

# STATE OF MINNESOTA

## Office of the State Auditor



**Rebecca Otto**  
**State Auditor**

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**COTTONWOOD-JACKSON**  
**COMMUNITY HEALTH SERVICES**  
**JACKSON, MINNESOTA**

YEARS ENDED DECEMBER 31, 2004 AND 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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**COTTONWOOD-JACKSON  
COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

**Years Ended December 31, 2004 and 2005**



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

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**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

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**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

ORGANIZATION  
2005

Office	Name
Board of Health	
Cottonwood County Commissioners	
1st District	Gary Sorenson
2nd District	Ron Kuecker
3rd District	Chuck Severson <sup>2</sup>
4th District	Norman Holman
5th District	John Oeltjenbruns
Jackson County Commissioners	
1st District	Craig Rubis
2nd District	Loren Tusa
3rd District	Kathy Hohenstein
4th District	Roger Ringkob <sup>1</sup>
5th District	Robert Ferguson <sup>3</sup>
Nursing Director/Administrator	Patricia Stewart

<sup>1</sup>Chair 2006

<sup>2</sup>Chair 2005

<sup>3</sup>Chair 2004

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REBECCA OTTO  
STATE AUDITOR

# STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

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## INDEPENDENT AUDITOR'S REPORT

Board of Health  
Cottonwood-Jackson Community Health Services

We have audited the accompanying financial statements of Cottonwood-Jackson Community Health Services as of and for the years ended December 31, 2004 and 2005, as listed in the table of contents. These financial statements are the responsibility of the Health Services' management. Our responsibility is to express an opinion on these financial statements based on our audit.

Except as discussed in the following paragraphs, we conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 opinion.

We were unable to obtain sufficient competent evidential matter to support the capital asset balances on the statement of net assets at December 31, 2004 or 2005, or the changes during the year.

In our opinion, except for the effects of such adjustments on the financial statements, if any, as might have been determined to be necessary had we been able to examine evidence regarding capital asset balances and changes, the financial statements referred to above present fairly, in all

material respects, the financial position of Cottonwood-Jackson Community Health Services as of December 31, 2004 and 2005, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

*/s/Rebecca Otto*

REBECCA OTTO  
STATE AUDITOR

*/s/Greg Hierlinger*

GREG HIERLINGER, CPA  
DEPUTY STATE AUDITOR

End of Fieldwork: September 6, 2006

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

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**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
December 31, 2004 and 2005  
(Unaudited)

Cottonwood-Jackson Community Health Services Management's Discussion and Analysis (MD&A) provides an overview of the Health Services' financial activities for the fiscal years ended December 31, 2004 and 2005. Since this information is designed to focus on the current year's activities, resulting changes, and currently known facts, it should be read in conjunction with the Health Services financial statements.

The Health Services is a joint powers enterprise operation of Cottonwood and Jackson Counties created to provide community health care for the residents of the two-county area.

**OVERVIEW OF THE FINANCIAL STATEMENTS**

This MD&A is intended to serve as an introduction to the basic financial statements. The Health Services basic financial statements consist of two parts: the financial statements and the notes to the financial statements. The MD&A (this section) is required to accompany the basic financial statements and, therefore, is included as required supplementary information.

The financial statements present the Health Services financial activities and consist of the following:

- The statement of net assets compares the assets and liabilities to give an overall view of the financial health of the Health Services.
- The statement of revenues, expenses, and changes in net assets provides information on an aggregate view of the Health Services finances. All of the current year's revenues and expenses are taken into account, regardless of when the cash was received or paid.
- The statement of cash flows provides sources and uses of cash for the Health Services.

## FINANCIAL ANALYSIS

### Net Assets

	2004	2005	Increase (Decrease)	Percent Change (%)	2003 Comparative
<b>Assets</b>					
Current and other assets	\$ 356,038	\$ 419,205	\$ 63,167	17.74	\$ 233,660
Capital assets	54,306	50,975	(3,331)	(6.13)	54,383
<b>Total Assets</b>	<b>\$ 410,344</b>	<b>\$ 470,180</b>	<b>\$ 59,836</b>	<b>14.58</b>	<b>\$ 288,043</b>
<b>Liabilities</b>					
Current liabilities	\$ 60,210	\$ 57,700	\$ (2,510)	(4.17)	\$ 31,109
Noncurrent liabilities	61,977	77,303	15,326	24.73	86,422
<b>Total Liabilities</b>	<b>\$ 122,187</b>	<b>\$ 135,003</b>	<b>\$ 12,816</b>	<b>10.49</b>	<b>\$ 117,531</b>
<b>Net Assets</b>					
Invested in capital assets	\$ 54,306	\$ 50,975	\$ (3,331)	(6.13)	\$ 54,383
Restricted for other purposes	57,547	58,628	1,081	1.88	57,042
Unrestricted	176,304	225,574	49,270	27.95	59,087
<b>Total Net Assets</b>	<b>\$ 288,157</b>	<b>\$ 335,177</b>	<b>\$ 47,020</b>	<b>16.32</b>	<b>\$ 170,512</b>

Cottonwood-Jackson Community Health Services tried to maximize its restricted and unrestricted investments by investing in certificates of deposit with high interest rates as well as adding to total amount invested. The increase in assets from 2004 to 2005 was a result of that action.

The increase in total liabilities from 2004 to 2005 is due to an increase in salaries payable and an increase in long-term compensated absences payable. Salaries payable is due to a full two weeks of salaries earned in 2005 but not paid until 2006. Additionally, the Health Services has a number of employees accruing vacation and sick leave at the maximum rate and thus the reason for the increase in long-term compensated absences.

### Changes in Revenues, Expenses, and Net Assets

	2004	2005	Increase (Decrease)	Percent Change (%)	2003 Comparative
<b>Operating Revenues</b>					
Charges for services	\$ 531,079	\$ 566,323	\$ 35,244	6.64	\$ 467,630
Miscellaneous	44,494	36,205	(8,289)	(18.63)	28,071
<b>Total Operating Revenues</b>	<b>\$ 575,573</b>	<b>\$ 602,528</b>	<b>\$ 26,955</b>	<b>4.68</b>	<b>\$ 495,701</b>
<b>Nonoperating Revenues</b>					
Intergovernmental	578,462	671,493	93,031	16.08	555,306
Interest and donations	998	2,697	1,699	170.24	784
<b>Total Revenues</b>	<b>\$ 1,155,033</b>	<b>\$ 1,276,718</b>	<b>\$ 121,685</b>	<b>10.55</b>	<b>\$ 1,051,791</b>

	2004	2005	Increase (Decrease)	Percent Change (%)	2003 Comparative
Operating Expenses					
Professional services	\$ 984,407	\$ 1,172,383	\$ 187,976	19.10	\$ 1,033,713
Administration	29,858	46,472	16,614	55.64	29,967
Depreciation and loss on disposal	23,123	10,843	(12,280)	53.11	7,808
Total Expenses	<u>\$ 1,037,388</u>	<u>\$ 1,229,698</u>	<u>\$ 192,310</u>	18.54	<u>\$ 1,071,488</u>
Change in Net Assets	<u>\$ 117,645</u>	<u>\$ 47,020</u>	<u>\$ (70,625)</u>	(60.03)	<u>\$ (19,697)</u>

Total revenues increased from 2004 to 2005. Cottonwood-Jackson Community Health Services saw a 6.64 percent increase in charges for services. The majority of these dollars can be attributed to the increased Medicare patient load in the Home Health Care program. Additionally, Cottonwood-Jackson Community Health Services contracted with Nobles-Rock Public Health Services to participate in the Smoke Free Communities Grant; this brought in over \$100,000 in grant dollars.

Total expenses increased from 2004 to 2005 due to the increase in services provided. Increased Home Care clients resulted in additional Home Health Aide hours and medical supplies to care for those clients. New staff was hired, and supplies and equipment were purchased to carry out the Smoke Free Communities Work Plan. This is all in addition to the increase in employee salaries and health insurance premiums.

#### **CAPITAL ASSETS ADMINISTRATION**

##### **Capital Assets (Net of Depreciation)**

	2004	2005	Increase (Decrease)	Percent Change (%)
Machinery, furniture, and equipment	<u>\$ 54,306</u>	<u>\$ 50,975</u>	<u>\$ (3,331)</u>	(6.13%)

Additions were the purchase of an agency vehicle, copier, as well as computers and other equipment for the Smoke Free Communities Grant.

#### **FUTURE EVENTS**

Cottonwood-Jackson Community Health Services looks forward to the future. The Public Health Board and administration always assess the needs of our community citizens along with the grants, fees, and state and local dollars it will be receiving for the coming year. Cottonwood-Jackson Community Health Services will evaluate staffing patterns to handle the activities for the coming year. We will monitor the Health Services financial status monthly and monitor activities planned for our community.

## **CONTACTING THE HEALTH SERVICES FINANCIAL MANAGEMENT**

This financial report is designed to provide our citizens, taxpayers, customers, and creditors with a general overview of Cottonwood-Jackson Community Health Services finances and to show the Health Services accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Administrator, Patricia A. Stewart, Administrator, Cottonwood-Jackson Community Health Services, 407 - 5th Street, Suite 209; Jackson, Minnesota 56143.

## **BASIC FINANCIAL STATEMENTS**

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**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

**EXHIBIT 1**

**STATEMENT OF NET ASSETS  
DECEMBER 31, 2004 AND 2005**

	<b>2004</b>	<b>2005</b>
<b><u>Assets</u></b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 137,489	\$ 172,874
Petty cash and change funds	60	60
Accounts receivable	119,531	103,961
Due from other governments	41,411	83,682
<b>Restricted assets</b>		
Cash and pooled investments	56,992	57,795
Accrued interest receivable	555	833
<b>Total current assets</b>	<b>\$ 356,038</b>	<b>\$ 419,205</b>
<b>Noncurrent assets</b>		
Depreciable capital assets (net)	54,306	50,975
<b>Total Assets</b>	<b>\$ 410,344</b>	<b>\$ 470,180</b>
<b><u>Liabilities</u></b>		
<b>Current liabilities</b>		
Accounts payable	\$ 12,196	\$ 12,246
Salaries payable	27,615	32,193
Compensated absences payable	18,262	12,772
Due to other governments	2,137	489
<b>Total current liabilities</b>	<b>\$ 60,210</b>	<b>\$ 57,700</b>
<b>Noncurrent liabilities</b>		
Compensated absences payable	61,977	77,303
<b>Total Liabilities</b>	<b>\$ 122,187</b>	<b>\$ 135,003</b>
<b><u>Net Assets</u></b>		
Invested in capital assets	\$ 54,306	\$ 50,975
Restricted for other purposes	57,547	58,628
Unrestricted	176,304	225,574
<b>Total Net Assets</b>	<b>\$ 288,157</b>	<b>\$ 335,177</b>

**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

**EXHIBIT 2**

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS  
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2005**

	2004	2005
<b>Operating Revenues</b>		
Charges for services	\$ 531,079	\$ 566,323
Preadmission screening	15,668	14,770
Immunizations	19,657	12,119
Miscellaneous	9,169	9,316
<b>Total Operating Revenues</b>	<b>\$ 575,573</b>	<b>\$ 602,528</b>
<b>Operating Expenses</b>		
Family health	\$ 308,335	\$ 243,632
Disease prevention and control	47,353	59,201
Home health care	565,103	653,242
Health promotion	63,616	216,308
Administration	29,858	46,472
Depreciation	9,423	10,197
Loss on disposal of capital assets	13,700	646
<b>Total Operating Expenses</b>	<b>\$ 1,037,388</b>	<b>\$ 1,229,698</b>
<b>Operating Income (Loss)</b>	<b>\$ (461,815)</b>	<b>\$ (627,170)</b>
<b>Nonoperating Revenues (Expenses)</b>		
Intergovernmental		
State		
Local public health	\$ 120,012	\$ 120,030
Minnesota miscellaneous boards	1,114	1,249
Minnesota ENABL	44,559	31,000
Federal		
Women, Infants, and Children	64,988	69,327
Immunization Grants	1,800	1,150
Centers for Disease Control and Prevention	39,205	36,712
Temporary Assistance for Needy Families	18,765	19,625
Maternal and Child Health	37,234	37,247
Local		
County appropriations	220,252	221,663
Other	29,584	132,988
Interest income	998	2,697
Contributions and donations	949	502
<b>Total Nonoperating Revenues (Expenses)</b>	<b>\$ 579,460</b>	<b>\$ 674,190</b>
<b>Increase (Decrease) in Net Assets</b>	<b>\$ 117,645</b>	<b>\$ 47,020</b>
<b>Net Assets - January 1, restated (Note 1.G.)</b>	<b>170,512</b>	<b>288,157</b>
<b>Net Assets - December 31</b>	<b>\$ 288,157</b>	<b>\$ 335,177</b>

**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

**EXHIBIT 3**

**STATEMENT OF CASH FLOWS  
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2005  
Increase (Decrease) in Cash and Cash Equivalents**

	<b>2004</b>	<b>2005</b>
<b>Cash Flows from Operating Activities</b>		
Receipts from customers and users	\$ 567,308	\$ 618,098
Payments to employees and suppliers	(1,009,609)	(1,206,039)
<b>Net cash provided by (used in) operating activities</b>	<b>\$ (442,301)</b>	<b>\$ (587,941)</b>
<b>Cash Flows from Noncapital Financing Activities</b>		
Intergovernmental receipts	\$ 336,701	\$ 324,662
County appropriations	220,252	221,663
Other local grants	19,546	82,395
Contributions	949	502
<b>Net cash provided by (used in) noncapital financing activities</b>	<b>\$ 577,448</b>	<b>\$ 629,222</b>
<b>Cash Flows from Capital and Related Financing Activities</b>		
Acquisition of capital assets	\$ (23,046)	\$ (7,512)
<b>Cash Flows from Investing Activities</b>		
Investment income	\$ 1,375	\$ 2,419
<b>Net Increase (Decrease) in Cash and Cash Equivalents</b>	<b>\$ 113,476</b>	<b>\$ 36,188</b>
<b>Cash and Cash Equivalents at January 1</b>	<b>81,065</b>	<b>194,541</b>
<b>Cash and Cash Equivalents at December 31</b>	<b>\$ 194,541</b>	<b>\$ 230,729</b>
<b>Reconciliation of operating income to net cash provided by (used in) operating activities</b>		
<b>Operating income</b>	<b>\$ (461,815)</b>	<b>\$ (627,170)</b>
<b>Adjustments to reconcile operating income to net cash provided by (used in) operating activities</b>		
Depreciation expense	\$ 9,423	\$ 10,197
Loss on disposal of capital assets	13,700	646
(Increase) decrease in accounts receivable	(8,265)	15,570
Increase (decrease) in accounts payable	4,019	50
Increase (decrease) in salaries payable	5,370	4,578
Increase (decrease) in compensated absences payable - current	18,262	(5,490)
Increase (decrease) in compensated absences payable - long-term	(24,445)	15,326
Increase (decrease) in due to other governments	1,450	(1,648)
<b>Total adjustments</b>	<b>\$ 19,514</b>	<b>\$ 39,229</b>
<b>Net Cash Provided by (Used in) Operating Activities</b>	<b>\$ (442,301)</b>	<b>\$ (587,941)</b>

**Noncash capital and related financing**

Cottonwood-Jackson Community Health Services disposed of \$21,400 of capital assets with accumulated depreciation of \$7,700 in 2004 and \$2,065 of capital assets with accumulated depreciation of \$1,419 in 2005.

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**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

**NOTES TO THE FINANCIAL STATEMENTS  
AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2005**

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1. Summary of Significant Accounting Policies

Cottonwood-Jackson Community Health Services' financial statements are prepared in accordance with generally accepted accounting principles (GAAP) as of and for the years ended December 31, 2004 and 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 (FASB) issued through November 30, 1989, (when applicable) that do not conflict with or contradict GASB pronouncements. Although the Board of Health has the option to apply FASB pronouncements issued after that date, the Board has chosen not to do so. The more significant accounting policies established in GAAP and used by the Health Services are discussed below.

In June 1999, GASB unanimously approved Statement No. 34, *Basic Financial Statements--and Management's Discussion and Analysis--for State and Local Governments*. For the first time, the financial statements include a Management's Discussion and Analysis section providing an analysis of the Health Services' overall financial position and results of operations.

This and other changes are reflected in the accompanying financial statements (including the notes to the financial statements). The Health Services has elected to implement all provisions of the statement in the current year.

A. Financial Reporting Entity

Cottonwood-Jackson Community Health Services operates under Minn. Stat. ch. 145A and was established by a joint powers agreement effective January 1, 1977. The Board of Health is made up of the five elected County Commissioners from both Cottonwood and Jackson Counties.

The primary activities of the Health Services are to protect and promote the health of the general population within the counties by emphasizing the prevention of disease, injury, disability, and preventable death through the promotion of effective coordination and use of community resources, and by extending health services into the community.

**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

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1. Summary of Significant Accounting Policies (Continued)

B. Basis of Presentation

The Health Services' accounts are organized as an enterprise activity. The operations are accounted for with a set of self-balancing accounts that comprise its assets, liabilities, equities, revenues, and expenses. Enterprise activities are used to account for operations that provide a service to citizens financed primarily by charges to users of that service, and activities where the periodic measurement of net income is deemed appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

C. Measurement Focus and Basis of Accounting

The Health Services' 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. Shared revenues are generally recognized in the period the appropriation goes into effect. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

D. Budgetary Data

An annual budget is prepared on the accrual basis of accounting in accordance with generally accepted accounting principles. This budget is approved by the Health Services.

E. Assets, Liabilities, and Equity Accounts

1. Assets

Cash and Cash Equivalents

For purposes of the statement of cash flows, all cash and highly liquid investments (including restricted assets) with a maturity of three months or less when purchased are considered to be cash equivalents.

**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

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1. Summary of Significant Accounting Policies

E. Assets, Liabilities, and Equity Accounts

1. Assets (Continued)

Accounts Receivable

A summary of accounts receivable, including allowance for uncollectible accounts at December 31, 2004 and 2005, is:

	<u>2004</u>	<u>2005</u>
Gross accounts receivable	\$ 147,025	\$ 134,143
Less: allowance for uncollectibles	<u>(27,494)</u>	<u>(30,182)</u>
Net Accounts Receivable	<u>\$ 119,531</u>	<u>\$ 103,961</u>

Restricted Assets

Certain funds are classified as restricted assets because their use is limited. Included in restricted assets are funds set aside to be used for the Alice Mann Good for People Education and Scholarship Fund and interest receivable for those funds.

Capital Assets

Capital assets are recorded at cost and consist of equipment. Depreciation is provided on the straight-line basis over ten years, the estimated useful lives of the assets.

2. Liabilities

Compensated Absences

Compensated absences are considered expenses when incurred. Earned but unpaid vacation and sick leave that is vested or expected to vest are shown on the balance sheet as a long-term liability. A current portion of the liability is calculated based on a five-year trend analysis.

**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

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1. Summary of Significant Accounting Policies

E. Assets, Liabilities, and Equity Accounts (Continued)

3. Net Assets

Invested in capital assets represents the accumulated value of the capital assets of the Health Services.

Unrestricted net assets represent the accumulated earnings of the Health Services.

4. 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 end of 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.

F. Revenues and Expenses

1. Revenues

In accordance with GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, revenues for nonexchange transactions are recognized based on the principal characteristics of the revenue. Exchange transactions are recognized as revenue when the exchange occurs.

Intergovernmental

Government-mandated nonexchange transactions occur when a government at one level provides resources to a government at another level and requires that government to use them for a specific purpose. The provider government establishes purpose restrictions and also may establish time requirements. Federal and state grants mandating the Health Services perform particular programs are government-mandated nonexchange transactions. Revenues are recognized when eligibility and time requirements are met, usually when the corresponding expense is incurred.

**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

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1. Summary of Significant Accounting Policies

F. Revenues and Expenses

1. Revenues

Intergovernmental (Continued)

Voluntary nonexchange transactions result from legislative or contractual agreements, such as grants, entitlements, appropriations, and donations. The provider may establish purpose restrictions or eligibility requirements. Revenues are recognized in the year to which they apply according to the statute or contract. Other gifts and contributions from individuals are also considered voluntary nonexchange transactions and are generally recognized when received.

Exchange Transactions

Other revenues, such as charges for services and investment income, are recognized as revenue when earned.

2. Expenses

Expenses are recognized when incurred.

G. Prior Period Adjustment

In 2004, the Health Services implemented GASB Statement No. 34, *Basic Financial Statements--and Management's Discussion and Analysis--for State and Local Governments*. Also, a correction was necessary to remove amounts reported in prior years as contributed capital due to a reporting error. The restated beginning net assets amount for the enterprise fund was calculated as follows:

Fund equity - December 31, 2003	\$ 181,667
Correction of an error in reporting of contributed capital	<u>(11,155)</u>
Net Assets - January 1, 2004	<u>\$ 170,512</u>

**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

2. Stewardship, Compliance, and Accountability

Budget

Below is a summary of the budgeted and actual amounts for the years ended December 31, 2004 and 2005:

	2004		Variance Favorable (Unfavorable)
	Budget	Actual	
Operating Revenues	\$ 587,357	\$ 575,573	\$ (11,784)
Operating Expenses	1,085,256	1,037,388	47,868
Operating Income (Loss)	\$ (497,899)	\$ (461,815)	\$ 36,084
Nonoperating Revenues (Expenses)	497,899	579,460	81,561
Net Income (Loss)	<u>\$ -</u>	<u>\$ 117,645</u>	<u>\$ 117,645</u>
	2005		
	Budget	Actual	Variance Favorable (Unfavorable)
Operating Revenues	\$ 599,922	\$ 602,528	\$ 2,606
Operating Expenses	1,254,673	1,229,698	24,975
Operating Income (Loss)	\$ (654,751)	\$ (627,170)	\$ 27,581
Nonoperating Revenues (Expenses)	654,751	674,190	19,439
Net Income (Loss)	<u>\$ -</u>	<u>\$ 47,020</u>	<u>\$ 47,020</u>

**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

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3. Detailed Notes

A. Assets

Deposits and Investments

Reconciliation of the Health Services' total cash as reported in the basic financial statements to deposits, cash on hand, and investments follows:

	2004	2005
Petty cash and change funds	\$ 60	\$ 60
Savings	130,620	157,769
Certificates of deposit	45,500	45,500
Cash with fiscal agent	18,361	27,400
Total Deposits and Investments	\$ 194,541	\$ 230,729

	2004	2005
Cash and cash equivalents	\$ 137,489	\$ 172,874
Petty cash and change funds	60	60
Restricted cash	56,992	57,795
Total Cash	\$ 194,541	\$ 230,729

a. Deposits

Minn. Stat. §§ 118A.02 and 118A.04 authorize the Health Services to designate a depository for public funds and to invest in certificates of deposit. Minn. Stat. § 118A.03 requires all Health Services 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.

**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

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3. Detailed Notes

A. Assets

Deposits and Investments

a. Deposits (Continued)

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.

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a financial institution failure, the Health Services’ deposits may not be returned to it. The Health Services does not have a deposit policy for custodial credit risk. As of December 31, 2004, the Health Services’ deposits were not exposed to custodial credit risk. At December 31, 2005, \$25,439 of the Health Services’ deposits were 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 Health Services:

- (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;

**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

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3. Detailed Notes

A. Assets

Deposits and Investments

b. Investments (Continued)

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

During the years ended December 31, 2004 and 2005, the Health Services had no investments.

Due From Other Governments

The following amounts were due from other governments at December 31, 2004 and 2005:

	December 31	
	2004	2005
Grants		
Federal	\$ 14,603	\$ 9,865
State	16,770	13,186
Local	10,038	60,631
Total	\$ 41,411	\$ 83,682

**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

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3. Detailed Notes

A. Assets (Continued)

Capital Assets (Unaudited)

A summary of capital assets at December 31, 2004 and 2005, follows:

	December 31	
	2004	2005
Equipment	\$ 88,683	\$ 94,130
Less: accumulated depreciation	(34,377)	(43,155)
Total	\$ 54,306	\$ 50,975

B. Liabilities

Vacation and Sick Leave

Under the Health Services' personnel policies, employees are granted vacation leave in varying amounts based on their length of service. Vacation leave accrual varies from 5 to 20 days per year. Sick leave accrual is 12 days per year.

Unused accumulated vacation and vested sick leave are paid to employees upon termination. Unvested sick leave, approximately \$85,670 at December 31, 2004, and \$88,315 at December 31, 2005, is available to employees in the event of illness-related absences and is not paid to them at termination.

Compensated Absences

The net change in compensated absences for the years ended December 31, 2004 and 2005, are:

	2004	2005
Compensated absences - January 1	\$ 86,422	\$ 80,239
Net change	(6,183)	9,836
Compensated absences - December 31	\$ 80,239	\$ 90,075

**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

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4. Pension Plans

A. Plan Description

All full-time and certain part-time employees of Cottonwood-Jackson Community Health Services are covered by defined benefit plans administered by the Public Employees Retirement Association of Minnesota (PERA). The PERA administers the Public Employees Retirement Fund, which is a cost-sharing, multiple-employer retirement plan. The plan is 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.

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.

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 and 1.7 percent for each successive year. Using 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 Retirement Fund members whose annuity is calculated using Method 1, 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.

**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

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4. Pension Plans

A. Plan Description (Continued)

The PERA issues a publicly available financial report that includes financial statements and required supplementary information for the Public Employees Retirement Fund. That report may be obtained on the internet at [www.mnpera.org](http://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.

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 Health Services 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 were 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. The Health Services is required to contribute the following percentages of annual covered payroll:

In 2004 and 2005	
Public Employees Retirement Fund	
Basic Plan members	11.78%
Coordinated Plan members	5.53
In 2006	
Public Employees Retirement Fund	
Basic Plan members	11.78%
Coordinated Plan members	6.00

The Health Services' contributions for the years ending December 31, 2005, 2004, and 2003, were \$40,186, \$35,903, and \$36,546, respectively, equal to the contractually required contributions for each year as set by state statute.

**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

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5. Summary of Significant Contingencies and Other Items

A. Claims and Litigation

The Health Services, in connection with the normal conduct of its affairs, is involved in various claims, judgments, and litigation. The Health Services' attorney estimates that the potential claims against the Health Services that would not be covered by insurance would not materially affect the financial statements.

B. Risk Management

The Health Services is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Health Services is managing these risks with a membership in the Minnesota Counties Insurance Trust (MCIT), a public entity risk pool. The Health Services retains risk for the deductible portions of the insurance policies. The amounts of these deductibles are considered immaterial to the financial statements.

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 \$720,000, \$760,000, and \$390,000 per claim in 2004, 2005, and 2006, respectively. Should the MCIT Workers' Compensation Division liabilities exceed assets, MCIT may assess the Health Services in a method and amount to be determined by MCIT.

The Property and Casualty Division of MCIT is self-sustaining and the Health Services 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 Health Services in a method and amount to be determined by MCIT.

For health insurance, the Health Services participates in Jackson County's self-insurance program. Jackson County handles its self-insurance in its General Fund. Additional disclosures, as required by GASB Statement No. 10, *Accounting and Reporting for Risk Financing and Related Insurance Issues*, are disclosed on a County-wide basis in the Jackson County Annual Financial Report.

**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

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5. Summary of Significant Contingencies and Other Items

B. Risk Management (Continued)

The Health Services did not have a loss exceeding the limits of insurance coverage for any of the past three years. There were no significant reductions in insurance from the prior year.

C. Jointly-Governed Organizations

Cottonwood County Family Services Collaborative provides for the improvement in the social, emotional, educational, and economic outcomes of all Cottonwood County children, adolescents, and their families through activities that coordinate support and services. During 2004 and 2005, the Health Services paid \$300 per year to the Collaborative.

Jackson County Children's Mental Health and Family Services Network Collaborative promotes the improvement of the outcome of Jackson County children and their families through the utilization of existing resources by creating a more efficient and effective system of delivering services. During 2004 and 2005, the Health Services paid \$500 per year to the Collaborative.

The Minnesota Counties Computer Cooperative provides computer programming services for the Health Services. During 2004 and 2005, the Health Services purchased no services.



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**COTTONWOOD-JACKSON COMMUNITY HEALTH SERVICES  
JACKSON, MINNESOTA**

**SCHEDULE OF FINDINGS AND RECOMMENDATIONS  
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2005**

**FINDINGS AND RECOMMENDATIONS**

**A. INTERNAL CONTROL OVER FINANCIAL REPORTING**

**PREVIOUSLY REPORTED ITEMS NOT RESOLVED**

**99-1 Segregation of Duties**

Due to the limited number of office personnel at Cottonwood-Jackson Community Health Services, segregation of accounting functions necessary to ensure adequate accounting control is not possible. This is not unusual in operations the size of the Health Services; however, the Health Services' management should constantly be aware of this condition and realize that a concentration of duties and responsibilities in a limited number of individuals is not desirable from an accounting point of view.

We recommend the Health Services be aware of the lack of segregation of the accounting functions and, if possible, implement oversight procedures to ensure that the internal control policies and procedures are being implemented by staff.

**Client's Response:**

*The Board of Health is aware that it is desirable to segregate duties in the accounting department of Cottonwood-Jackson CHS. However, due to the size of the agency it is not possible to separate the accounting department to the desirable level of control nor is it financially feasible.*

**00-1 Capital Assets**

Upon a review of Cottonwood-Jackson Community Health Services' capital asset records, the following items were noted:

- The Health Services approved Jackson County's capital assets policy as its own; however, the capitalization threshold of \$5,000 appears to be too high for the type of capital assets at Cottonwood-Jackson Community Health Services. The Health Services is capitalizing assets over \$500, which does not agree with their policy.

- Detailed capital asset records are maintained, and tags are used to identify capital assets; however, this detailed record is not reconciled to the financial reporting records. The financial reporting records provide very little detail other than the total amount of capital assets purchased each year.
- Current procedures do not adequately identify and value additions and deletions.
- All equipment is depreciated over ten years. Some of the equipment capitalized, such as computer equipment, may have a much shorter useful life.

We recommend the Health Services develop and implement policies and procedures, appropriate to the entity, to strengthen internal control over capital assets. Policies and procedures should include the following to meet the requirements of generally accepted accounting principles:

- Establish a formal capitalization policy appropriate for the entity. This policy should be approved by the Health Services and cover buildings, vehicles, computers, software, and items of a certain value appropriate to the entity.
- Reconciliation of the detailed equipment records to the financial statement fixed asset records.
- Establish reasonable useful lives for capital assets.
- Establish an ongoing system for identifying purchases and dispositions of all capital assets meeting the requirements of the capitalization policy.

Client's Response:

*The Board of Health will approve an updated Capital Assets Policy at their October 26, 2006, meeting. This updated policy will define Fixed Assets as being tangible in nature in that the physical substance does not materially change its form through use, the useful life is greater than one year, and the cost is at or above \$1,000.*

*It will also define capital outlay with a dollar value of \$300 to \$999, a useful life expectancy of greater than two years, and will be included in the Capital Assets System. Cottonwood-Jackson CHS also purchases non-expendable supplies with a dollar value under \$300 and should not be included in the Capital Assets System except for: cameras, printers, desks, chairs, tables, file cabinets, and bookcases.*

*An updated inventory will be done before the next audit and will reflect the Capital Assets Policy adopted on October 26, 2006.*

B. MINNESOTA LEGAL COMPLIANCE

ITEM ARISING THIS YEAR

05-1 Collateral Pledged to Secure Deposits

Federal deposit insurance (FDIC) and collateral pledged at December 31, 2005, was insufficient for the amount on deposit at the United Prairie Bank by \$25,439.

Minn. Stat. § 118A.03 provides that, to the extent funds deposited are in excess of available federal deposit insurance, “[t]he total amount of the collateral computed at its market value shall be at least ten percent more than the amount on deposit plus accrued interest at the close of the business day.”

We recommend that the Health Services monitor the deposits in designated depositories to ensure that funds are fully protected as required by Minn. Stat. § 118A.03 at all times.

Client's Response:

*Fiscal Officer spoke with United Prairie Bank regarding this matter on September 7, 2006. The bank agreed to provide security pursuant to Minn. Stat. § 118A.03 immediately.*

C. MANAGEMENT PRACTICES

PREVIOUSLY REPORTED ITEM NOT RESOLVED

98-1 Disaster Recovery Plan

Cottonwood-Jackson Community Health Services rents time on Jackson County’s AS/400 for recording financial transactions, disbursements, and payroll. In the event of a disaster, the Health Services would rely on Jackson County’s disaster recovery plan to restore operations; however, Jackson County does not have a formal County Board-approved policy. The absence of a formal disaster recovery plan prevents the timely recovery of vital information and adds to the cost of any interruption.

We recommend Cottonwood-Jackson Community Health Services work with Jackson County to complete and approve a disaster recovery plan.

Client's Response:

*Cottonwood-Jackson CHS is working with Jackson County to develop a Disaster Recovery Plan.*

D. OTHER ITEM FOR CONSIDERATION

Governmental Accounting Standards Board Statements

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.

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

- determine if employees are provided OPEB;
- if OPEB are being provided, the Health Services 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 Health Services determines that the establishment of a trust is desirable in order to fund the OPEB, the Health Services 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 Health Services will have to decide whether to hire an actuary.

If applicable for Cottonwood-Jackson Community Health Services, GASB Statements 43 and 45 would be implemented for the years ended December 31, 2008 and 2009, respectively.

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REBECCA OTTO  
STATE AUDITOR

# STATE OF MINNESOTA

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### **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  
Cottonwood County

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Cottonwood County as of and for the year ended December 31, 2005, and have issued our report thereon dated October 17, 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 Cottonwood 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 matters involving internal control over financial reporting and its operation 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 Recommendations as items 99-1 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, we do not believe the reportable condition indicated above is a material weakness.

### Compliance and Other Matters

As part of obtaining reasonable assurance about whether Cottonwood 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, Cottonwood County complied with the material terms and conditions of applicable legal provisions, except as described in the Schedule of Findings and Recommendations as items 01-6, 02-2, and 05-2.

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/Rebecca Otto*

REBECCA OTTO  
STATE AUDITOR

*/s/Greg Hierlinger*

GREG HIERLINGER, CPA  
DEPUTY STATE AUDITOR

End of Fieldwork: October 17, 2006