash equivalents	318,595	21,980
Cash and cash equivalents, beginning of year	30,223	27,226
Cash and cash equivalents, end of year	\$ 348,818	\$ 49,206
Reconciliation of operating loss to net cash used in operating activities		
Operating loss	\$ (188,920)	\$ (16,138)
Change in assets and liabilities:		
Loans receivable	(1,604,557)	5,183
Accrued interest receivable on loans	(7,823)	1,732
Other receivables	(11,503)	(1,844)
Due from Battle Creek Unlimited, Inc.	(2,894)	2,895
Due to Battle Creek Unlimited, Inc.	(29,669)	-
Net cash used in operating activities	\$ (1,845,366)	\$ (8,172)

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

NOTES TO FINANCIAL STATEMENTS

CITY OF BATTLE CREEK DIRECT INVESTMENT FUNDS ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.

Notes to Financial Statements

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The City of Battle Creek Direct Investment Funds Administered by Battle Creek Unlimited, Inc. (the “Direct Investment Funds”) consist of the Economic Development Fund, an enterprise fund of the City of Battle Creek, Michigan (the “City”), and the Downtown Development Authority Revolving Loan Fund, an enterprise fund of the Battle Creek Downtown Development Authority (the “DDA”), a component unit of the City of Battle Creek, Michigan. The Direct Investment Funds provide financing to businesses to create and retain jobs in the City and DDA district, respectively.

The net position of the Economic Development Fund is the property of the City of Battle Creek; the fund was originally created by an appropriation from the City. The net position of the Downtown Development Authority Revolving Loan Fund is the property of the DDA; the fund was originally created by a grant received by the DDA from the Miller Foundation. Both the City and DDA contract with Battle Creek Unlimited, Inc. to administer these funds.

The accounting policies of the Direct Investment Funds conform with generally accepted accounting principles as applicable to proprietary funds. A summary of significant accounting policies follows.

Reporting Entity

These financial statements present the financial position, changes in financial position and cash flows of an enterprise fund of the City and an enterprise fund of the DDA; both funds are an integral part of the respective reporting entities. The Direct Investment Funds are not a component unit of the City, DDA or any other reporting entity, as defined by the Governmental Accounting Standards Board (GASB).

Basis of Accounting

The Direct Investment Funds are separate accounting entities with a self-balancing set of accounts used to report financial position, changes in financial position and cash flows. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain governmental functions and activities.

The Direct Investment Funds are operated as enterprise funds, which are used to account for those operations that are financed and operated in a manner similar to private business or where the governing body has decided that the determination of revenues earned, costs incurred and/or net income is necessary for management accountability. Enterprise funds are accounted for on the flow of economic resources measurement focus and use the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Proprietary funds distinguish operating revenues and expenses from nonoperating 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. The operating revenues of the City of Battle Creek Direct Investment Funds Administered by Battle Creek Unlimited, Inc. include interest on loans, loan fees and other revenue. Operating expenses of the enterprise funds include administration, a loan loss provision/recovery and other operating costs. All revenue and expenses not meeting this definition are reported as nonoperating revenues and expenses.

**CITY OF BATTLE CREEK DIRECT INVESTMENT FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.**

Notes to Financial Statements

Deposits and Investments

The Direct Investment Funds' cash and cash equivalents consist of demand deposits. Investments are stated at fair value and consist of U.S. treasury notes, Michigan municipal bonds, money market accounts, a certificate of deposit and other U.S. government obligations.

State statutes authorize local governments to deposit in the accounts of federally insured banks, credit unions, and savings and loan associations, and to invest in obligations of the U.S. Treasury, certain commercial paper, repurchase agreements, bankers acceptances, and mutual funds composed of otherwise legal investments.

Loans Receivable

Loans receivable consist of balances outstanding from borrowers and are reported net of amounts estimated to be uncollectible.

Net Position

Restricted net position, if any, represents amounts that are for approved loan applications or minority lending.

2. DEPOSITS AND INVESTMENTS

Deposits

At year-end, the carrying amount and bank balance of the Economic Development Fund's deposits were \$348,818. Also at year-end, the carrying amount and bank balance of the DDA Revolving Loan Fund's deposits were \$49,206. Because it is infeasible to allocate risk to individual component units or pool participants, aggregate cash and investment categorizations are presented in the City's basic financial statements.

Investments

At year end, the fair value of the Direct Investment Funds' investment balances were as follows:

	Economic Development Fund	DDA Revolving Loan Fund
Investments at fair value		
U.S. agencies	\$ 1,681,838	\$ 322,889
Municipal bonds	1,190,000	715,000
Money market accounts	1,142,944	38,900
Certificate of deposit	242,055	-
	<u>4,256,837</u>	<u>1,076,789</u>
Total investments	<u>\$ 4,256,837</u>	<u>\$ 1,076,789</u>

Credit Risk. The Direct Investment Funds' investments in debt securities of U.S. agencies are rated AA+, municipal bonds A- and money market accounts AAA by Standard and Poor's. The certificate of deposit is not rated.

**CITY OF BATTLE CREEK DIRECT INVESTMENT FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.**

Notes to Financial Statements

Custodial Credit Risk. For investments, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Direct Investment Funds will not be able to recover the value of their investments or collateral securities that are in the possession of an outside party. Although uninsured and unregistered, the Direct Investment Funds' investments are not exposed to custodial credit risk since the securities are held by the counterparty's trust department in the Direct Investment Funds' name.

Concentration of Credit Risk. At June 30, 2018, the investment portfolio of the two funds was concentrated as follows:

Investment Type	Issuer	% of Portfolio	
		Economic Development Fund	DDA Revolving Loan Fund
U.S. agencies	Federal National Mortgage Association	15.20%	13.36%
	Federal Home Loan Mortgage Corporation	24.30%	16.63%
Municipal bonds	Michigan Municipal Bond Authority	27.96%	66.40%
Money market accounts	Fifth Third Securities	26.85%	3.61%
Certificate of deposit	Wells Fargo Bank	5.69%	0.00%

Interest Rate Risk. As of June 30, 2018, maturities of the City of Battle Creek's Direct Investment Funds investments in debt securities were as follows:

	Economic Development Fund				
	Less Than 1 Year	1-5 Years	6-10 Years	Over 10 Years	Total
U.S. agencies	\$ -	\$ -	\$ -	\$ 1,681,838	\$ 1,681,838
Municipal bonds	-	285,000	190,000	715,000	1,190,000
Money market accounts	1,142,944	-	-	-	1,142,944
Certificate of deposit	-	242,055	-	-	242,055
	<u>\$ 1,142,944</u>	<u>\$ 527,055</u>	<u>\$ 190,000</u>	<u>\$ 2,396,838</u>	<u>\$ 4,256,837</u>

CITY OF BATTLE CREEK DIRECT INVESTMENT FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.

Notes to Financial Statements

	Downtown Development Authority Revolving Loan Fund				
	Less Than 1 Year	1-5 Years	6-10 Years	Over 10 Years	Total
U.S. agencies	\$ -	\$ -	\$ -	\$ 322,889	\$ 322,889
Municipal bonds	-	-	240,000	475,000	715,000
Money market accounts	38,900	-	-	-	38,900
	<u>\$ 38,900</u>	<u>\$ -</u>	<u>\$ 240,000</u>	<u>\$ 797,889</u>	<u>\$ 1,076,789</u>

The Direct Investment Funds' investment policies are not more restrictive than the investment policies authorized by state statute as listed in Note 1.

Fair Value Measurements. The Direct Investment Funds categorize its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; and Level 3 inputs are significant unobservable inputs. These levels are determined by the Direct Investment Funds' investment manager, and are determined at the fund level based on a review of the investment's class, structure, and what kind of securities are held in funds. The investment manager will request the information from the fund manager, if necessary.

The Direct Investment Funds' recurring fair value measurements as of June 30, 2018 were related to its investments in government agency securities, municipal bonds, money market accounts and a certificate of deposit. The money market funds are valued using quoted prices in active markets (Level 1 inputs.) Government agency securities and municipal bonds are valued using significant other observable inputs of the underlying securities and bonds (Level 2 inputs).

3. LOANS OUTSTANDING

Loans receivable outstanding as of June 30, 2018, are summarized as follows:

	Economic Development Fund	DDA Revolving Loan Fund
Total loans outstanding	\$ 4,672,057	\$ 342,496
Allowance for loan losses	-	(79,978)
Net loans outstanding	4,672,057	262,518
Less amount's expected to be collected within one year	<u>3,133,352</u>	<u>21,943</u>
Amount expected to be collected beyond one year	<u>\$ 1,538,705</u>	<u>\$ 240,575</u>

**CITY OF BATTLE CREEK DIRECT INVESTMENT FUNDS
ADMINISTERED BY BATTLE CREEK UNLIMITED, INC.**

Notes to Financial Statements

The Economic Development Fund entered into an agreement during the year that provided up to \$3,500,000 in the form of a construction and related term loan. Commencing on November 1, 2018, payments are due in monthly installments of \$24,170 including interest at 3% per annum. All outstanding principal and accrued interest is due on September 30, 2020. As of June 30, 2018 outstanding draws on the construction loan were \$1,688,115. The remaining commitment was \$1,811,885 at June 30, 2018.

The Economic Development Fund has a loan receivable outstanding of \$3,000,000, unrelated to the construction and term loan described above, to one borrower which represents 61% of the total loans outstanding at June 30, 2018. This loan also represents 32% of the unrestricted net position of the Economic Development Fund at June 30, 2018.

The Economic Development Fund has an additional \$500,000 loan commitment at June 30, 2018. Commitment is unrelated to the construction, term loan and loan receivables noted above.



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*

December 26, 2018

To the Honorable Mayor and City Commissioners
of the City of Battle Creek and Direct Investment Fund Committee
of Battle Creek Unlimited, Inc.
City of Battle Creek, Michigan

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 enterprise funds of the *City of Battle Creek Direct Investment Funds Administered by Battle Creek Unlimited, Inc.* (the "Direct Investment Funds") (which consists of an enterprise fund of the City of Battle Creek, Michigan and an enterprise fund of the Battle Creek Downtown Development Authority, a component unit of the City of Battle Creek, Michigan), as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the Direct Investment Funds' basic financial statements, and have issued our report thereon dated December 26, 2018.

Internal Control Over Financial Reporting

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Direct Investment Funds' 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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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 Direct Investment Funds' 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.

Rehmann Loborn LLC