

STATE OF MINNESOTA

Office of the State Auditor



Patricia Anderson
State Auditor

HOUSTON COUNTY
CALEDONIA, MINNESOTA

YEAR ENDED DECEMBER 31, 2005

Description of the Office of the State Auditor

The Office of the State Auditor serves as a watchdog for Minnesota taxpayers by helping to ensure financial integrity, accountability, and cost-effectiveness in local governments throughout the state.

Through financial, compliance, and special audits, the State Auditor oversees and ensures that local government funds are used for the purposes intended by law and that local governments hold themselves to the highest standards of financial accountability.

The State Auditor performs approximately 250 financial and compliance audits per year and has oversight responsibilities for over 4,300 local units of government throughout the state. The office currently maintains five divisions:

Audit Practice - conducts financial and legal compliance audits for local governments;

Government Information - collects and analyzes financial information for cities, towns, counties, and special districts;

Legal/Special Investigations - provides legal analysis and counsel to the Office and responds to outside inquiries about Minnesota local government law; as well as investigates allegations of misfeasance, malfeasance, and nonfeasance in local government;

Pension - monitors investment, financial, and actuarial reporting for over 700 public pension funds; and

Tax Increment Financing, Investment and Finance - promotes compliance and accountability in local governments' use of tax increment financing through financial and compliance audits.

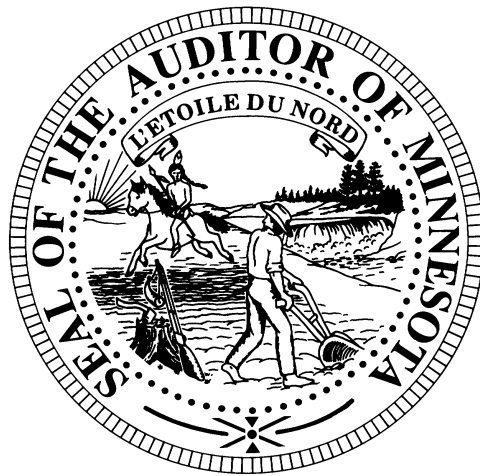
The State Auditor serves on the State Executive Council, State Board of Investment, Land Exchange Board, Public Employee's Retirement Association Board, Minnesota Housing Finance Agency, and the Rural Finance Authority Board.

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**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

Year Ended December 31, 2005



**Audit Practice Division
Office of the State Auditor
State of Minnesota**

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**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

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CALEDONIA, MINNESOTA**

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**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

ORGANIZATION
DECEMBER 31, 2005

		<u>Term Expires</u>
Elected		
Commissioners		
Board Member	Larry Graf	District 1
Vice Chair	Kevin Kelleher*	District 2
Chair	Ann Thompson	District 3
Board Member	David Corcoran	District 4
Board Member	Tom Bjerke	District 5
Attorney	Richard Jackson	January 2007
Auditor	A. Peter Johnson	January 2007
County Recorder	Beverly Bauer	January 2007
County Sheriff	Darryl Peterson	January 2007
District Judge	James Fabian	January 2007
Treasurer	Audrey M. Petersen	January 2007
Appointed		
Assessor	Thomas Dybing	December 2008
County Engineer	Tracey Von Bargaen**	May 2007
Coroner	Regional Medical Center	Indefinite
Court Administrator	Darlene Kuhlers	Indefinite
Social Services Director	Beth Wilms	Indefinite
Public Health Nurse	Linda Grupa	Indefinite
Veterans Service Officer	Robert Gross	October 2007

*Chair 2006

**Tracey Von Bargaen resigned effective May 2007; Marcus Evans is the current County Engineer.

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STATE OF MINNESOTA
OFFICE OF THE STATE AUDITOR

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PATRICIA ANDERSON
STATE AUDITOR

INDEPENDENT AUDITOR'S REPORT

Board of County Commissioners
Houston County

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Houston County, Minnesota, as of and for the year ended December 31, 2005, which collectively comprise the County's basic financial statements as listed in the table of contents. These financial statements are the responsibility of Houston County's management. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of Houston County as of December 31, 2005, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1.E. to the financial statements, the County's reporting entity changed in 2005.

The Management's Discussion and Analysis and required supplementary information budgetary comparison schedules as listed in the table of contents are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the method of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming opinions on the financial statements that collectively comprise Houston County's basic financial statements. The supplementary information and other schedule listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued a report dated November 14, 2006, on our consideration of Houston County'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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

/s/Pat Anderson

PATRICIA ANDERSON
STATE AUDITOR

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

End of Fieldwork: November 14, 2006

MANAGEMENT'S DISCUSSION AND ANALYSIS

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**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

MANAGEMENT'S DISCUSSION AND ANALYSIS
December 31, 2005
(Unaudited)

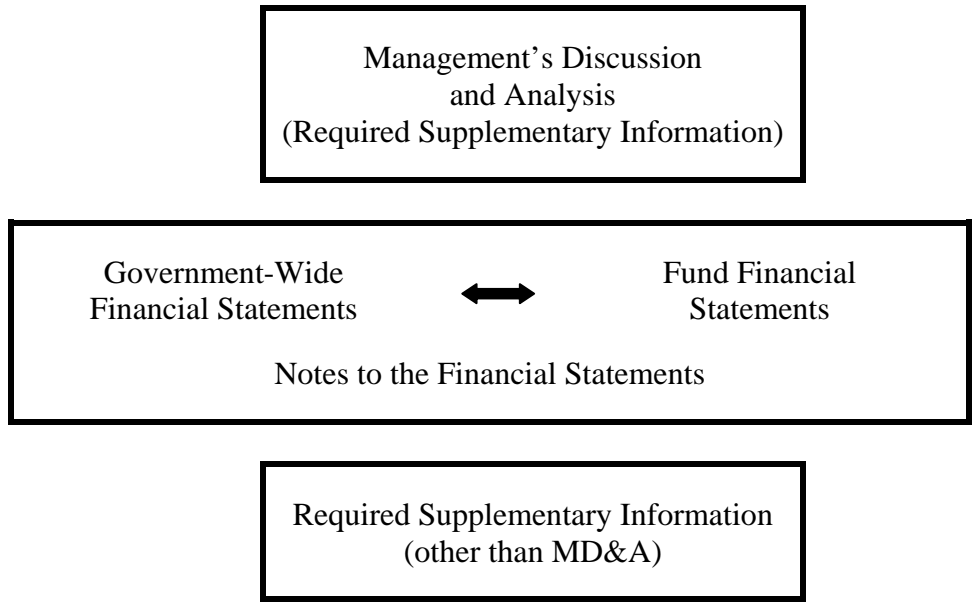
Houston County's discussion and analysis provides an overview of the County's financial activities for the fiscal year ended December 31, 2005. Since this information is designed to focus on current year activities, resulting changes, and currently known facts, it should be read in conjunction with the County's financial statements.

FINANCIAL HIGHLIGHTS

- Governmental activities' total net assets are \$64,683,957, of which \$53,284,373 is invested in capital assets and \$2,380,909 is restricted to specific purposes.
- Houston County's net assets increased by \$3,096,077 for the year ended December 31, 2005.
- The net cost of governmental activities for the current fiscal year was \$4,370,763. The net cost was funded by general revenues, including taxes and grants.
- Governmental funds' fund balances decreased by \$358,827. Most of the decrease was due to the County 249 road improvement project in the Road and Bridge Department.

OVERVIEW OF THE FINANCIAL STATEMENTS

This Management's Discussion and Analysis (MD&A) is intended to serve as an introduction to the basic financial statements. Houston County's basic financial statements consist of three parts: government-wide financial statements, fund financial statements, and notes to the financial statements. The MD&A (this section) and certain budgetary comparison schedules are required to accompany the basic financial statements and, therefore, are included as required supplementary information. The following chart demonstrates how the different pieces are interrelated.



There are two government-wide financial statements. The Statement of Net Assets and the Statement of Activities (Exhibits 1 and 2) provide information about the activities of the County as a whole and present a longer-term view of the County's finances. Fund financial statements start on page 13. For governmental activities, these statements tell how these services were financed in the short term as well as what remains for future spending. Fund financial statements also report the County's operations in more detail than the government-wide statements by providing information about the County's most significant funds. The remaining statements provide financial information about activities for which the County acts solely as an agent for the benefit of those outside of the government.

Government-Wide Financial Statements--The Statement of Net Assets and the Statement of Activities

Our analysis of the County as a whole is shown on Exhibits 1 and 2. The Statement of Net Assets and the Statement of Activities report information about the County as a whole and about its activities in a way that helps the reader determine whether the County's financial condition has improved or declined as a result of the year's activities. These statements include all assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the County's net assets and changes in them. You can think of the County's net assets--the difference between assets and liabilities--as one way to measure the County's financial health or financial position. Over time, increases or decreases in the County's net assets are one indicator of whether its financial health is improving or deteriorating. You will need to consider other nonfinancial factors, however, such as changes in the County's property tax base and the condition of County roads, to assess the overall health of the County.

The Statement of Activities presents information showing how the County's net assets changed during the year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows only in future years. The activities of Houston County are presented as governmental activities because they are principally supported by taxes and intergovernmental revenues. The County's basic services are reported here, including general government, public safety, transportation, sanitation, human services, culture and recreation, conservation of natural resources, and economic development.

Fund Financial Statements

Our analysis of the County's major funds begins on page 13. The fund financial statements provide detailed information about the significant funds--not the County as a whole. Some funds are required to be established by state law. However, the County Board establishes some funds to help it control and manage money for a particular purpose or to show that it is meeting legal responsibilities for using certain taxes, grants, and other money. The County's governmental funds use the following accounting method.

The County's basic services are reported in governmental funds, which focus on how money flows into and out of those funds and the balances left at year-end that are available for spending. These funds are reported using an accounting method called modified accrual accounting. This method measures cash and all other financial assets that can be readily converted to cash. The governmental fund statements provide a detailed short-term view of the County's general government operations and the basic services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the County's programs. We describe the relationship (or differences) between governmental activities (reported in the Statement of Net Assets and the Statement of Activities) and governmental funds in a reconciliation in a statement following each governmental fund financial statement.

Reporting the County's Fiduciary Responsibilities

The County is the trustee, or fiduciary, over assets that can be used only by other governments, nonprofits, or individuals. All of the County's fiduciary activities are reported in a separate Statement of Fiduciary Net Assets. We exclude these activities from the County's other financial statements because the County cannot use these assets to finance its operations.

THE COUNTY AS A WHOLE

The County's net assets increased from \$61,587,880 (restated) to \$64,683,957.

Table 1
Net Assets
(in Millions)

	<u>2005</u>	<u>2004</u>
Current and other assets	\$ 12.8	\$ 12.7
Capital assets	<u>53.4</u>	<u>50.2</u>
Total Assets	<u>\$ 66.2</u>	<u>\$ 62.9</u>
Long-term debt outstanding	\$ 0.8	\$ 0.7
Other liabilities	<u>0.7</u>	<u>0.6</u>
Total Liabilities	<u>\$ 1.5</u>	<u>\$ 1.3</u>
Net Assets		
Invested in capital assets	\$ 53.3	\$ 50.2
Restricted	2.4	2.6
Unrestricted	<u>9.0</u>	<u>8.8</u>
Total Net Assets	<u>\$ 64.7</u>	<u>\$ 61.6</u>

Net assets of the County's governmental activities increased by 5.0 percent (\$61,587,880 compared to \$64,683,957).

Table 2
Changes in Net Assets
(in Millions)

	<u>2005</u>	<u>2004</u>
Revenues		
Program revenues		
Fees, fines, charges, and other	\$ 2.3	\$ 2.1
Operating grants and contributions	7.5	7.1
Capital grants and contributions	0.5	0.5
General revenues		
Property taxes	4.9	4.5
Other taxes	0.1	0.2
Grants and contributions	2.0	1.8
Other general revenues	<u>0.4</u>	<u>0.4</u>
Total Revenues	<u>\$ 17.7</u>	<u>\$ 16.6</u>

	<u>2005</u>	<u>2004</u>
Program expenses		
General government	\$ 2.7	\$ 2.6
Public safety	2.1	2.1
Transportation	3.2	5.0
Human services	4.0	3.4
Health	1.3	1.2
Sanitation	0.7	0.7
Culture and recreation	0.2	0.2
Conservation of natural resources	0.3	0.3
Economic development	0.1	-
	<u>14.6</u>	<u>15.5</u>
Total Program Expenses	\$ 14.6	\$ 15.5
	<u>3.1</u>	<u>1.1</u>
Increase (Decrease) in Net Assets	\$ 3.1	\$ 1.1

Governmental Activities

The cost of all governmental activities this year was \$14,646,242. However, as shown in the Statement of Activities, the amount that the taxpayers ultimately financed for these activities through County property taxes was only \$4,928,004, because some of the cost was paid by those who directly benefited from the programs (\$2,285,265) or by other governments and organizations that subsidized certain programs with grants and contributions (\$8,027,684). The County paid for the remaining “public benefit” portion of governmental activities with \$4,333,293 in general revenues, primarily property taxes and other revenues, such as interest and general entitlements.

Table 3 presents the cost of each of the County’s four largest program functions, as well as each function’s net cost (total cost, less revenues generated by the activities). The net cost shows the financial burden that was placed on the County’s taxpayers by each of these functions.

Table 3
Governmental Activities
(in Millions)

	<u>Total Cost of Services</u>		<u>Net Cost of Services</u>	
	<u>2005</u>	<u>2004</u>	<u>2005</u>	<u>2004</u>
Transportation	\$ 3.2	\$ 5.0	\$ (1.5)	\$ 0.4
Human services	4.0	3.4	1.5	1.1
General government	2.7	2.6	2.2	2.1
Public safety	2.1	2.1	1.7	1.7

FINANCIAL ANALYSIS OF THE COUNTY'S FUNDS

As noted earlier, Houston County uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The focus of the County's funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the County's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a county's net resources available for spending at the end of the year.

At December 31, 2005, Houston County's governmental funds reported combined ending fund balances of \$10,273,714, a decrease of \$358,827 in comparison with 2004. Approximately, 40 percent of this amount (\$4,105,193) constitutes unreserved, undesignated fund balance, which is available for spending at the County's discretion. The remainder of fund balance is reserved or designated to indicate that it is not available for new spending because it has already been committed.

The General Fund is the chief operating fund of Houston County. At December 31, 2005, unreserved, undesignated fund balance was \$2,661,826, while total fund balance was \$5,944,657. As a measure of the General Fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved, undesignated fund balance represents 35 percent of total General Fund expenditures, while total fund balance represents 77 percent of the same amount.

The Road and Bridge Fund's fund balance decreased by \$441,573, for an ending balance of \$2,408,752, of which \$275,057 is unreserved, undesignated. The decrease is due to increased spending in the Road and Bridge Fund. The Social Services Fund decreased by \$127,838 to \$1,920,305, of which \$1,168,310, or 61 percent, is undesignated.

General Fund Budgetary Highlights

Houston County did not revise its General Fund budget during 2005. For the year ended December 31, 2005, expenditures exceeded appropriations by \$604,119, with the largest overages in the general government function.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At the end of 2005, the County had \$53,427,772 invested in a broad range of capital assets, including land, buildings, highways and streets, and equipment. (See Table 4.) This amount represents a net increase (including additions and deductions) of \$3,266,270, or 6.5 percent, over last year.

Table 4
Capital Assets at Year-End
(Net of Depreciation, in Millions)

	2005	2004
Land	\$ 1.9	\$ 1.8
Construction in progress	4.4	1.3
Buildings and improvements	1.5	1.5
Machinery, vehicles, furniture, and equipment	2.3	2.2
Infrastructure	43.3	43.4
Totals	\$ 53.4	\$ 50.2

This year's major addition was due to a \$3,039,379 increase in road construction in progress projects.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The County's elected and appointed officials considered many factors when setting the fiscal year 2006 budget, tax rates, and fees that will be charged.

- The State of Minnesota has projected a significant budget deficit, and it is anticipated that there will be significant reductions in state aids to local governments.
- County General Fund expenditures for 2006 are budgeted to decrease 2.1 percent from 2005 due to reductions in grant funded programs available.
- Property tax levies have increased 8.75 percent for 2006.

CONTACTING HOUSTON COUNTY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the County's finances and to show the County's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the County Auditor, A. Peter Johnson, Houston County Courthouse, 304 South Marshall Street, Caledonia, Minnesota 55921.

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BASIC FINANCIAL STATEMENTS

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GOVERNMENT-WIDE FINANCIAL STATEMENTS

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**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT 1

**STATEMENT OF NET ASSETS
GOVERNMENTAL ACTIVITIES
DECEMBER 31, 2005**

Assets

Cash and pooled investments	\$	6,918,562
Petty cash and change funds		17,035
Investments		2,405,777
Taxes receivable		
Prior - net		88,363
Accounts receivable - net		164,914
Accrued interest receivable		68,019
Loans receivable		110,098
Due from other governments		2,755,334
Prepaid items		8,539
Inventories		233,554
Capital assets		
Nondepreciable		6,293,691
Depreciable - net of accumulated depreciation		47,134,081
		47,134,081
Total Assets	\$	66,197,967

Liabilities

Accounts payable	\$	328,218
Salaries payable		107,421
Contracts payable		175,541
Due to other governments		118,415
Customer deposits		2,647
Long-term liabilities		
Due within one year		175,910
Due in more than one year		605,858
		605,858
Total Liabilities	\$	1,514,010

Net Assets

Invested in capital assets	\$	53,284,373
Restricted for		
Highways and streets		1,892,081
General government		99,774
Public safety		142,364
Economic development		246,690
Unrestricted		9,018,675
		9,018,675
Total Net Assets	\$	64,683,957

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT 2

**STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2005**

	Expenses	Fees, Charges, Fines, and Other	Program Revenues		Net (Expense) Revenues and Changes in Net Assets
			Operating Grants and Contributions	Capital Grants and Contributions	
<u>Functions/Programs</u>					
Primary government					
Governmental activities					
General government	\$ 2,770,853	\$ 457,929	\$ 44,497	\$ -	\$ (2,268,427)
Public safety	2,149,257	110,949	292,455	-	(1,745,853)
Transportation	3,253,934	163,104	4,117,595	512,220	1,538,985
Sanitation	711,411	482,967	-	-	(228,444)
Human services	3,974,048	11,185	2,424,311	-	(1,538,552)
Health	1,261,797	915,002	386,372	-	39,577
Culture and recreation	207,857	19,745	-	-	(188,112)
Conservation of natural resources	297,024	1,030	250,234	-	(45,760)
Economic development	57,531	123,354	-	-	65,823
Total	<u>\$ 14,683,712</u>	<u>\$ 2,285,265</u>	<u>\$ 7,515,464</u>	<u>\$ 512,220</u>	<u>\$ (4,370,763)</u>
General Revenues					
Property taxes					\$ 4,928,004
Mortgage registry and deed tax					15,832
Payments in lieu of tax					136,080
Grants and contributions not restricted to specific programs					1,959,890
Unrestricted investment earnings					297,318
Miscellaneous					129,716
Total general revenues					<u>\$ 7,466,840</u>
Change in net assets					<u>\$ 3,096,077</u>
Net Assets - Beginning					<u>61,587,880</u>
Net Assets - Ending					<u>\$ 64,683,957</u>

FUND FINANCIAL STATEMENTS

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GOVERNMENTAL FUNDS

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**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT 3

**BALANCE SHEET
GOVERNMENTAL FUNDS
DECEMBER 31, 2005**

	General	Road and Bridge	Social Services	Total Governmental Funds
<u>Assets</u>				
Cash and pooled investments	\$ 5,424,252	\$ 592,149	\$ 902,161	\$ 6,918,562
Petty cash and change funds	16,935	100	-	17,035
Investments	247,091	1,166,686	992,000	2,405,777
Taxes receivable				
Prior	54,452	16,698	17,213	88,363
Accounts receivable	131,482	663	32,769	164,914
Accrued interest receivable	46,673	10,855	10,491	68,019
Loans receivable	110,098	-	-	110,098
Due from other funds	10,747	-	-	10,747
Due from other governments	164,998	2,305,940	284,396	2,755,334
Inventories	-	233,554	-	233,554
Prepaid items	8,539	-	-	8,539
Total Assets	\$ 6,215,267	\$ 4,326,645	\$ 2,239,030	\$ 12,780,942

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

**EXHIBIT 3
(Continued)**

**BALANCE SHEET
GOVERNMENTAL FUNDS
DECEMBER 31, 2005**

	<u>General</u>	<u>Road and Bridge</u>	<u>Social Services</u>	<u>Total Governmental Funds</u>
<u>Liabilities and Fund Balances</u>				
Liabilities				
Accounts payable	\$ 81,346	\$ 47,081	\$ 199,791	\$ 328,218
Salaries payable	67,561	17,893	21,967	107,421
Contracts payable	-	175,541	-	175,541
Due to other funds	-	-	10,747	10,747
Due to other governments	33,935	8,851	75,629	118,415
Deferred revenue - unavailable	85,121	1,668,527	10,591	1,764,239
Customer deposits	2,647	-	-	2,647
Total Liabilities	\$ 270,610	\$ 1,917,893	\$ 318,725	\$ 2,507,228
Fund Balances				
Reserved for				
Inventories	\$ -	\$ 233,554	\$ -	\$ 233,554
Loans receivable	110,098	-	-	110,098
Prepaid items	8,540	-	-	8,540
Law library	12,448	-	-	12,448
Recorder's unallocated funds	21,857	-	-	21,857
Recorder's equipment purchases	65,469	-	-	65,469
E-911	142,364	-	-	142,364
Future projects	69,109	-	-	69,109
Road projects	-	416,859	-	416,859
Economic development revolving loan	67,483	-	-	67,483
Unreserved				
Designated for future expenditures	69,106	600,000	-	669,106
Designated for investments' unrealized gains	83,658	-	-	83,658
Designated for cash flows	2,255,000	754,000	662,547	3,671,547
Designated for compensated absences	377,699	129,282	89,448	596,429
Undesignated	2,661,826	275,057	1,168,310	4,105,193
Total Fund Balances	\$ 5,944,657	\$ 2,408,752	\$ 1,920,305	\$ 10,273,714
Total Liabilities and Fund Balances	\$ 6,215,267	\$ 4,326,645	\$ 2,239,030	\$ 12,780,942

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT 4

**RECONCILIATION OF GOVERNMENTAL FUNDS BALANCE SHEET TO
THE GOVERNMENT-WIDE STATEMENT OF NET ASSETS--GOVERNMENTAL ACTIVITIES
DECEMBER 31, 2005**

Fund balances - total governmental funds (Exhibit 3)	\$	10,273,714
Amounts reported for governmental activities in the statement of net assets are different because:		
Capital assets, net of accumulated depreciation, used in governmental activities are not financial resources and, therefore, are not reported in the governmental funds.		53,427,772
Other long-term assets are not available to pay for current period expenditures and, therefore, are deferred in the governmental funds.		1,764,239
Long-term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported in the governmental funds.		
Loans payable	\$ (42,000)	
Capital leases payable	(143,339)	
Compensated absences	(596,429)	(781,768)
Net assets of governmental activities (Exhibit 1)		<u>\$ 64,683,957</u>

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT 5

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2005**

	<u>General</u>	<u>Road and Bridge</u>	<u>Social Services</u>	<u>Total Governmental Funds</u>
Revenues				
Taxes	\$ 3,059,175	\$ 941,066	\$ 951,769	\$ 4,952,010
Licenses and permits	59,636	1,270	-	60,906
Intergovernmental	2,370,273	4,634,970	2,849,663	9,854,906
Charges for services	1,761,794	152,464	11,185	1,925,443
Fines and forfeits	24,996	-	-	24,996
Gifts and contributions	1,859	-	-	1,859
Interest on investments	213,459	42,620	41,239	297,318
Miscellaneous	392,166	11,470	-	403,636
Total Revenues	\$ 7,883,358	\$ 5,783,860	\$ 3,853,856	\$ 17,521,074
Expenditures				
Current				
General government	\$ 2,809,151	\$ -	\$ -	\$ 2,809,151
Public safety	2,209,864	-	-	2,209,864
Transportation	95,211	6,220,360	-	6,315,571
Sanitation	735,153	-	-	735,153
Human services	-	-	3,981,694	3,981,694
Health	1,271,301	-	-	1,271,301
Culture and recreation	206,766	-	-	206,766
Conservation of natural resources	297,660	-	-	297,660
Economic development	52,168	-	-	52,168
Total Expenditures	\$ 7,677,274	\$ 6,220,360	\$ 3,981,694	\$ 17,879,328
Excess of Revenues Over (Under) Expenditures	\$ 206,084	\$ (436,500)	\$ (127,838)	\$ (358,254)
Other Financing Sources (Uses)				
Capital lease/installment purchase	\$ -	\$ 143,339	\$ -	\$ 143,339
Proceeds from sale of capital assets	4,500	3,500	-	8,000
Total Other Financing Sources (Uses)	\$ 4,500	\$ 146,839	\$ -	\$ 151,339
Net Change in Fund Balances	\$ 210,584	\$ (289,661)	\$ (127,838)	\$ (206,915)
Fund Balances - January 1	5,734,073	2,850,325	2,048,143	10,632,541
Increase (decrease) in reserved for inventories	-	(151,912)	-	(151,912)
Fund Balances - December 31	\$ 5,944,657	\$ 2,408,752	\$ 1,920,305	\$ 10,273,714

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT 6

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND
CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE
GOVERNMENT-WIDE STATEMENT OF ACTIVITIES--GOVERNMENTAL ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2005**

Net change in fund balances - total governmental funds (Exhibit 5) \$ (206,915)

Amounts reported for governmental activities in the statement of activities are different because:

In the funds, under the modified accrual basis, receivables not available for expenditures are deferred. In the statement of activities, those revenues are recognized when earned. The adjustment to revenues between the fund statements and the statement of activities is the increase (decrease) in revenues deferred as unavailable.

Deferred revenues - December 31	\$ 1,764,239	
Deferred revenues - January 1	(1,505,524)	258,715

Governmental funds report capital outlay as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. Also, in the statement of activities, only the gain or loss on disposal of capital assets is reported; whereas, in the governmental funds, the proceeds from the disposal increase financial resources. Therefore, the change in net assets differs from the change in fund balance by the net book value of the assets disposed of.

Expenditures for general capital assets	\$ 4,980,735	
Net book value of disposed assets	(45,470)	
Current year depreciation	(1,668,995)	3,266,270

The issuance of long-term debt provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets. Also, governmental funds report the effect of issuance costs, premiums, discounts, and similar items when the debt is first issued; whereas, these amounts are deferred and amortized in the statement of activities.

Capital leases entered into		(143,339)
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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 governmental funds.

Change in inventories	\$ (151,912)	
Change in compensated absences	73,258	(78,654)

Change in net assets of governmental activities (Exhibit 2) \$ 3,096,077

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FIDUCIARY FUNDS

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HOUSTON COUNTY
CALEDONIA, MINNESOTA

EXHIBIT 7

STATEMENT OF FIDUCIARY NET ASSETS
FIDUCIARY FUNDS
DECEMBER 31, 2005

	<u>Agency</u>
<u>Assets</u>	
Cash and pooled investments	\$ 1,171,554
Due from other governments	<u>3,721</u>
Total Assets	<u>\$ 1,175,275</u>
<u>Liabilities</u>	
Accounts payable	\$ 121,735
Due to other governments	<u>1,053,540</u>
Total Liabilities	<u>\$ 1,175,275</u>

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**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

NOTES TO THE FINANCIAL STATEMENTS
AS OF AND FOR THE YEAR ENDED DECEMBER 31, 2005

1. Summary of Significant Accounting Policies

The County's financial statements are prepared in accordance with generally accepted accounting principles (GAAP) as of and for the year ended December 31, 2005. The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (statements and interpretations). Governments are also required to follow the pronouncements of the Financial Accounting Standards Board issued through November 30, 1989, (when applicable) that do not conflict with or contradict GASB pronouncements. The more significant accounting policies established in GAAP and used by the County are discussed below.

A. Financial Reporting Entity

Houston County was established February 23, 1854, and is an organized county having the powers, duties, and privileges granted counties by Minn. Stat. ch. 373. As required by accounting principles generally accepted in the United States of America, these financial statements present Houston County (primary government) and its component units for which the County is financially accountable. The County is governed by a five-member Board of Commissioners elected from districts within the County. The Board is organized with a chair and vice chair elected at the annual meeting in January of each year.

Blended Component Unit

Blended component units are legally separate organizations so intertwined with the County that they are, in substance, the same as the County and, therefore, are reported as if they were part of the County. Houston County has one blended component unit, which is reported as part of the General Fund.

Component Unit	Component Unit Included in Reporting Entity Because	Separate Financial Statements
Houston County Economic Development Authority (EDA) provides for development within the County.	County Commissioners are the members of the EDA Board.	Separate financial statements are not prepared.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

1. Summary of Significant Accounting Policies

A. Financial Reporting Entity (Continued)

Joint Ventures

The County participates in a joint venture described in Note 4.D. The County also participates in jointly-governed organizations described in Note 4.C.

B. Basic Financial Statements

1. Government-Wide Statements

The government-wide financial statements (the statement of net assets and the statement of activities) display information about the primary government and its component units. These statements include the financial activities of the overall County government, except for fiduciary activities. Eliminations have been made to minimize the double counting of internal activities. Governmental activities are normally supported by taxes and intergovernmental revenues.

The government-wide statement of net assets is presented on a consolidated basis by column and is reported on a full accrual, economic resource basis, which recognizes all long-term assets and receivables as well as long-term debt and obligations. The County's net assets are reported in three parts: (1) invested in capital assets, (2) restricted net assets, and (3) unrestricted net assets. The County first utilizes restricted resources to finance qualifying activities.

The statement of activities demonstrates the degree to which the direct expenses of each function of the County's governmental activities are offset by program revenues. Direct expenses are those clearly identifiable with a specific function or activity. Program revenues include: (1) fees, fines, and charges paid by the recipients of goods, services, or privileges provided by a given function or activity; and (2) grants and contributions restricted to meeting the operational or capital requirements of a particular function or activity. Revenues not classified as program revenues, including all taxes, are presented as general revenues.

2. Fund Financial Statements

The fund financial statements provide information about the County's funds, including its fiduciary funds and blended component unit. Separate statements for each fund category--governmental and fiduciary--are presented.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

1. Summary of Significant Accounting Policies

B. Basic Financial Statements

2. Fund Financial Statements (Continued)

The County reports the following major governmental funds:

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

The Road and Bridge Special Revenue Fund is used to account for revenues and expenditures of the County Highway Department, which is responsible for the construction and maintenance of roads, bridges, and other projects affecting County roadways.

The Social Services Special Revenue Fund is used to account for economic assistance and community social services programs.

The County reports the following fund type:

Agency funds are custodial in nature and do not present results of operations or have a measurement focus. These funds account for assets that the County holds for others in an agent capacity.

C. Measurement Focus and Basis of Accounting

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Houston County considers all revenues as available if collected within 60 days after the end of the current period. Property and other taxes, licenses, and interest are all considered

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

1. Summary of Significant Accounting Policies

C. Measurement Focus and Basis of Accounting (Continued)

susceptible to accrual. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on long-term debt, compensated absences, and claims and judgments, which are recognized as expenditures to the extent that they have matured. Proceeds of long-term debt and acquisitions under capital leases are reported as other financing sources.

When both restricted and unrestricted resources are available for use, it is the County's policy to use restricted resources first and then unrestricted resources as needed.

D. Assets, Liabilities, and Net Assets or Equity

1. Deposits and Investments

The cash balances of substantially all funds are pooled and invested by the County Treasurer for the purpose of increasing earnings through investment activities. Pooled and fund investments are reported at their fair value at December 31, 2005, based on market prices. Pursuant to Minn. Stat. § 385.07, investment earnings on cash and pooled investments are credited to the General Fund. Other funds received investment earnings based on other state statutes, grant agreements, contracts, and bond covenants. Pooled investment earnings for 2005 were \$158,789.

2. Receivables and Payables

Activities between funds representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (the current portion of interfund loans) or "advances to/from other funds" (the noncurrent portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds."

Advances between funds, as reported in the fund financial statements, are offset by a fund balance reserve account to indicate they are not available for appropriation and are not expendable available financial resources.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Assets or Equity

2. Receivables and Payables (Continued)

All receivables are shown net of an allowance for uncollectibles.

Property taxes are levied as of January 1 on property values assessed as of the same date. The tax levy notice is mailed in March with the first half payment due May 15 and the second half payment due October 15. Unpaid taxes at December 31 become liens on the respective property and are classified in the financial statements as delinquent taxes receivable.

3. Inventories and Prepaid Items

All inventories are valued at cost using the first in/first out (FIFO) method. Inventories in governmental funds are recorded as expenditures when purchased rather than when consumed. Inventories at the government-wide level are recorded as expenses when consumed.

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

4. Capital Assets

Capital assets, which include property, plant, equipment, and infrastructure assets (for example, roads, bridges, and similar items), are reported in the government-wide financial statements. Capital assets are defined by the County as assets with an initial, individual cost of more than \$10,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Assets or Equity

4. Capital Assets (Continued)

Property, plant, and equipment of the County is depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Buildings	50
Building improvements	50
Public domain infrastructure	50 - 75
Furniture, equipment, and vehicles	3 - 20

5. Compensated Absences

The liability for compensated absences reported in the financial statements consists of unpaid, accumulated annual vacation and sick leave balances. The liability has been calculated using the vesting method, in which leave amounts for both employees who currently are eligible to receive termination payments and other employees who are expected to become eligible in the future to receive such payments upon termination are included. Compensated absences are accrued when incurred in the government-wide financial statements. A liability for these amounts is reported in the governmental funds only if they have matured, for example, as a result of employee resignations and retirements.

6. Deferred Revenue

All County funds and the government-wide financial statements defer revenue for resources that have been received, but not yet earned. Governmental funds also report deferred revenue in connection with receivables for revenues not considered to be available to liquidate liabilities of the current period.

7. Long-Term Obligations

In the government-wide statement of net assets, long-term debt and other long-term obligations are reported as liabilities. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Assets or Equity

7. Long-Term Obligations (Continued)

the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of the debt issued is reported as an other financing source. Premiums received on debt issuances are reported as other financing sources, while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

8. Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts not available for appropriation or legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans subject to change.

9. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

E. Change in Reporting Entity

Prior to 2005, the Crooked Creek Watershed District was reported as a discrete component unit. After further review, it was determined that a financial benefit or burden did not exist. Accordingly, the Crooked Creek Watershed District is no longer reported in the County's financial statements as a component unit.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

2. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

Reconciliation of the County's total cash and investments to the basic financial statements follows:

Government-wide statement of net assets	
Governmental activities	
Cash and pooled investments	\$ 6,918,562
Petty cash and change funds	17,035
Investments	2,405,777
Statement of fiduciary net assets	
Cash and pooled investments	<u>1,171,554</u>
 Total Cash and Investments	 <u>\$ 10,512,928</u>

a. Deposits

Minn. Stat. §§ 118A.02 and 118A.04 authorize the County to designate a depository for public funds and to invest in certificates of deposit. Minn. Stat. § 118A.03 requires that all county deposits be protected by insurance, surety bond, or collateral. The market value of collateral pledged shall be at least ten percent more than the amount on deposit plus accrued interest at the close of the financial institution's banking day, not covered by insurance or bonds.

Authorized collateral includes treasury bills, notes and bonds; issues of U.S. government agencies; general obligations rated "A" or better, revenue obligations rated "AA" or better; irrevocable standard letters of credit issued by the Federal Home Loan Bank; and certificates of deposit. Minnesota statutes require that securities pledged as collateral be held in safekeeping in a restricted account at the Federal Reserve Bank or in an account at a trust department of a commercial bank or other financial institution not owned or controlled by the financial institution furnishing the collateral.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

2. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

a. Deposits (Continued)

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a financial institution failure, the County's deposits may not be returned to it. The County does not have a deposit policy for custodial credit risk. As of December 31, 2005, the County does not have any deposits exposed to custodial credit risk.

b. Investments

Minn. Stat. §§ 118A.04 and 118A.05 generally authorize the following types of investments as available to the County:

- (1) securities which are direct obligations or are guaranteed or insured issues of the United States, its agencies, its instrumentalities, or organizations created by an act of Congress, except mortgage-backed securities defined as "high risk" by Minn. Stat. § 118A.04, subd. 6;
- (2) mutual funds through shares of registered investment companies provided the mutual fund receives certain ratings depending on its investments;
- (3) general obligations of the State of Minnesota and its municipalities, and in certain state agency and local obligations of Minnesota and other states provided such obligations have certain specified bond ratings by a national bond rating service;
- (4) bankers' acceptances of United States banks;
- (5) commercial paper issued by United States corporations or their Canadian subsidiaries that is rated in the highest quality category by two nationally recognized rating agencies and matures in 270 days or less; and

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

2. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

b. Investments (Continued)

- (6) with certain restrictions, in repurchase agreements, securities lending agreements, joint powers investment trusts, and guaranteed investment contracts.

Interest Rate Risk

Interest rate risk is the risk that changes in the market interest rates will adversely affect the fair value of an investment. The County minimizes its exposure to interest rate risk by investing in both short-term and long-term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations.

The County does not have a policy regarding investment maturity limits.

Investment Type	Fair Value	Less Than 1 Year	2 - 3 Years	3 - 13 Years
Federal Home Loan Bank	\$ 4,146,747	\$ 981,093	\$ 1,105,254	\$ 2,060,400
Federal Home Loan Mortgage Corporation	432,909	149,047	98,178	185,684
Federal National Mortgage Corporation	524,969	-	-	524,969
Government National Mortgage Association Pool	14,253	-	-	14,253
Small Business Administration loan	70,098	-	-	70,098
Negotiable certificates of deposit	3,477,158	675,000	974,005	1,828,153
Total Investments	\$ 8,666,134	\$ 1,805,140	\$ 2,177,437	\$ 4,683,557

Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. It is the County's policy, as set by the Houston County Investment Policy, to invest only in securities that meet the ratings requirements of state statute.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

2. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

b. Investments

Credit Risk (Continued)

The County is required to disclose the credit quality ratings of investments in debt securities, external investment pools, money market funds, bond mutual funds, and other pooled investments of fixed income securities. Houston County invests in the following investment pools/mutual funds:

	<u>Credit Rating</u>	<u>Rating Agency</u>	<u>Fair Value</u>
Federal Home Loan Bank	AAA	Standard & Poor's	\$ 4,146,747
Federal Home Loan Mortgage Corporation	A-1+	Standard & Poor's	432,909
Federal National Mortgage Corporation	AAA	Standard & Poor's	524,969
Small Business Administration Loan	AAA	Standard and Poor's	70,098

Custodial Credit Risk

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The County does not have a policy on custodial credit risk. At December 31, 2005, none of Houston County's investments were subject to custodial credit risk.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

2. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

b. Investments (Continued)

Concentration of Credit Risk

The concentration of credit risk is the risk of loss that may be caused by the County's investment in a single issuer. The County's investment policy does not currently address this risk. Investments in any one issuer that represent five percent or more of the County's investments are as follows:

Issuer	Reported Amount
Federal Home Loan Bank	\$ 4,146,747
Federal Home Loan Mortgage Corporation	432,909
Fannie Mae	524,969

2. Receivables

Receivables as of December 31, 2005, for the County's governmental activities, including the applicable allowances for uncollectible accounts, are as follows:

Accounts receivable, gross	\$ 350,608
Less: allowance for social services uncollectible	(185,694)
Net Accounts Receivable	\$ 164,914

The loans receivable balance of \$110,098 includes \$102,024, which is not scheduled for collection in the subsequent year.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

2. Detailed Notes on All Funds

A. Assets (Continued)

3. Capital Assets

Capital asset activity for the year ended December 31, 2005, was as follows:

	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets not depreciated				
Land	\$ 252,046	\$ 144,000	\$ -	\$ 396,046
Land - infrastructure right-of-way	1,343,717	8,549	-	1,352,266
Land improvements	185,490	-	-	185,490
Construction in progress - infrastructure	1,320,510	4,288,414	1,249,035	4,359,889
Total capital assets not depreciated	\$ 3,101,763	\$ 4,440,963	\$ 1,249,035	\$ 6,293,691
Capital assets depreciated				
Buildings	\$ 1,492,106	\$ -	\$ -	\$ 1,492,106
Building improvements	989,754	-	-	989,754
Other improvements	177,103	-	-	177,103
Machinery, furniture, and equipment	3,841,938	542,545	213,181	4,171,302
Infrastructure	75,110,079	1,246,262	34,032	76,322,309
Total capital assets depreciated	\$ 81,610,980	\$ 1,788,807	\$ 247,213	\$ 83,152,574
Less: accumulated depreciation for				
Buildings	\$ 631,449	\$ 28,542	\$ -	\$ 659,991
Building improvements	460,877	19,795	-	480,672
Other improvements	36,843	3,542	-	40,385
Machinery, furniture, and equipment	1,705,659	314,210	181,039	1,838,830
Infrastructure	31,716,413	1,302,906	20,704	32,998,615
Total accumulated depreciation	\$ 34,551,241	\$ 1,668,995	\$ 201,743	\$ 36,018,493
Total capital assets depreciated, net	\$ 47,059,739	\$ 119,812	\$ 45,470	\$ 47,134,081
Governmental Activities Capital Assets, Net	\$ 50,161,502	\$ 4,560,775	\$ 1,294,505	\$ 53,427,772

Depreciation expense was charged to functions/programs as follows:

Governmental Activities	
General government	\$ 68,006
Public safety	57,741
Highways and streets, including depreciation of infrastructure assets	1,524,966
Sanitation	11,828
Culture and recreation	1,091
Economic development	5,363
Total Depreciation Expense - Governmental Activities	\$ 1,668,995

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

2. Detailed Notes on All Funds (Continued)

B. Interfund Receivables, Payables, and Transfers

The composition of interfund balances as of December 31, 2005, is as follows:

Due To/From Other Funds

Receivable Fund	Payable Fund	Amount
General	Social Services	\$ 10,747

C. Liabilities

1. Operating Leases

The County leases Extension Office space under a noncancelable operating lease. The cost for the lease was \$8,644 for the year ended December 31, 2005. The future minimum lease payments for the lease are as follows:

Year Ending December 31	Amount
2006	\$ 9,261
2007	9,261

2. Capital Leases/Installment Purchases

The County has entered into a lease agreement as lessee for financing the acquisition of certain equipment. This lease agreement qualifies as a capital lease for accounting purposes and, therefore, has been recorded at the present value of its future minimum lease payment as of the inception date. The motor grader lease is paid from the Road and Bridge Special Revenue Fund. This capital lease consists of the following at December 31, 2005:

Lease	Maturity	Installment	Payment Amount	Original	Balance
Motor grader	2006	Annually	\$ -	\$ 143,339	\$ 143,339

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

2. Detailed Notes on All Funds

C. Liabilities

2. Capital Leases/Installment Purchases (Continued)

The future minimum lease obligation and the net present value of this minimum lease payment as of December 31, 2005, is as follows

Year Ending December 31	Governmental Activities
2006	\$ 151,425
Less: amount representing interest	(8,086)
Present Value of Minimum Lease Payments	\$ 143,339

3. Loans Payable

Houston County received a grant of \$142,000 from the Minnesota Department of Employment and Economic Development. The County used the grant to make an installment loan to fund an economic development project in the County. The County is entitled to the first \$100,000 of principal and interest repayments, and the remaining \$42,000 is to be repaid to the state. Payments on the state loan are deferred until December 2012 when monthly payments of \$1,205, including interest at 6.0 percent, will be made until March 2016. Total payments due from 2012 to 2016, including interest of \$4,265 at December 31, 2005, are \$46,265. The loan payments will be made in the General Fund.

Debt service requirements at December 31, 2005, were as follows:

Year Ending December 31	State Loan	
	Principal	Interest
2010 - 2014	\$ 25,333	\$ 3,617
2015 - 2016	16,667	648
Total	\$ 42,000	\$ 4,265

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

2. Detailed Notes on All Funds

C. Liabilities (Continued)

4. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2005, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Capital Leases	\$ -	\$ 143,339	\$ -	\$ 143,339	\$ 143,339
Loans payable	42,000	-	-	42,000	-
Compensated absences	669,687	-	73,258	596,429	32,571
Long-Term Liabilities	<u>\$ 711,687</u>	<u>\$ 143,339</u>	<u>\$ 73,258</u>	<u>\$ 781,768</u>	<u>\$ 175,910</u>

3. Employee Retirement Systems and Pension Plans

A. Plan Description

All full-time and certain part-time employees of Houston County are covered by defined benefit pension plans administered by the Public Employees Retirement Association of Minnesota (PERA). The PERA administers the Public Employees Retirement Fund, the Public Employees Police and Fire Fund, and the Public Employees Correctional Fund, which are cost-sharing, multiple-employer retirement plans. These plans are established and administered in accordance with Minn. Stat. chs. 353 and 356.

Public Employees Retirement Fund members belong to either the Coordinated Plan or the Basic Plan. Coordinated Plan members are covered by Social Security, and Basic Plan members are not. All new members must participate in the Coordinated Plan. All police officers, firefighters, and peace officers who qualify for membership by statute are covered by the Public Employees Police and Fire Fund. Members who are employed in a county correctional institution and have direct contact with inmates are covered by the Public Employees Correctional Fund.

The PERA provides retirement benefits as well as disability benefits to members and benefits to survivors upon death of eligible members. Benefits are established by state statute and vest after three years of credited service. The retirement benefits are based on a member's highest average salary for any five successive years of allowable service, age, and years of credit at termination of service.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

3. Employee Retirement Systems and Pension Plans

A. Plan Description (Continued)

Two methods are used to compute benefits for Coordinated and Basic Plan members. The retiring member receives the higher of a step-rate benefit accrual formula (Method 1) or a level accrual formula (Method 2). Under Method 1, the annuity accrual rate for a Basic Plan member is 2.2 percent of average salary for each of the first ten years of service and 2.7 percent for each year thereafter. For a Coordinated Plan member, the annuity accrual rate is 1.2 percent of average salary for each of the first ten years of service and 1.7 percent for each successive year. Under Method 2, the annuity accrual rate is 2.7 percent of average salary for Basic Plan members and 1.7 percent for Coordinated Plan members for each year of service. For Public Employees Police and Fire Fund members, the annuity accrual rate is 3.0 percent of average salary for each year of service. For Public Employees Correctional Fund members, the annuity accrual rate is 1.9 percent of average salary for each year of service.

For all Public Employees Retirement Fund members whose annuity is calculated using Method 1, and for all Public Employees Police and Fire Fund and Public Employees Correctional Fund members, a full annuity is available when age plus years of service equal 90. A reduced retirement annuity is also available to eligible members seeking early retirement.

The benefit provisions stated in the previous paragraphs of this section are current provisions and apply to active plan participants. Vested, terminated employees who are entitled to benefits but are not yet receiving them are bound by the provisions in effect at the time they last terminated public service.

The PERA issues a publicly available financial report that includes financial statements and required supplementary information for the Public Employees Retirement Fund, the Public Employees Police and Fire Fund, and the Public Employees Correctional Fund. That report may be obtained on the internet at www.mnpera.org; by writing to PERA at 60 Empire Drive, Suite 200, Saint Paul, Minnesota 55103-2088; or by calling 651-296-7460 or 1-800-652-9026.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

3. Employee Retirement Systems and Pension Plans (Continued)

B. Funding Policy

Pension benefits are funded from member and employer contributions and income from the investment of fund assets. Minn. Stat. ch. 353 sets the rates for employer and employee contributions. These statutes are established and amended by the State Legislature. The County makes annual contributions to the pension plans equal to the amount required by state statutes. Public Employees Retirement Fund Basic Plan members and Coordinated Plan members are required to contribute 9.10 and 5.10 percent, respectively, of their annual covered salary in 2005. Contribution rates in the Coordinated Plan increased in 2006 to 5.50 percent. Public Employees Police and Fire Fund members are required to contribute 6.20 percent of their annual covered salary in 2005. That rate increased to 7.00 percent in 2006. Public Employees Correctional Fund members are required to contribute 5.83 percent of their annual covered salary.

The County is required to contribute the following percentages of annual covered payroll in 2005 and 2006:

	2005	2006
Public Employees Retirement Fund		
Basic Plan members	11.78%	11.78%
Coordinated Plan members	5.53	6.00
Public Employees Police and Fire Fund	9.30	10.50
Public Employees Correctional Fund	8.75	8.75

The County's contributions for the years ending December 31, 2005, 2004, and 2003, for the Public Employees Retirement Fund, the Public Employees Police and Fire Fund, and the Public Employees Correctional Fund were:

	Public Employees Retirement Fund	Public Employees Police and Fire Fund	Public Employees Correctional Fund
2005	\$ 234,998	\$ 50,532	\$ 35,631
2004	230,008	50,265	32,943
2003	227,308	50,260	27,245

These contribution amounts are equal to the contractually required contributions for each year as set by state statute.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

4. Summary of Significant Contingencies and Other Items

A. Risk Management

The County is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; injuries to employees; or natural disasters for which the County carries commercial insurance. The County has entered into a joint powers agreement with other Minnesota counties to form the Minnesota Counties Insurance Trust (MCIT). The County is a member of both the MCIT Workers' Compensation and Property and Casualty Divisions. For other risk, the County carries commercial insurance. There were no significant reductions in insurance from the prior year. The amount of settlements did not exceed insurance coverage for the past three fiscal years.

The Workers' Compensation Division of MCIT is self-sustaining based on the contributions charged, so that total contributions plus compounded earnings on these contributions will equal the amount needed to satisfy claims liabilities and other expenses. MCIT participates in the Workers' Compensation Reinsurance Association with coverage at \$760,000 and \$390,000 per claim in 2005 and 2006, respectively. Should the MCIT Workers' Compensation Division liabilities exceed assets, MCIT may assess the County in a method and amount to be determined by MCIT.

The Property and Casualty Division of MCIT is self-sustaining, and the County pays an annual premium to cover current and future losses. MCIT carries reinsurance for its property lines to protect against catastrophic losses. Should the MCIT Property and Casualty Division liabilities exceed assets, MCIT may assess the County in a method and amount to be determined by MCIT.

The County has entered into a joint powers agreement with the MCIT to authorize the Board to exercise the common powers of the participating governmental units in connection with certain matters pertaining to the administration and funding of group employee benefits and other financial risk management services. The County may choose to participate in any of the services offered. The County may withdraw from the pool at any time giving a 90-day written notice. There is no contingent liability after withdrawal.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

4. Summary of Significant Contingencies and Other Items (Continued)

B. Contingent Liabilities

The County has entered into an agreement with the Minnesota Department of Agriculture and a local lending institution to jointly administer the Agricultural Best Management Loan Program to individuals to implement projects that prevent or mitigate nonpoint source water pollution. While the County is not liable for the repayment of the loans in any manner, it does have certain responsibilities under the agreement. The County has met those responsibilities for 2005.

The County is a defendant in various lawsuits. Although the outcome of these lawsuits is not presently determinable, in the opinion of the County Attorney, the resolution of these matters will not have a material adverse effect on the financial condition of the County.

C. Jointly-Governed Organizations

Houston County, in conjunction with other local governments, has formed joint powers boards to provide a variety of services. The County appoints at least one member to the following organizations:

The Southeast Minnesota Water Resources Board provides regional water quality services to several counties. During the year, the Board received \$3,112 from Houston County.

The Southeast Minnesota Emergency Management Services provides various health services to several counties.

The Workforce Development provides various job training services to several counties. During the year, Houston County paid \$99,338 to the Workforce Development.

The Southeast Minnesota Community Action Council (SEMCCAC) provides various social services emergency assistance services to several counties. It also provides housing and redevelopment for Houston County through Bluff Country. During the year, Houston County paid \$17,143 to SEMCCAC.

The Southeastern Minnesota Narcotics Task Force provides drug enforcement services to several counties. During the year, the County paid \$5,000 to the Task Force.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

4. Summary of Significant Contingencies and Other Items

C. Jointly-Governed Organizations (Continued)

The Southeastern Minnesota Library provides regional library services to counties and cities in southeastern Minnesota. During the year, Houston County paid \$71,364 to the Library.

The Minnesota Counties Computer Cooperative (MCCC) provides computer programming services to several Minnesota counties. During the year, Houston County paid \$78,686 to the MCCC.

D. Joint Venture

Family Services Collaborative

The Houston County Family Services Collaborative was established in 1995 under the authority of Minn. Stat. §§ 471.59 and 124D.23. The Collaborative includes Houston County, four Houston County school districts, and SEMCAC, each of which appoints members to the Collaborative's governing board. The purpose of the Collaborative is to provide a coordinated approach to support and nurture individuals and families through prevention and intervention so as to ensure success for every child.

Control of the Collaborative is vested in a Board of Directors. Houston County appoints two members to this Board. Houston County acts as fiscal agent for the Collaborative. The Collaborative is financed by state grants and appropriations from participating members. During 2005, Houston County provided no funding. In the event of withdrawal from the Collaborative, the withdrawing party shall give a 30-day notice. The withdrawing party remains liable for fiscal obligations incurred prior to the effective date of withdrawal and shall not be entitled to any compensation as long as the Collaborative continues in existence. Should the Collaborative cease to exist, all property, real and personal, at the time of termination shall be distributed by the governing board.

Currently, the Collaborative does not prepare complete financial statements; therefore, the Collaborative does not have audited financial statements. Financial information can be obtained by contacting the following:

Loretta Lillegraven
Fiscal Supervisor
Houston County Public Health Nursing Department
Caledonia, Minnesota 55921

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REQUIRED SUPPLEMENTARY INFORMATION

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**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

Schedule 1

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2005**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Revenues				
Taxes	\$ 3,077,855	\$ 3,077,855	\$ 3,059,175	\$ (18,680)
Licenses and permits	44,775	44,775	59,636	14,861
Intergovernmental	2,069,037	2,069,037	2,370,273	301,236
Charges for services	1,629,200	1,629,200	1,761,794	132,594
Fines and forfeits	18,000	18,000	24,996	6,996
Gifts and contributions	-	-	1,859	1,859
Investment earnings	100,050	100,050	213,459	113,409
Miscellaneous	272,385	272,385	392,166	119,781
Total Revenues	\$ 7,211,302	\$ 7,211,302	\$ 7,883,358	\$ 672,056
Expenditures				
Current				
General government				
Commissioners	\$ 191,984	\$ 191,984	\$ 252,563	\$ (60,579)
Courts	28,500	28,500	76,349	(47,849)
County auditor	193,993	193,993	209,570	(15,577)
License bureau	79,144	79,144	77,294	1,850
County treasurer	120,629	120,629	110,109	10,520
County assessor	305,856	305,856	303,946	1,910
Elections	31,859	31,859	31,781	78
Data processing	235,334	235,334	262,439	(27,105)
Personnel	130,549	130,549	123,203	7,346
Attorney	219,098	219,098	219,185	(87)
Law library	29,000	29,000	45,534	(16,534)
Recorder	173,809	173,809	175,099	(1,290)
Surveyor	149,275	149,275	132,934	16,341
Planning and zoning	197,422	197,422	154,432	42,990
Buildings and plant	220,902	220,902	390,591	(169,689)
Veterans service officer	59,572	59,572	58,477	1,095
Unallocated	206,600	206,600	185,645	20,955
Total general government	\$ 2,573,526	\$ 2,573,526	\$ 2,809,151	\$ (235,625)
Public safety				
Sheriff	\$ 952,138	\$ 952,138	\$ 945,719	\$ 6,419
Boat and water safety	8,708	8,708	6,075	2,633
Coroner	44,000	44,000	46,076	(2,076)
E-911 system	111,598	111,598	108,039	3,559
Law enforcement center	671,356	671,356	821,911	(150,555)
Community corrections	171,941	171,941	231,221	(59,280)
Civil defense	46,598	46,598	50,823	(4,225)
Total public safety	\$ 2,006,339	\$ 2,006,339	\$ 2,209,864	\$ (203,525)

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

Schedule 1
(Continued)

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2005**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Expenditures				
Current (Continued)				
Transportation				
Airport	\$ 25,800	\$ 25,800	\$ 95,211	\$ (69,411)
Sanitation				
Solid waste	\$ 399,696	\$ 399,696	\$ 412,781	\$ (13,085)
Recycling	297,260	297,260	322,372	(25,112)
Total sanitation	\$ 696,956	\$ 696,956	\$ 735,153	\$ (38,197)
Health				
Nursing service	\$ 1,207,587	\$ 1,207,587	\$ 1,257,051	\$ (49,464)
Transportation	10,000	10,000	10,000	-
Health center	4,250	4,250	4,250	-
Total health	\$ 1,221,837	\$ 1,221,837	\$ 1,271,301	\$ (49,464)
Culture and recreation				
Historical society	\$ 34,000	\$ 34,000	\$ 34,000	\$ -
Parks	14,000	14,000	24,492	(10,492)
Regional library	71,364	71,364	71,364	-
Other	72,020	72,020	76,910	(4,890)
Total culture and recreation	\$ 191,384	\$ 191,384	\$ 206,766	\$ (15,382)
Conservation of natural resources				
Cooperative extension	\$ 132,906	\$ 132,906	\$ 121,881	\$ 11,025
Soil and water conservation	135,350	135,350	135,350	-
Agricultural society/County fair	18,000	18,000	18,000	-
Water planning	23,107	23,107	22,429	678
Total conservation of natural resources	\$ 309,363	\$ 309,363	\$ 297,660	\$ 11,703
Economic development				
Community development	\$ 42,900	\$ 42,900	\$ 46,768	\$ (3,868)
Other	5,050	5,050	5,400	(350)
Total economic development	\$ 47,950	\$ 47,950	\$ 52,168	\$ (4,218)
Total Expenditures	\$ 7,073,155	\$ 7,073,155	\$ 7,677,274	\$ (604,119)

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

Schedule 1
(Continued)

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2005**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Excess of Revenues Over (Under) Expenditures	\$ 138,147	\$ 138,147	\$ 206,084	\$ 67,937
Other Financing Sources (Uses)				
Proceeds from sale of assets	5,000	5,000	4,500	(500)
Net Change in Fund Balance	\$ 143,147	\$ 143,147	\$ 210,584	\$ 67,437
Fund Balance - January 1	<u>5,734,073</u>	<u>5,734,073</u>	<u>5,734,073</u>	<u>-</u>
Fund Balance - December 31	<u>\$ 5,877,220</u>	<u>\$ 5,877,220</u>	<u>\$ 5,944,657</u>	<u>\$ 67,437</u>

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

Schedule 2

**BUDGETARY COMPARISON SCHEDULE
ROAD AND BRIDGE FUND
FOR THE YEAR ENDED DECEMBER 31, 2005**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Revenues				
Taxes	\$ 949,865	\$ 949,865	\$ 941,066	\$ (8,799)
Licenses and permits	750	750	1,270	520
Intergovernmental	5,059,289	5,059,289	4,634,970	(424,319)
Charges for services	122,000	122,000	152,464	30,464
Investment earnings	34,200	34,200	42,620	8,420
Miscellaneous	9,250	9,250	11,470	2,220
Total Revenues	\$ 6,175,354	\$ 6,175,354	\$ 5,783,860	\$ (391,494)
Expenditures				
Current				
Transportation				
Administration	\$ 180,690	\$ 180,690	\$ 199,275	\$ (18,585)
Maintenance	1,480,431	1,480,431	1,642,721	(162,290)
Construction	3,970,465	3,970,465	3,465,748	504,717
Equipment maintenance and shop	773,768	773,768	912,616	(138,848)
Total Expenditures	\$ 6,405,354	\$ 6,405,354	\$ 6,220,360	\$ 184,994
Excess of Revenues Over (Under) Expenditures	\$ (230,000)	\$ (230,000)	\$ (436,500)	\$ (206,500)
Other Financing Sources (Uses)				
Capital lease/installment purchase	\$ -	\$ -	\$ 143,339	\$ 143,339
Proceeds from sale of assets	-	-	3,500	3,500
Total Other Financing Sources (Uses)	\$ -	\$ -	\$ 146,839	\$ 146,839
Net Change in Fund Balance	\$ (230,000)	\$ (230,000)	\$ (289,661)	\$ (59,661)
Fund Balance - January 1	2,850,325	2,850,325	2,850,325	-
Increase (decrease) in reserved for inventories	-	-	(151,912)	(151,912)
Fund Balance - December 31	\$ 2,620,325	\$ 2,620,325	\$ 2,408,752	\$ (211,573)

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

Schedule 3

**BUDGETARY COMPARISON SCHEDULE
SOCIAL SERVICES FUND
FOR THE YEAR ENDED DECEMBER 31, 2005**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Revenues				
Taxes	\$ 967,507	\$ 967,507	\$ 951,769	\$ (15,738)
Intergovernmental	2,982,525	2,982,525	2,849,663	(132,862)
Charges for services	-	-	11,185	11,185
Interest on investments	35,000	35,000	41,239	6,239
Total Revenues	\$ 3,985,032	\$ 3,985,032	\$ 3,853,856	\$ (131,176)
Expenditures				
Current				
Human services				
Income maintenance	\$ 881,994	\$ 881,994	\$ 746,696	\$ 135,298
Social services	3,103,038	3,103,038	3,234,998	(131,960)
Total Expenditures	\$ 3,985,032	\$ 3,985,032	\$ 3,981,694	\$ 3,338
Net Change in Fund Balance	\$ -	\$ -	\$ (127,838)	\$ (127,838)
Fund Balance - January 1	2,048,143	2,048,143	2,048,143	-
Fund Balance - December 31	\$ 2,048,143	\$ 2,048,143	\$ 1,920,305	\$ (127,838)

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**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

**NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION
FOR THE YEAR ENDED DECEMBER 31, 2005**

1. Budgetary Information

Annual budgets are adopted on a basis consistent with generally accepted accounting principles for all governmental funds. All annual appropriations lapse at fiscal year-end.

On or before mid-June of each year, all departments and agencies submit requests for appropriations to the County Auditor so that a budget can be prepared. Before October 31, the proposed budget is presented to the Houston County Board for review. The Board holds public hearings, and a final budget must be prepared and adopted no later than December 31.

The appropriated budget is prepared by fund, function, and department. The County's department head may make transfers of appropriations within a department. Transfers of appropriations between departments require approval of the County Board. The legal level of budgetary control (the level at which expenditures may not legally exceed appropriations) is the fund level. During the year, the Board made no supplemental budgetary appropriations.

Encumbrance accounting is employed in governmental funds. Encumbrances (such as purchase orders or contracts) outstanding at year-end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be reapportioned and honored during the subsequent year.

2. Excess of Expenditures Over Appropriations

For the year ended December 31, 2005, expenditures exceeded appropriations in the General Fund by \$604,119. These over-expenditures were funded by a prior year fund equity.

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SUPPLEMENTARY INFORMATION

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**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

AGENCY FUNDS

Agency funds are used to account for assets held by a governmental unit as an agent for individuals, private organizations, other governmental units, and other funds.

The Crooked Creek Watershed Fund accounts for reimbursements to the Watershed District for operations and the collection of assessments to pay the Watershed District's bonded debt and interest.

The Health Fund is used to account for employees' pre-tax health benefits.

The Revolving Fund accounts for the transfer of County collections to the state (mortgage registry tax, game and fish license sales, motor vehicle license sales, state deed tax sales, and state revenue taxes) and the apportionment of state-aid payments for police and fire departments to cities and towns.

The Soil and Water Conservation Fund accounts for the assets of the Root River Soil and Water Conservation District held by the County.

The School Districts Fund accounts for property taxes collected and remitted by the County to the various school districts in the County.

The Family Collaborative Fund accounts for monies received and expended by the Family Services Collaborative.

The Taxes and Penalties Fund accounts for the collection and distribution of property taxes (current and delinquent).

The Towns and Cities Fund accounts for the taxes and other amounts received by the County for the various towns and cities.

The Historic Bluff Country Fund accounts for the monies received and expended by Historic Bluff Country.

The Victim Services Fund accounts for the funds of Victim Services, a nonprofit agency for which the County is the fiscal agent.

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**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

Statement 1

**COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES
ALL AGENCY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2005**

	Balance January 1	Additions	Deductions	Balance December 31
<u>CROOKED CREEK WATERSHED</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 318	\$ 15,311	\$ 15,439	\$ 190
<u>Liabilities</u>				
Due to other governments	\$ 318	\$ 15,311	\$ 15,439	\$ 190
 <u>HEALTH</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 53,228	\$ 131,805	\$ 132,793	\$ 52,240
<u>Liabilities</u>				
Accounts payable	\$ 53,228	\$ 131,805	\$ 132,793	\$ 52,240
 <u>REVOLVING</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 19,816	\$ 3,200,699	\$ 3,207,855	\$ 12,660
<u>Liabilities</u>				
Due to other governments	\$ 19,816	\$ 3,200,699	\$ 3,207,855	\$ 12,660

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

*Statement 1
(Continued)*

**COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES
ALL AGENCY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2005**

	Balance January 1	Additions	Deductions	Balance December 31
<u>SOIL AND WATER CONSERVATION FUND</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 305,866	\$ 527,969	\$ 568,644	\$ 265,191
<u>Liabilities</u>				
Due to other governments	\$ 305,866	\$ 527,969	\$ 568,644	\$ 265,191
 <u>SCHOOL DISTRICTS</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 93,542	\$ 3,556,739	\$ 3,552,503	\$ 97,778
<u>Liabilities</u>				
Due to other governments	\$ 93,542	\$ 3,556,739	\$ 3,552,503	\$ 97,778
 <u>FAMILY COLLABORATIVE</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 535,608	\$ 859,568	\$ 837,024	\$ 558,152
<u>Liabilities</u>				
Due to other governments	\$ 535,608	\$ 859,568	\$ 837,024	\$ 558,152

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

Statement 1
(Continued)

**COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES
ALL AGENCY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2005**

	Balance January 1	Additions	Deductions	Balance December 31
<u>TAXES AND PENALTIES</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 53,850	\$ 15,938,842	\$ 15,923,707	\$ 68,985
<u>Liabilities</u>				
Accounts payable	\$ 53,850	\$ 118,895	\$ 103,760	\$ 68,985
Due to other funds	-	7,014,868	7,014,868	-
Due to other governments	-	8,805,079	8,805,079	-
Total Liabilities	\$ 53,850	\$ 15,938,842	\$ 15,923,707	\$ 68,985
 <u>TOWNS AND CITIES</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 117,098	\$ 4,648,148	\$ 4,661,416	\$ 103,830
<u>Liabilities</u>				
Due to other governments	\$ 117,098	\$ 4,648,148	\$ 4,661,416	\$ 103,830
 <u>HISTORIC BLUFF COUNTRY</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 918	\$ 33,429	\$ 37,558	\$ (3,211)
Due from other governments	-	3,721	-	3,721
Total Assets	\$ 918	\$ 37,150	\$ 37,558	\$ 510
<u>Liabilities</u>				
Accounts payable	\$ -	\$ 37,150	\$ 36,640	\$ 510
Due to other governments	918	-	918	-
Total Liabilities	\$ 918	\$ 37,150	\$ 37,558	\$ 510

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

Statement 1
(Continued)

**COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES
ALL AGENCY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2005**

	Balance January 1	Additions	Deductions	Balance December 31
<u>VICTIM SERVICES</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 8,874	\$ 47,634	\$ 40,769	\$ 15,739
<u>Liabilities</u>				
Due to other governments	\$ 8,874	\$ 47,634	\$ 40,769	\$ 15,739
 <u>TOTAL ALL AGENCY FUNDS</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 1,189,118	\$ 28,960,144	\$ 28,977,708	\$ 1,171,554
Due from other governments	-	3,721	-	3,721
Total Assets	\$ 1,189,118	\$ 28,963,865	\$ 28,977,708	\$ 1,175,275
<u>Liabilities</u>				
Accounts payable	\$ 107,078	\$ 287,850	\$ 273,193	\$ 121,735
Due to other funds	-	7,014,868	7,014,868	-
Due to other governments	1,082,040	21,661,147	21,689,647	1,053,540
Total Liabilities	\$ 1,189,118	\$ 28,963,865	\$ 28,977,708	\$ 1,175,275

OTHER SCHEDULES

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**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

Schedule 4

**SCHEDULE OF INTERGOVERNMENTAL REVENUE
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2005**

Shared Revenue

State

Highway users tax	\$	3,797,616
HACA		966,937
Market value credit		826,782
PERA rate reimbursement		23,696
Disparity reduction aid		139,652
Police aid		50,264
		5,804,947

Total Shared Revenue **\$ 5,804,947**

Reimbursement for Services

Minnesota Department of Human Services	\$	847,564
		847,564

Payments

Local

Local contribution	\$	2,823
Payments in lieu of taxes		136,080
		138,903

Total Payments **\$ 138,903**

Grants

State

Minnesota Department of		
Corrections	\$	96,111
Public Safety		85,160
Transportation		8,801
Health		275,929
Natural Resources		103,954
Human Services		1,049,165
Water and Soil Resources Board		95,284
Office of Environmental Assistance		50,996
		1,765,400

Total State **\$ 1,765,400**

Federal

Department of		
Agriculture	\$	50,511
Defense		1,058
Transportation		511,291
Homeland Security		58,003
Health and Human Services		677,229
		1,298,092

Total Federal **\$ 1,298,092**

Total Grants **\$ 3,063,492**

Total Intergovernmental Revenue **\$ 9,854,906**

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

Schedule 5

**TAX CAPACITY, TAX RATES, LEVIES, AND PERCENTAGE OF COLLECTIONS
FOR CALENDAR YEARS 2004 THROUGH 2006**

	<u>Tax Year 2004</u>		<u>Tax Year 2005</u>		<u>Tax Year 2006</u>	
	<u>Net Tax Capacity</u>	<u>Tax Capacity Rate Percent (%)</u>	<u>Net Tax Capacity</u>	<u>Tax Capacity Rate Percent (%)</u>	<u>Net Tax Capacity</u>	<u>Tax Capacity Rate Percent (%)</u>
Tax Capacity						
Real property	\$ 9,925,014		\$ 10,990,349		\$ 12,224,102	
Personal property	249,294		275,489		269,973	
Tax increment financing	(131,150)		(152,958)		(140,092)	
Net Tax Capacity	<u>\$ 10,043,158</u>		<u>\$ 11,112,880</u>		<u>\$ 12,353,983</u>	
Tax Levied for County						
County Revenue	\$ 3,347,172	33.675	\$ 3,582,915	32.696	\$ 3,901,411	32.125
Road and Bridge	993,282	9.89	1,122,528	10.101	1,304,136	10.556
Human Services	1,140,799	11.359	1,135,557	10.218	1,146,453	9.280
Net Tax Levy	<u>\$ 5,481,253</u>	<u>54.924</u>	<u>\$ 5,841,000</u>	<u>53.015</u>	<u>\$ 6,352,000</u>	<u>51.961</u>
Taxable Valuations	<u>Tax Capacity</u>	<u>Market Value</u>	<u>Tax Capacity</u>	<u>Market Value</u>	<u>Tax Capacity</u>	<u>Market Value</u>
Light and Power Tax						
Transmission lines	\$ 5,876	\$ 293,800	\$ 6,080	\$ 304,000	\$ 6,202	\$ 310,100
Distribution lines	334	16,700	346	17,300	354	17,700
Total Taxable Valuations - Light and Power	<u>\$ 6,210</u>	<u>\$ 310,500</u>	<u>\$ 6,426</u>	<u>\$ 321,300</u>	<u>\$ 6,556</u>	<u>\$ 327,800</u>
Light and Power Tax Levy						
Transmission lines	\$ 7,164	\$ 346	\$ 7,318	\$ 326	\$ 7,204	\$ 434
Distribution lines	406	20	416	18	412	24
Total Light and Power Tax Levy	<u>\$ 7,570</u>	<u>\$ 366</u>	<u>\$ 7,734</u>	<u>\$ 344</u>	<u>\$ 7,616</u>	<u>\$ 458</u>
Percentage of tax collections for all purposes	99.02%		99.05%			

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**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

Schedule 6

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED DECEMBER 31, 2005

I. SUMMARY OF AUDITOR'S RESULTS

- A. Our report expresses an unqualified opinion on the financial statements of Houston County.
- B. Reportable conditions in internal control were disclosed by the audit of financial statements of Houston County and are reported in the "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*." Reportable condition 05-1 is a material weakness.
- C. No instances of noncompliance material to the financial statements of Houston County were disclosed during the audit.
- D. A reportable condition relating to the audit of the major federal award programs is reported in the "Report on Compliance with Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance with OMB Circular A-133." The reportable condition is a material weakness.
- E. The Auditor's Report on Compliance for the major federal award programs for Houston County expresses an unqualified opinion.
- F. No findings were disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133.
- G. The major programs are:
 - Cluster Programs
 - Child Care Development Block Grant CFDA #93.575
 - Child Care Mandatory and Matching Funds CFDA #93.596
 - Social Services Block Grant Title XX CFDA #93.667
- H. The threshold for distinguishing between Types A and B programs was \$300,000.
- I. Houston County was determined to be a low-risk auditee.

II. FINDINGS RELATED TO FINANCIAL STATEMENTS AUDITED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

INTERNAL CONTROL

PREVIOUSLY REPORTED ITEM NOT RESOLVED

98-1 Disaster Recovery Plan and Data Processing Security
01-2

As noted in prior audits, Houston County has not developed a formal written disaster recovery plan to ensure continued County operation in the case of a disaster or major computer breakdown. A formal disaster recovery plan would give greater assurance that the County is prepared for a disaster or major computer breakdown. With the County's record management relying more on electronic recordkeeping, such as an imaging system, the daily operations and financial risks of loss are increasing. The County needs to provide for the continuance of several important services and applications processed by its computer system, including the preparation of payroll, the calculation of tax assessments and settlements, the recording of receipts and disbursements, and imaging documents. Some of these applications provide data needed within very short time spans. Data not easily recoverable could be lost, time could be lost in recovering data, and there would be increased costs to recover the data.

A formal disaster recovery plan should address natural disasters and computer failures. Some of the items commonly found in disaster recovery plans include, but are not limited to, the following:

- a list of key personnel, including the actual recovery team(s), who should be available during the recovery process;
- a description of the responsibilities of each member of the recovery team(s) and of all other County staff;
- a plan of how the County should continue operations until normal operations are re-established--this could include the use of alternative computer facilities or the use of manual procedures;
- a list of materials the County would need to continue operations and how they would be obtained;
- identification of what space should be used;

- a plan on how back-up data would be obtained from a secure storage area and how the data would be used;
- a timetable of when procedures would take place; and
- a schedule for developing, periodically reviewing, testing, and updating the plan.

The County has one security setting on the AS/400 set below the recommended minimums for the AS/400. The QLMTDEVSSN setting is set at 0. This system determines whether a user can be signed on at more than one workstation at the same time. The recommended setting value is 1.

We recommend that the County Board officially develop, implement, and test a disaster recovery plan. All County employees should be familiar with the plan. The plan should detail the steps to be taken to continue operations in the event of a disaster. The plan should have copies with each member of the recovery team, in the data center, and stored at a secure off-site location. We also recommend the County review its security settings for its AS/400 and document the need not to follow recommended security levels and what other procedures it has in place to provide the needed security.

ITEM ARISING THIS YEAR

05-1 Segregation of Duties

Within the County Treasurer's Office and several smaller departments throughout the County, the duties are not adequately segregated between those employees that have access to assets and the accounting records. We noted in our review that the Treasurer's Office has one employee, a Deputy, other than the County Treasurer. In the absence of the Treasurer or the Deputy, the County Information System Supervisor assists with the duties in the Treasurer's Office. There are occasions when both the Treasurer and Deputy are away from the Office, and the County Information System Supervisor performs all the duties in the Treasurer's Office. This situation poses a lack of segregation of duties because the Information System Supervisor has access to all aspects of the County computer applications and also access to perform certain Treasurer duties. This situation can cause unintentional or intentional errors not to be caught on a timely basis.

We recommend that the County Board take the necessary steps to adequately segregate the duties between those that have access to County's assets and the accounting records.

III. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARD PROGRAMS

A. COMPLIANCE

ITEM ARISING THIS YEAR

05-2 Failure to Perform Case Redetermination - Child Care Assistance Program
(CFDA #93.596)

In our review, we noted that the County did not perform the required redetermination of several participants on the program. The redetermination is required to be done within every 12 months to determine if the participant is still eligible for the program, any changes within the household, and what the participant's co-payment is because of household income and size of family. We also found two case files did not have the proper calculation for co-payment listed in DHS Bulletin #04-68-06, which lists the 2005 co-payment schedules for the Child Care Assistance Program.

We recommend the County follow the program requirements of the Child Care Assistance Program and make sure case files are up to date and co-payments follow the DHS state fiscal year co-payment schedules for the Child Care Assistance Program.

Corrective Action Plan:

Name of Contact Person Responsible for Corrective Action:

Bonnie Goetzing, Financial Assistance Supervisor

Corrective Action Planned:

Prior to our Childcare visit, the County had no way of tracking reviews. Since your visit, we have set up an Excel spreadsheet with the case load list, addresses, and months the reviews are due. Every six months the labels are printed, and a monthly reminder is given out for mailing the reviews.

The County plan is to have the Supervisor pull one file monthly to review from each of the worker's case loads. These cases will be selected randomly, and a file will be kept on all reviews. When reviewing the files, we will check for verifications, household size, income calculation, fee

schedule applied, and timeliness of reviews. The Financial Assistance Supervisor is the person responsible for this, the Financial Assistance Supervisor in turn will report any findings to the Human Services Director.

Anticipated Completion Date:

Already implemented.

B. INTERNAL CONTROL

ITEM ARISING THIS YEAR

05-3 Controls Over Child Care Case Files (CFDA #93.596)

During our review of the Child Care Assistance Program control procedures, we found a lack of controls for monitoring case file redeterminations as required within every twelve months. This information is needed to determine eligibility requirements. There is no proper advance notice of when these redeterminations are needed, other than to manually look at the application or old redetermination in the individual case file to determine if this redetermination is needed.

We recommend the County set up controls that will let the case worker know when redeterminations are needed as well as any other information needed for the Child Care Assistance Program.

Corrective Action Plan:

Name of Contact Person Responsible for Corrective Action:

Bonnie Goetzinger, Financial Assistance Supervisor

Corrective Action Planned:

Prior to our Childcare visit, the County had no way of tracking reviews. Since your visit, we have set up an Excel spreadsheet with the case load list, addresses, and months the reviews are due. Every six months the labels are printed, and a monthly reminder is given out for mailing the reviews.

The County plan is to have the Supervisor pull one file monthly to review from each of the worker's caseloads. These cases will be selected randomly, and a file will be kept on all reviews. When reviewing the files, we will check for verifications, household size, income calculation, fee schedule applied, and timeliness of reviews. The Financial Assistance Supervisor is the person responsible for this, the Financial Assistance Supervisor in turn will report any findings to the Human Services Director.

Anticipated Completion Date:

Already implemented.

IV. OTHER FINDINGS AND RECOMMENDATIONS

A. MINNESOTA LEGAL COMPLIANCE

PREVIOUSLY REPORTED ITEMS RESOLVED

Financial Statement Presentation (02-5)

Minn. Stat. § 375.17 states the County is responsible for preparing the financial statements by the first part of March following year-end.

Resolution

Houston County is working with the State Auditor's Office to prepare financial data in a timely manner.

Publishing Board Minutes, Financial Statements, and Claims Paid (03-1)

Houston County was not complying with Minn. Stat. § 375.12 for publishing minutes and claims paid.

Resolution

We did not find any noncompliance with Minn. Stat. § 375.12.

B. MANAGEMENT PRACTICES

ITEM ARISING THIS YEAR

05-4 Revolving Fund Cash Balance

As of December 31, 2005, the Revolving Agency Fund cash balance was \$12,660 and the account activity report cash balance was \$51,845. Manual warrants were entered into the IFS system but not the cash credits. The County contacted TriMin to get the issue resolved but did not follow up with them to ensure the correction was made. Therefore, the Treasurer's cash trial balance and account activity report cash balance were out of balance.

We recommend the County contact TriMin and have the problem corrected.

PREVIOUSLY REPORTED ITEM NOT RESOLVED

00-4 Consolidated General Ledger

Currently, separate general ledgers are maintained by the County Auditor and the Social Services Department. Each department enters its detailed transactions in the corresponding general ledger. The detailed financial transactions recorded in the Social Services Department ledger are interfaced with the County's main general ledger, maintained by the County Auditor's Office, as "batched" totals with no detail information.

The County Auditor and Road and Bridge Department general ledgers are partially integrated. The disbursement transactions are entered into the cost system by the Road and Bridge Department accountant and interfaced with the County's main general ledger in detail. The receipts transactions are entered into the main general ledger by the County Auditor and entered again by the Road and Bridge accountant as "batched" adjustments to the costing section of the ledger.

Accounting and reporting controls are more efficient and effective when all transactions are accounted for in one centralized general ledger. The County Board and management are better able to implement and maintain internal control over one centralized computer system than several decentralized systems. Security access controls to a centralized general ledger could be established so that departments and employees would have the same responsibility and authority for entering detailed transactions as is currently done with separate departmental general ledgers. Managers and employees should have access to assets or records

based only on the specific needs commensurate with their positions. A centralized general ledger generally provides more uniformity and consistency in accounting for financial transactions. In addition, it allows senior management to have independent access to financial information for the entire County as needed to manage and monitor its financial operations.

We strongly recommend that the County Board provide the necessary directives to department managers to complete the process of consolidating all transactions into one general ledger system. This would improve efficiencies in maintaining County financial records and preparing required reports.

C. OTHER ITEM FOR CONSIDERATION

Other Postemployment Benefits (OPEB)

The Governmental Accounting Standards Board (GASB) recently issued Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which establishes financial reporting for OPEB plans, and Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, which governs employer accounting and financial reporting for OPEB. These standards, similar to what GASB Statements 25 and 27 did for government employee pension benefits and plans, provide the accounting and reporting standards for the various other postemployment benefits many local governments offer to their employees. OPEB can include many different benefits offered to retirees such as health, dental, life, and long-term care insurance coverage.

If retirees are included in an insurance plan and pay a rate similar to that paid for younger active employees, this implicit subsidy is considered OPEB. In fact, local governments may be required to continue medical insurance coverage pursuant to Minn. Stat. § 471.61, subd. 2b. This benefit is common when accumulated sick leave is used to pay for retiree medical insurance. Under the new GASB statements, accounting for OPEB is now similar to the accounting used by governments for pension plans.

Schedule 6
(Continued)

Some of the issues that the County Board will need to address in order to comply with the statements are:

- determine if employees are provided OPEB;
- if OPEB are being provided, the County Board will have to determine whether it will advance fund the benefits or pay for them on a pay-as-you-go basis;
- if OPEB are being provided, and the County Board determines that the establishment of a trust is desirable in order to fund the OPEB, the County Board will have to wait until legislation is enacted authorizing the creation of an OPEB trust and establishing an applicable investment standard; and
- in order to determine annual costs and liabilities that need to be recognized, the County Board will have to decide whether to hire an actuary.

If applicable for Houston County, GASB Statements 43 and 45 would be implemented for the years ending December 31, 2007 and 2008, respectively.

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OTHER REQUIRED REPORTS

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PATRICIA ANDERSON
STATE AUDITOR

**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***

Board of County Commissioners
Houston County

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Houston County as of and for the year ended December 31, 2005, and have issued our report thereon dated November 14, 2006. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Houston County's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operations that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the County's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable conditions are described in the accompanying Schedule of Findings and Questioned Costs as items 98-1/01-2 and 05-1.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the

financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions listed above, we consider item 05-1 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Houston County's financial statements are free of 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*.

Minnesota Legal Compliance

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the provisions of the *Minnesota Legal Compliance Audit Guide for Local Government*, promulgated by the State Auditor pursuant to Minn. Stat. § 6.65. Accordingly, the audit included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

The *Minnesota Legal Compliance Audit Guide for Local Government* contains six categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, and miscellaneous provisions. Our study included all of the listed categories.

The results of our tests indicate that, for the items tested, Houston County complied with the material terms and conditions of applicable legal provisions.

This report is intended solely for the information and use of the Board of County Commissioners, management, and federal awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than those specified parties.

/s/Pat Anderson

PATRICIA ANDERSON
STATE AUDITOR

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

End of Fieldwork: November 14, 2006



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PATRICIA ANDERSON
STATE AUDITOR

REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

Board of County Commissioners
Houston County

Compliance

We have audited the compliance of Houston County with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended December 31, 2005. Houston County's major federal programs are identified in the Summary of Auditor's Results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the County's management. Our responsibility is to express an opinion on the County's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Houston County's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the County's compliance with those requirements.

In our opinion, Houston County complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended December 31, 2005.

However, the results of our auditing procedures disclosed instances of noncompliance with those requirements that are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying Schedule of Findings and Questioned Costs as item 05-2.

Internal Control Over Compliance

The management of Houston County is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the County's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on the internal control over compliance in accordance with OMB Circular A-133.

We noted a matter involving the internal control over compliance and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect Houston County's ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts, and grants. The reportable condition is described in the accompanying Schedule of Findings and Questioned Costs as item 05-3.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, the reportable condition listed above was considered to be a material weakness.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Houston County as of and for the year ended December 31, 2005, and have issued our report thereon dated November 14, 2006. Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise the County's basic financial statements. The accompanying Schedule of Expenditures

of Federal Awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

This report is intended solely for the information and use of the Board of County Commissioners, management, and federal awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than those specified parties.

/s/Pat Anderson

PATRICIA ANDERSON
STATE AUDITOR

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

End of Fieldwork: November 14, 2006

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**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

Schedule 7

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2005**

Federal Grantor Pass-Through Agency Grant Program Title	Federal CFDA Number	Expenditures
U.S. Department of Agriculture		
Passed Through Minnesota Department of Health Special Supplemental Nutrition Program for Women, Infants, and Children	10.557	\$ 45,081
Passed Through Minnesota Department of Human Services Matching Grants for Food Stamp Program	10.561	2,538
Total U.S. Department of Agriculture		\$ 47,619
U.S. Department of Defense		
Passed Through Minnesota Department of Employment and Economic Development Flood Control	12.104	\$ 1,058
U.S. Department of Transportation		
Passed Through Minnesota Department of Transportation Airport Improvement Program	20.106	\$ 55,027
Highway Planning and Construction	20.205	479,724
State and Community Highway Safety	20.600	2,735
Total U.S. Department of Transportation		\$ 537,486
U.S. Department of Health and Human Services		
Passed Through Minnesota Department of Health Centers for Disease Control and Prevention - Investigations and Technical Assistance	93.283	\$ 29,454
Temporary Assistance for Needy Families (TANF)	93.558	14,203
Maternal and Child Health Services Block Grant	93.994	21,705
Passed Through Minnesota Department of Human Services Temporary Assistance for Needy Families (TANF)	93.558	70,614
Child Care Development Block Grant	93.575	123,296
Child Care Mandatory and Matching Funds	93.596	160,215
Children's Justice Grant	93.643	5,900
Child Welfare Services - State Grants	93.645	17,431
Foster Care Title IV-E	93.658	97,191
Social Services Block Grant Title XX	93.667	112,627
Chafee Foster Care Independent Living	93.674	6,608
Community Mental Health Services	93.958	2,100
Total U.S. Department of Health and Human Services		\$ 661,344

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

Schedule 7
(Continued)

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2005**

Federal Grantor Pass-Through Agency Grant Program Title	Federal CFDA Number	Expenditures
U.S. Department of Homeland Security		
Passed Through Minnesota Department of Public Safety		
State Domestic Preparedness Equipment Support Program	97.004	\$ 46,083
Homeland Security Grant	97.067	<u>11,920</u>
Total U.S. Department of Homeland Security		\$ 58,003
Total Federal Awards		\$ <u>1,305,510</u>

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2005**

1. Reporting Entity

The Schedule of Expenditures of Federal Awards presents the activities of federal award programs expended by Houston County. The County's reporting entity is defined in Note 1 to the financial statements.

2. Basis of Presentation

The accounting records for grant programs are maintained on the modified accrual basis of accounting. Under the modified accrual basis, revenues are recorded when susceptible to accrual, that is, both measurable and available. Available means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Expenditures are recorded when the liability is incurred.

The information in this schedule is presented in accordance with the requirements of Office of Management and Budget OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

3. Reconciliation to Schedule of Intergovernmental Revenues

Federal grant revenue per Schedule of Intergovernmental Revenues	\$ 1,298,092
Special Supplemental Nutrition for Women, Infants, and Children grant deferred in 2004 and recognized in 2005	(2,892)
Airport Improvement Program grant received more than 60 days after year-end	7,527
Highway Planning and Construction grant deferred in 2004 and recognized in 2005	(4,716)
Highway Planning and Construction grant received more than 60 days after year-end	23,986
State and Community Highway Safety grant deferred in 2004 and recognized in 2005	(602)
Temporary Assistance for Needy Families grant deferred in 2004 and recognized in 2005	(15,885)
	<hr/>
Expenditures per Schedule of Expenditures of Federal Awards	<u>\$ 1,305,510</u>

4. Pass-Through Grant Numbers

Pass-through grant numbers were not assigned by the pass-through agencies.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

5. Subgrants

During 2005, the County did not pass any federal money to subrecipients.