

STATE OF MINNESOTA

Office of the State Auditor



Patricia Anderson
State Auditor

ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA

FOR THE YEAR ENDED DECEMBER 31, 2004

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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**ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA**

For the Year Ended December 31, 2004



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

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**ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA**

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**ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA**

ORGANIZATION
DECEMBER 31, 2004

			<u>Terms Expires</u>
Elected			
Commissioners			
Chair	Larry Larson	Lake County	January 2005
Vice Chair	Peg Sweeney	St. Louis County	January 2005
Board Member	Gordon Aanerud	Carlton County	January 2007
Board Member	Janice Hall	Cook County	January 2007
Board Member	Bill Kron	St. Louis County	January 2005
Board Member	Richard Brenner	Carlton County	January 2005
Board Member	Wade Pavleck	Koochiching County	January 2007
Board Member	Steve Raukar	St. Louis County	January 2005
Appointed			
Executive Director	Tom Roy		Indefinite

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STATE OF MINNESOTA

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PATRICIA ANDERSON
STATE AUDITOR

INDEPENDENT AUDITOR'S REPORT

Arrowhead Regional Corrections
Duluth, Minnesota

We have audited the accompanying financial statements of the governmental activities and the General Fund of Arrowhead Regional Corrections as of and for the year ended December 31, 2004, which collectively comprise Arrowhead Regional Corrections' basic financial statements as listed in the table of contents. These financial statements are the responsibility of Arrowhead Regional Corrections' 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 financial position of the governmental activities and the General Fund of Arrowhead Regional Corrections as of December 31, 2004, 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.

The Management's Discussion and Analysis and the required supplementary information 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 methods of measurement and presentation of the required supplemental 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 Arrowhead Regional Corrections' basic financial statements. The supplementary information listed in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements of Arrowhead Regional Corrections. 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 our report dated September 2, 2005, on our consideration of Arrowhead Regional Corrections' 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: September 2, 2005

MANAGEMENT'S DISCUSSION AND ANALYSIS

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**ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA**

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

Our Management's Discussion and Analysis (MD&A) of Arrowhead Regional Corrections financial performance provides an overview of the financial activities for the fiscal year ended December 31, 2004. Please read it in conjunction with the accompanying basic financial statements.

FINANCIAL HIGHLIGHTS

The total net assets of Arrowhead Regional Corrections increased by \$.3 million or 4.5 percent.

The Arrowhead Regional Corrections General Fund reported an ending fund balance of \$3.5 million, an increase of \$.4 million. Part of the fund balance, \$1.6 million, is reserved and not available for appropriation. Of the remaining \$1.9 million (unreserved fund balance), \$1.4 million has been designated for specific uses and \$.5 million remains undesignated.

The General Fund reported an excess of revenue over expenditures of \$.4 million.

OVERVIEW OF THE FINANCIAL STATEMENTS

This MD&A is intended to serve as an introduction to Arrowhead Regional Corrections basic financial statements. The basic financial statements comprise three components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the financial statements. This report contains other supporting schedules in addition to the basic financial statements.

Government-wide financial statements: The Statement of Net Assets and the Statement of Activities report information about Arrowhead Regional Corrections as a whole and about its 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 current year revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report Arrowhead Regional Corrections' net assets and changes to them. Net assets--the difference between assets and liabilities--is one way to measure Arrowhead Regional Corrections' financial health, or financial position. Over time, increases or decreases in Arrowhead Regional Corrections' net assets are one indicator of whether its financial health is

improving or deteriorating. You will need to consider other non-financial factors, such as the condition of buildings and structures, to assess the overall health of Arrowhead Regional Corrections. The government-wide financial statements can be found on Exhibits 1 and 2.

Fund financial statements: These statements provide detailed information about the General Fund, not Arrowhead Regional Corrections as a whole. The Arrowhead Regional Corrections' General Fund is considered a governmental fund.

All of Arrowhead Regional Corrections' services are reported in the General Fund, which focuses on how money flows into and out of the fund and any balance left at year-end is available for spending. This fund is reported using the modified accrual method of accounting, which measures cash and all other financial assets that can be readily converted to cash. The General Fund statements provide a detailed short-term view of Arrowhead Regional Corrections' operations and the basic services it provides. General Fund information helps determine whether there are more or fewer financial resources that can be spent in the near future to finance Arrowhead Regional Corrections programs. We describe the relationship (or differences) between governmental activities (reported in the Statement of Net Assets and the Statement of Activities) and the General Fund in a reconciliation following each of the fund financial statements. The basic financial statements for the General Fund can be found on Exhibits 3 through 6.

Notes to the financial statements: The notes provide additional information essential to a full understanding of the data provided in the government-wide and fund financial statements.

Supporting schedules: The budgetary comparison schedule, notes to required supplementary data, and schedule of intergovernmental data are provided on Schedules 1 and 2.

Government-Wide Financial Analysis

Net assets may, over time be a useful indicator of a government's financial position. In the case of Arrowhead Regional Corrections, assets exceeded liabilities by \$6.7 million.

By far the largest portion of Arrowhead Regional Corrections' net assets is the investment in capital assets. Because Arrowhead Regional Corrections uses these capital assets to provide services to participants, they are not available for future spending.

Table 1
Arrowhead Regional Corrections
Net Assets
(in Millions)

	Governmental Activities	
	2004	2003
Current and other assets	\$ 4.1	\$ 3.9
Capital assets	6.6	6.7
Total Assets	\$ 10.7	\$ 10.6
Other liabilities	\$ 0.5	\$ 0.8
Long-term liabilities outstanding	3.5	3.4
Total Liabilities	\$ 4.0	\$ 4.2
Net Assets:		
Invested in capital assets	\$ 6.6	\$ 6.7
Unrestricted	0.1	(0.3)
Total Net Assets	\$ 6.7	\$ 6.4

The following analysis focuses on Arrowhead Regional Corrections net assets (Table 1).

Governmental Activities

Arrowhead Regional Corrections' net assets increased by \$0.3 million, or 4.5 percent, from \$6.4 million to \$6.7 million. Arrowhead Regional Corrections is able to report positive balances in both categories of net assets for 2004 because current and other assets exceed total liabilities.

Current and other assets are primarily cash and pooled investments (76.6 percent or \$3.1 million).

The long-term liabilities outstanding are 100 percent compensated absences. Other liabilities decreased \$0.3 million due to a reduction in salaries payable. Other liabilities and long-term liabilities are detailed on the general fund balance sheet under liabilities.

A detailed analysis of capital assets is presented in Table 3, under the heading Capital Assets and Debt Administration.

Table 2
Arrowhead Regional Corrections
Changes in Net Assets
(in Millions)

	Governmental Activities	
	2004	2003
Revenues		
Program Revenues	\$ 0.6	\$ 0.5
Charges for services	2.3	2.6
Operating grants and contributions		
General Revenues		
Community corrections act subsidy	3.8	3.9
Grant and contributions not restricted to specific programs	10.2	10.9
Miscellaneous	0.3	0.2
Total Revenues	<u>\$ 17.2</u>	<u>\$ 18.1</u>
Expenses		
Program expenses		
Administration	\$ 1.4	\$ 1.6
Court and field services	7.9	8.1
Northeast Regional Corrections Center	4.5	4.4
Arrowhead Juvenile Center	3.1	3.1
Total Expenses	<u>\$ 16.9</u>	<u>\$ 17.2</u>
Increase (Decrease) in Net Assets	\$ 0.3	\$ 0.9
Net Assets, January 1	<u>6.4</u>	<u>5.5</u>
Net Assets, December 31	<u><u>\$ 6.7</u></u>	<u><u>\$ 6.4</u></u>

The following analysis focuses on the Arrowhead Regional Corrections' changes in net assets (Table 2).

Governmental Activities

Total revenues were \$0.9 million less in 2004 than in 2003, a reduction of 4.7 percent.

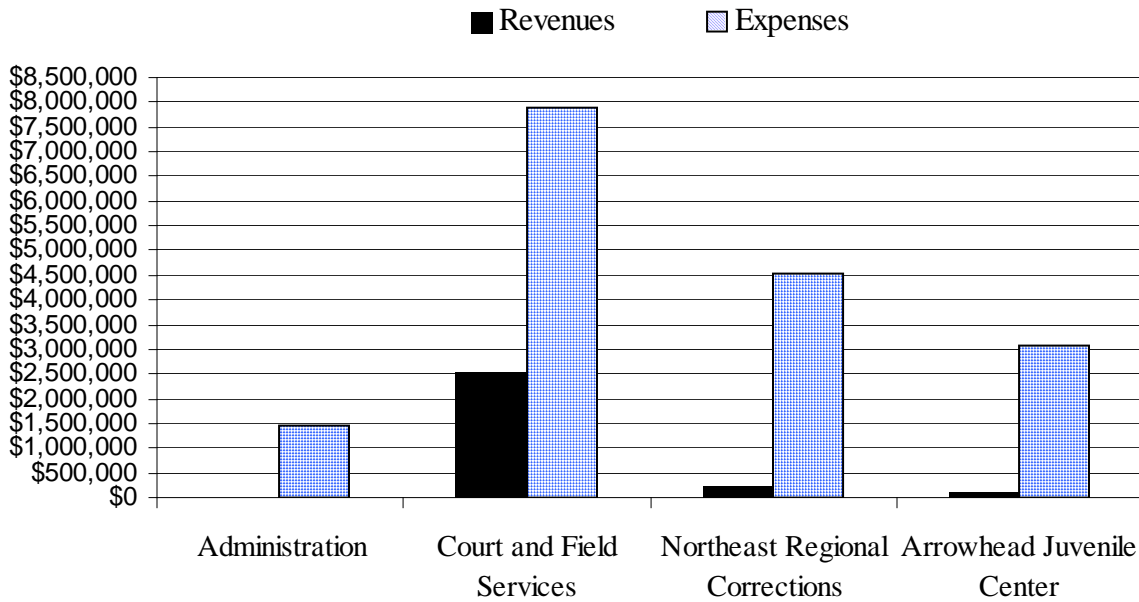
Operating grants and contributions were from state and federal grants. Federal operating grants of \$0.4 million were received during 2004, the same as 2003. State operating grants declined \$0.4 million in 2004.

Arrowhead Regional Corrections received \$10.2 million in grants and contributions not restricted to specific programs. That was a \$0.7 million reduction from 2003. The five member counties contributed \$10.1 million in 2004 compared to \$10.8 million in 2003.

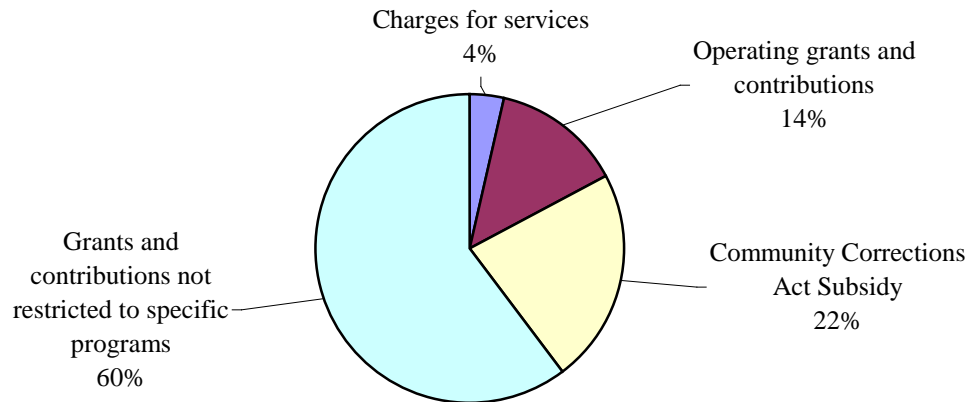
Total expenses declined in 2004 by \$0.3 million.

Court and field services accounted for 46.7 percent of all Arrowhead Regional Corrections program expenses for 2004.

Expenses & Program Revenues: Governmental Activities



Revenues by Source: Governmental Activities



Financial Analysis of the General Fund

As noted earlier, Arrowhead Regional Corrections uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

General Fund. The focus of Arrowhead Regional Corrections' General Fund is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing Arrowhead Regional Corrections' financing requirements. In particular, unreserved fund balance may serve as a useful measure of Arrowhead Regional Corrections' net resources available for spending at the end of the fiscal year.

As of December 31, 2004, Arrowhead Regional Corrections' General Fund reported a fund balance of \$3.5 million, compared with \$3.1 million in 2003. Most of the combined fund balance, or \$1.9 million, was unreserved fund balance, which is available for spending at Arrowhead Regional Corrections' discretion. Of the \$1.9 million unreserved fund balance, \$1.4 million was designated. Designations reflect Arrowhead Regional Corrections' self-imposed limitations on otherwise available expendable resources. Designated for compensated absences of \$1.0 million is the largest designation. The remaining \$1.6 million is reserved. Fund balance is reserved because it is either unavailable for spending or legally restricted. Reserved for juvenile probation of \$1.2 million is the largest reserved fund balance.

Arrowhead Regional Corrections' fund balance increased \$.4 million as a result of revenues exceeding expenditures.

General Fund Budgetary Highlights

In 2003, Arrowhead Regional Corrections laid off nineteen employees and had to cut programs, and reduce and eliminate outside contracts for services. The effects of those layoffs, cuts, and reductions continued in 2004.

Through an increase in funding from specific counties, a few employees were recalled from layoff to positions they held prior to the layoffs.

A couple of new grant sources for programming were pursued and awarded. However, minimal legislative support for increased funding was received. A federal Drug Court grant was received and has been very effective with offenders with drug addiction.

Arrowhead Regional Corrections is a regional organization providing services to five counties in Northeastern Minnesota. Funding is provided through the Minnesota Department of Corrections through the Community Corrections Act Subsidy, Carlton County, Cook County, Koochiching County, St. Louis County, and a number of federal and state grants.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At year-end, the County showed total capital assets of \$6.6 million. These amounts represent a broad range of capital assets, including land, buildings, machinery, and vehicles. Detail is presented immediately below in Table 3.

Table 3
Capital Assets at Year-End
(Net of Depreciation, in Millions)

	Governmental Activities	
	2004	2003
Land	\$ 0.5	\$ 0.5
Buildings and improvements	6.0	6.0
Vehicles	0.1	0.2
Totals	<u>\$ 6.6</u>	<u>\$ 6.7</u>

The decrease in capital assets was due to depreciation expense exceeding \$.2 million of new purchases.

Additional information on Arrowhead Regional Corrections' capital assets can be found in the notes to the financial statements.

Debt Administration

At year-end, Arrowhead Regional Corrections did not have any bonded debt.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

Arrowhead Regional Corrections continues to be both state and county budget responsive. In July 2005, we were awarded new money from the State to work with serious offenders locally. Local funding may become more of a challenge.

Total population for the five Arrowhead Regional Corrections counties, based on 2005 projections, is 267,100. St. Louis County's population continues to represent 76 percent of the total, while Cook County's population makes up 2 percent of the total. Carlton contributes 12 percent, Koochiching contributes 5 percent, and Lake contributes 4 percent of the total Arrowhead Regional Corrections population. These numbers have increased for all counties except Koochiching, from the 2000 census to the 2005 projections. The combined Arrowhead Regional Corrections population increased by 1.6 percent from 2000 to the 2005 projection, while the overall state population increased by 5.6 percent.

As an agency we suffer with other government agencies with increased health insurance costs and increased energy costs. The depressed economy will continue to impact criminal justice agencies statewide.

CONTACTING THE ARROWHEAD REGIONAL CORRECTIONS FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of finances and to show Arrowhead Regional Corrections' accountability for the money it receives. If you have a question about this report or need information, contact the Arrowhead Regional Corrections Office at: 100 N. 5th Avenue West, Duluth, Minnesota 55802-1293.

BASIC FINANCIAL STATEMENTS

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GOVERNMENT-WIDE FINANCIAL STATEMENTS

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**ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA**

EXHIBIT 1

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

	<u>Governmental Activities</u>
<u>Assets</u>	
Cash and pooled investments	\$ 3,089,946
Receivables - net	810,319
Inventories	133,004
Capital assets	
Non-depreciable capital assets	454,123
Depreciable capital assets - net of accumulated depreciation	<u>6,166,634</u>
Total Assets	<u>\$ 10,654,026</u>
<u>Liabilities</u>	
Accounts payable and other current liabilities	\$ 443,783
Unearned revenue	37,984
Long-term liabilities	
Due in more than one year	<u>3,480,235</u>
Total Liabilities	<u>\$ 3,962,002</u>
<u>Net Assets</u>	
Invested in capital assets	\$ 6,620,757
Unrestricted	<u>71,267</u>
Total Net Assets	<u>\$ 6,692,024</u>

**ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA**

EXHIBIT 2

**STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2004**

	Program Revenues			
Expenses	Fees, Charges, Fines and Other	Operating Grants and Contributions	Net (Expense) Revenue and Change in Net Assets	
<u>Functions/Programs</u>				
Governmental activities				
Administration	\$ 1,442,231	\$ -	\$ -	\$ (1,442,231)
Court and field services	7,899,037	618,767	1,945,581	(5,334,689)
Northeast Regional Corrections Center	4,529,079	-	249,178	(4,279,901)
Arrowhead Juvenile Center	3,061,323	50,956	80,353	(2,930,014)
Interest	43	-	-	(43)
Total governmental activities	\$ 16,931,713	\$ 669,723	\$ 2,275,112	\$ (13,986,878)
 General Revenues				
Community Corrections Act Subsidy				\$ 3,781,675
Grants and contributions not restricted to specific programs				10,182,089
Miscellaneous				312,909
Total general revenues				\$ 14,276,673
Change in net assets				\$ 289,795
Net Assets - beginning				6,402,229
Net Assets - ending				\$ 6,692,024

FUND FINANCIAL STATEMENTS

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GOVERNMENTAL FUND

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**ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA**

EXHIBIT 3

**BALANCE SHEET
GENERAL FUND
DECEMBER 31, 2004**

Assets

Cash and pooled investments	\$	3,072,239
Petty cash and change funds		17,707
Accounts receivable		12,617
Due from other governments		797,702
Inventories		133,004
		133,004
Total Assets	\$	4,033,269

Liabilities and Fund Balance

Liabilities

Accounts payable	\$	212,014
Salaries payable		204,023
Contracts payable		8,881
Due to other governments		18,865
Deferred revenue - unavailable		29,945
Deferred revenue - unearned		37,984
		37,984
Total Liabilities	\$	511,712

Fund Balance

Reserved for		
Inventories	\$	133,004
Health and welfare		209,703
Juvenile probation		1,224,483
Unreserved		
Designated for cash flow		400,000
Designated for petty cash funds		17,707
Designated for compensated absences		1,000,903
Undesignated		535,757
		535,757
Total Fund Balance	\$	3,521,557

Total Liabilities and Fund Balance	\$	4,033,269
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**ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA**

EXHIBIT 4

**RECONCILIATION OF GENERAL FUND BALANCE SHEET TO
THE GOVERNMENT-WIDE STATEMENT OF NET ASSETS--GOVERNMENTAL ACTIVITIES
DECEMBER 31, 2004**

Fund balance - total general fund (Exhibit 3)	\$ 3,521,557
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 fund.	6,620,757
Other long-term assets are not available to pay for current-period expenditures and, therefore, are deferred in the fund.	29,945
Long-term liabilities are not due and payable in the current period and, therefore, are not reported in the fund. Compensated absences	<u>(3,480,235)</u>
Net assets of governmental activities (Exhibit 1)	<u>\$ 6,692,024</u>

**ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA**

EXHIBIT 5

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2004**

Revenues	
Intergovernmental	\$ 16,229,200
Charges for services	669,723
Miscellaneous	312,909
	17,211,832
Total Revenues	\$ 17,211,832
Expenditures	
Current	
Administration	\$ 1,416,393
Court and field services	7,862,175
Northeast Regional Corrections Center	4,380,255
Arrowhead Juvenile Center	2,966,760
Capital outlay	190,566
Debt service	
Principal retirement	8,823
Interest	94
	16,825,066
Total Expenditures	\$ 16,825,066
Excess of Revenues Over (Under) Expenditures	\$ 386,766
Fund Balance - January 1	3,137,328
Increase (decrease) i n reserved for inventories	(2,537)
	3,134,791
Fund Balance - December 31	\$ 3,134,791

**ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA**

EXHIBIT 6

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND
CHANGES IN FUND BALANCE OF THE GENERAL FUND TO THE
GOVERNMENT-WIDE STATEMENT OF ACTIVITIES--GOVERNMENTAL ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2004**

Net change in fund balance - general fund (Exhibit 5) \$ 386,766

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

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

Deferred revenue - December 31	\$ 29,945	
Deferred revenue - January 1	(22,830)	7,115

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.

Expenditures for general capital assets	\$ 190,566	
Current year depreciation	(238,290)	(47,724)

Repayment of debt principal is an expenditure in the general fund, but the repayment reduces long-term liabilities in the statement of net assets.

Principal repayments		
Capital lease		8,823

Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in the general fund.

Change in compensated absences	\$ (62,699)	
Change in inventories	(2,537)	
Change in accrued interest payable	51	(65,185)

Change in net assets of governmental activities (Exhibit 2) \$ 289,795

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

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

1. Summary of Significant Accounting Policies

The County's financial statements are prepared in accordance with generally accepted accounting principles (GAAP) for the year ended December 31, 2004. 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 County has the option to apply FASB pronouncements issued after that date to its business-type activities and enterprise funds, the County has chosen not to do so. The more significant accounting policies established in GAAP and used by the County are discussed below.

A. Financial Reporting Entity

Otter Tail County was established March 18, 1858, and is an organized county having the powers, duties, and privileges granted counties by Minn. Stat. ch. 373. 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.

Joint Ventures

The County participates in several joint ventures which are described in Note 8.B. The County also participates in jointly-governed organizations which are described in Note 8.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. 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, which normally are

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

1. Summary of Significant Accounting Policies

B. Basic Financial Statements

1. Government-Wide Statements (Continued)

supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges to external parties for support.

In the government-wide statement of net assets, both the governmental and business-type activities columns: (a) are presented on a consolidated basis by column; and (b) are 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, net of related debt; (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 and different business-type activity are offset by program revenues. Direct expenses are those that are 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 that are restricted to meeting the operational or capital requirements of a particular function or activity. Revenues that are 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. Separate statements for each fund category--governmental, proprietary, and fiduciary--are presented. The emphasis of governmental and proprietary fund financial statements is on major individual governmental and enterprise funds, with each displayed as separate columns in the fund financial statements. All remaining governmental funds are aggregated and reported as nonmajor funds.

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

1. Summary of Significant Accounting Policies

B. Basic Financial Statements

2. Fund Financial Statements (Continued)

Proprietary fund operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as subsidies and investment earnings, result from nonexchange transactions or incidental activities.

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

The Capital Improvement Special Revenue Fund is used to finance equipment acquisition or repair of buildings and other capital improvements. Financing will be provided by a tax levy and appropriations from other County funds.

The County reports the following major enterprise fund:

The Waste Management Enterprise Fund is used to account for the financial activities relating to the operation of waste disposal sites owned by Otter Tail County.

Additionally, the County reports the following fund types:

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.

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

1. Summary of Significant Accounting Policies (Continued)

C. Measurement Focus and Basis of Accounting

The government-wide, proprietary fund, and fiduciary fund 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. 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.

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. Otter Tail County considers all revenues to be available if they are collected within 60 days after the end of the current period. Property and other taxes, licenses, and interest are all considered to be susceptible to accrual. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, compensated absences, and claims and judgments, which are recognized as expenditures to the extent that they have matured. Proceeds of general 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, then unrestricted resources as they are needed.

D. Assets, Liabilities, and Net Assets or Equity

1. Cash and Cash Equivalents

The County has defined cash and cash equivalents to include cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition. Additionally, each fund's equity in the County's investment pool is treated as a cash equivalent because the funds can deposit or effectively withdraw cash at any time without prior notice or penalty.

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Assets or Equity (Continued)

2. 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, 2004, 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 2004 were \$430,125.

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

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Assets or Equity (Continued)

3. Receivables and Payables

Activity between funds representative of lending/borrowing arrangements outstanding at the end of the fiscal year is referred to as either “due to/from other funds” (the current portion of interfund loans) or “advances to/from other funds” (the non-current portion of interfund loans).

All other outstanding balances between funds are reported as “due to/from other funds.” Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as “internal balances.”

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

No allowance has been made for uncollectible receivables.

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 on 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.

4. 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 in proprietary funds and 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.

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Assets or Equity (Continued)

5. Restricted Assets

Certain funds of the County are classified as restricted assets on the statement of net assets because the restriction is either imposed by law through constitutional provisions or enabling legislation or imposed externally by creditors, grantors, contributors, or laws or regulations of other governments. Therefore, their use is limited by applicable laws and regulations.

6. Capital Assets

Capital assets, which include property, plant, equipment, and infrastructure assets (roads, bridges, sidewalks, and similar items), are reported in the applicable governmental or business-type activities column in the government-wide financial statements. Capital assets are defined by the government as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of one year. 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 asset's lives are not capitalized.

Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest incurred during the construction phase of capital assets of business-type activities is included as part of the capitalized value of the assets constructed. During the current period, the County did not have any capitalized interest.

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>
Land improvements	5 - 20
Buildings	40
Building improvements	Up to 30
Public domain infrastructure	20 - 100
Furniture, equipment, and vehicles	3 - 20

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Assets or Equity (Continued)

7. Compensated Absences

The liability for compensated absences reported in financial statements consists of unpaid, accumulated annual 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 and proprietary fund financial statements. A liability for these amounts is reported in the governmental funds for up to the annual accrual of vacation and vested sick leave if matured, for example, as a result of employee resignations and retirements.

8. 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.

9. Long-Term Obligations

In the government-wide financial statements, and proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using 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 other financing sources. 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.

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Assets or Equity (Continued)

10. 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.

11. 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. Prior Period Adjustment

Fund balances/net assets at January 1, 2004, were restated to correct errors in the prior year financial statements. Compensated absences are reported in the governmental fund statements to the extent they have matured as a result of employee resignations and retirements. Depreciation on the landfill was incorrectly calculated in the prior year.

In the government-wide statements, unearned federal disaster aid revenues were reported as revenue in the prior year.

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

1. Summary of Significant Accounting Policies

E. Prior Period Adjustment (Continued)

Restatements to beginning fund balance and fund net assets are as follows:

	Previously Reported December 31, 2003	Compensated Absences	Landfill Depreciation	As Restated, January 1, 2004
Fund Balance				
General Fund	\$ 9,202,976	\$ 369,537	\$ -	\$ 9,572,513
Road and Bridge Fund	1,181,992	97,141	-	1,279,133
Human Services Fund	7,948,044	326,541	-	8,274,585
Other governmental funds	5,715,409	-	-	5,715,409
Total Fund Balance	<u>\$ 24,048,421</u>	<u>\$ 793,219</u>	<u>\$ -</u>	<u>\$ 24,841,640</u>
Waste Management Fund	<u>\$ 8,763,579</u>	<u>\$ -</u>	<u>\$ (110,117)</u>	<u>\$ 8,653,462</u>

Restatements to the government-wide statements as of January 1, 2004 are as follows:

	Governmental Activities	Business-Type Activities	Total
Net Assets, previously reported	\$ 104,702,156	\$ 8,763,579	\$ 113,465,735
Landfill depreciation	-	(110,117)	(110,117)
Unearned disaster aid revenue	(358,361)	-	(358,361)
Net Assets, as restated	<u>\$ 104,343,795</u>	<u>\$ 8,653,462</u>	<u>\$ 112,997,257</u>

2. Stewardship, Compliance, and Accountability

A. Deficit Fund Equity

The following fund had a deficit fund balance as of December 31, 2004:

County Ditch Special Revenue Fund	<u>\$ 49,928</u>
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The County Ditch Fund's deficit will be eliminated with future special assessment levies against the benefited properties.

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

2. Stewardship, Compliance, and Accountability (Continued)

B. Excess of Expenditures Over Budget

The following is a summary of individual funds which had expenditures in excess of budget for the year ended December 31, 2004.

	Expenditures	Final Budget	Excess
General Fund	\$ 15,675,986	\$ 15,491,627	\$ 184,359
Special Revenue Funds			
Capital Improvement	2,484,692	2,047,413	437,279
Law Library	65,869	44,000	21,869
Debt Service Fund			
Veterans Home	176,307	143,633	32,674

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

The County's total cash and investments are reported as follows:

Cash and pooled investments	\$ 29,461,480
Change funds	30,640
Restricted assets	
Cash and pooled investments	1,017,178
Agency funds	1,032,973
Total Cash and Investments	\$ 31,542,271

Minn. Stat. §§ 118A.02 and 118A.04 authorize the County to deposit its cash and to invest in certificates of deposit in financial institutions designated by the County Treasurer. At December 31, 2004, the carrying amount of the County's deposits totaled \$14,804,649. The bank balance deposit amount was \$16,465,079. Minnesota statutes require that all County deposits be covered by insurance, surety bond, or collateral.

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments (Continued)

Following is a summary of the deposits covered by insurance or collateral at December 31, 2004.

	<u>Bank Balance</u>
Covered Deposits	
Insured, or collateralized with securities held by the County or its agent in the County's name	\$ 1,594,387
Collateralized with securities held by the pledging financial institution's agent in the County's name	<u>14,870,692</u>
Total covered deposits	\$ 16,465,079
Uncollateralized	<u>-</u>
Total	<u>\$ 16,465,079</u>

Three levels of custodial credit risk for securities are defined by generally accepted accounting principles:

- (1) securities that are insured or registered, or for which the securities are held by the County or its agent in the County's name;
- (2) securities that are uninsured and unregistered and are held by the counterparty's trust department or agent in the County's name; and
- (3) securities that are uninsured and unregistered and are held by the counterparty, or by its trust department or agent, but not in the County's name.

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments (Continued)

Following is a summary of the fair values of the County's investments, categorized into the aforementioned levels of risk, at December 31, 2004:

	Category			Fair Value
	1	2	3	
U.S. government securities	\$ 184,162	\$ -	\$ 3,234,183	\$ 3,418,345
Negotiable certificates of deposit				
Commercial paper	468,653	-	529,597	998,250
U.S. Treasury bonds	31,347	-	35,423	66,770
U.S. Treasury bills	53,616	-	941,584	995,200
U.S. Treasury notes	262,222	-	4,605,043	4,867,265
Total Investments	\$ 1,000,000	\$ -	\$ 9,345,830	\$ 10,345,830
Add				
Money market mutual funds				6,361,152
Minnesota Association of Governments Investing for Counties (MAGIC)				
Cash on hand				30,640
Deposits				14,804,649
Total Cash and Investments				\$ 31,542,271

2. Receivables

Receivables as of December 31, 2004, year-end for the County's governmental activities and business-type activities are as follows:

	Total Receivables	Amounts Not Scheduled for Collection During the Subsequent Year
Governmental Activities		
Taxes	\$ 317,334	\$ -
Special assessments	90,919	52,983
Accounts	342,988	-
Interest	60,446	-
Due from other governments	7,156,612	-
Total Governmental Activities	\$ 7,968,299	\$ 52,983

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

2. Receivables (Continued)

	Total Receivables	Amounts Not Scheduled for Collection During the Subsequent Year
Business-Type Activities		
Accounts	\$ 284,852	\$ -
Due from other governments	192,758	-
Total Business-Type Activities	\$ 477,610	\$ -

3. Capital Assets

Capital asset activity for the year ended December 31, 2004, was as follows:

Governmental Activities

	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets, not depreciated				
Land	\$ 2,075,962	\$ 173,160	\$ -	\$ 2,249,122
Construction in progress	15,631,651	5,702,066	9,008,876	12,324,841
Total capital assets not depreciated	\$ 17,707,613	\$ 5,875,226	\$ 9,008,876	\$ 14,573,963
Capital assets depreciated				
Land improvements	\$ 759,074	\$ 8,301	\$ -	\$ 767,375
Buildings	16,385,964	241,913	-	16,627,877
Building improvements	1,878,551	11,016	-	1,889,567
Machinery, furniture, and equipment	10,403,094	721,753	484,870	10,639,977
Infrastructure	78,700,504	8,593,803	-	87,294,307
Total capital assets depreciated	\$ 108,127,187	\$ 9,576,786	\$ 484,870	\$ 117,219,103

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

3. Capital Assets

Governmental Activities (Continued)

	Beginning Balance	Increase	Decrease	Ending Balance
Less: accumulated depreciation for				
Land improvements	\$ 107,473	\$ 69,934	\$ -	\$ 177,407
Buildings	4,246,268	406,036	-	4,652,304
Building improvements	201,347	47,345	-	248,692
Machinery, furniture, and equipment	6,516,713	951,871	484,870	6,983,714
Infrastructure	26,343,721	2,508,965	-	28,852,686
Total accumulated depreciation	<u>\$ 37,415,522</u>	<u>\$ 3,984,151</u>	<u>\$ 484,870</u>	<u>\$ 40,914,803</u>
Total capital assets depreciated, net	<u>\$ 70,711,665</u>	<u>\$ 5,592,635</u>	<u>\$ -</u>	<u>\$ 76,304,300</u>
Governmental Activities Capital Assets, Net	<u>\$ 88,419,278</u>	<u>\$ 11,467,861</u>	<u>\$ 9,008,876</u>	<u>\$ 90,878,263</u>

Business-Type Activities

	Beginning Balance (Restated)	Increase	Decrease	Ending Balance
Capital assets not depreciated				
Land	\$ 37,127	\$ -	\$ -	\$ 37,127
Capital assets depreciated				
Buildings	\$ 2,641,803	\$ 317,209	\$ -	\$ 2,959,012
Landfill	2,433,770	60,330	-	2,494,100
Machinery, furniture, and equipment	1,247,375	383,005	97,024	1,533,356
Total capital assets depreciated	<u>\$ 6,322,948</u>	<u>\$ 760,544</u>	<u>\$ 97,024</u>	<u>\$ 6,986,468</u>
Less: accumulated depreciation for				
Buildings	\$ 1,119,625	\$ 138,297	\$ -	\$ 1,257,922
Landfill	744,655	79,205	-	823,860
Machinery, furniture, and equipment	631,383	132,421	92,912	670,892
Total accumulated depreciation	<u>\$ 2,495,663</u>	<u>\$ 349,923</u>	<u>\$ 92,912</u>	<u>\$ 2,752,674</u>
Total capital assets depreciated, net	<u>\$ 3,827,285</u>	<u>\$ 410,621</u>	<u>\$ 4,112</u>	<u>\$ 4,233,794</u>
Business-Type Activities Capital Assets, Net	<u>\$ 3,864,412</u>	<u>\$ 410,621</u>	<u>\$ 4,112</u>	<u>\$ 4,270,921</u>

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

3. Capital Assets (Continued)

Depreciation expense was charged to functions/programs of the primary government as follows:

Governmental Activities		
General government	\$	601,086
Public safety		372,155
Highways and streets, including depreciation of infrastructure assets		2,945,732
Human services		58,006
Culture and recreation		2,681
Health		4,491
		4,491
Total Depreciation Expense - Governmental Activities	\$	3,984,151
Business-Type Activities		
Solid waste	\$	349,923

B. Interfund Receivables, Payables, and Transfers

The composition of interfund balances as of December 31, 2004, is as follows:

1. Due To/From Other Funds

Receivable Fund	Payable Fund	Amount
General	Human Services	\$ 20,420
	Ditch	12,727
	Solid Waste	117,627
Total Due to General Fund		\$ 150,774
Road and Bridge	Solid Waste	\$ 6,276
Capital Improvement	General	\$ 97,168
	Road and Bridge	3,000
Total Due to Capital Improvement Fund		\$ 100,168

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

3. Detailed Notes on All Funds

B. Interfund Receivables, Payables, and Transfers

1. Due To/From Other Funds (Continued)

Receivable Fund	Payable Fund	Amount
Other Governmental	General	\$ 1,064
	Road and Bridge	25,000
	Capital Improvement	20,422
	Other governmental funds	19,794
Total Due to Other Governmental Funds		\$ 66,280
Waste Management	General	\$ 5,398
	Road and Bridge	4
Total Due to Waste Management Fund		\$ 5,402
Agency Funds		
School Districts	Taxes and Penalties	\$ 209,898
Hospital Districts	Taxes and Penalties	2,660
Otter Tail County Sewer District	Taxes and Penalties	982
State Tax Revenue	Taxes and Penalties	86,609
Towns and Cities	Taxes and Penalties	229,371
Special Education District	Taxes and Penalties	4
Watershed Districts	Taxes and Penalties	681
Collaborative	General	173
Total Due to Agency Funds		\$ 530,378
Total Due To/From Other Funds		\$ 859,278

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

3. Detailed Notes on All Funds

B. Interfund Receivables, Payables, and Transfers (Continued)

2. Advances From/To Other Funds

Receivable Fund	Payable Fund	Amount
General	County Ditch	\$ 106,130

3. Interfund Transfers

Interfund transfers for the year ended December 31, 2004, consisted of the following:

Transfers to Capital Improvement Fund from General Fund	\$ 20,000	Provide County share of funding for E-911
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C. Liabilities

1. Payables

Payables at December 31, 2004, were as follows:

	Governmental Activities	Business-Type Activities
Accounts	\$ 869,343	\$ 123,065
Salaries	109,035	3,970
Contracts	952,718	22,000
Due to other governments	211,845	157,214
Total Payables	\$ 2,142,941	\$ 306,249

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities (Continued)

2. Deferred Revenue

Deferred revenue as of December 31, 2004, year-end for the County's governmental activities are as follows:

	Deferred Unavailable	Deferred Unearned
Governmental Activities		
Taxes	\$ 312,272	\$ -
State-aid highway allotments	4,498,845	-
Charges for services	65,220	-
Grants	697,284	48,225
Other	50,415	-
	<u>\$ 5,624,036</u>	<u>\$ 48,225</u>
Total Governmental Activities		

3. Construction Commitments

The government has active construction projects as of December 31, 2004. The projects include the following (amounts in thousands):

	Spent-to-Date	Remaining Commitment
Governmental Activities		
505 Remodeling Projects	\$ 618,825	\$ 684,677
	<u>\$ 618,825</u>	<u>\$ 684,677</u>

4. Other Postemployment Benefits

Retirees

The County provides post-retirement health care benefits for employees who retire or resign in good standing. Seventy-five percent of the employees' accumulated sick leave may be applied toward health insurance premiums. Benefits start from the date they leave the County's employment until death or the balance of their sick leave is depleted, whichever comes first. The rates are based on the County's

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities

4. Other Postemployment Benefits

Retirees (Continued)

group health policy rates. After ten years of service, employees have the option of being paid for a portion of their sick leave balance in accordance with the personnel policy instead of applying it toward health insurance.

As of year-end, the County has 13 eligible participants. The County finances the plan on a pay-as-you-go basis. During 2004, the County expended \$47,236 for these benefits.

5. Short-Term Capital Notes

In March 2004, the county issued \$465,000 General Obligation Capital Notes. The proceeds of the notes are to be used for the purchase of capital equipment. Repayment of the notes will be financed by taxes levied as part of the general property taxes of the county. The only principal payment is due on March 25, 2005.

Balance, January 1	\$ -
Additions	465,000
Reductions	<u>-</u>
Balance, December 31	<u>\$ 465,000</u>

6. Capital Leases

The County has entered into lease agreements as lessee for financing the acquisition of certain equipment. These lease agreements qualify as capital leases for accounting purposes and, therefore, have been recorded at the present value of their future minimum lease payments as of the inception date. These capital leases consist of the following at December 31, 2004:

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities

6. Capital Leases (Continued)

<u>Lease</u>	<u>Maturity</u>	<u>Installment</u>	<u>Payment Amount</u>	<u>Original</u>	<u>Balance</u>
Governmental Activities					
1995 building	2006	Monthly	\$ 4,880	\$ 500,000	\$ 105,773
2002 two patrol vehicles	2005	Yearly	9,367	34,452	9,159
2002 telephone system	2005	Monthly	570	17,300	565
2002 four radar units	2005	Monthly	299	9,181	1,170
2002 dictaphone equipment	2006	Yearly	8,273	35,193	15,469
2003 Assessor vehicle	2005	Yearly	4,018	11,427	<u>3,806</u>
Total Governmental Activities Capital Leases					<u>\$ 135,942</u>

The future minimum lease obligations and the net present value of these minimum lease payments as of December 31, 2004, were as follows:

<u>Year Ending December 31</u>	<u>Governmental Activities</u>
2005	\$ 81,985
2006	<u>61,953</u>
Total minimum lease payments	\$ 143,938
Less: amount representing interest	<u>7,996</u>
Present Value of Minimum Lease Payments	<u>\$ 135,942</u>

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities (Continued)

7. Long-Term Debt

Governmental Activities

Type of Indebtedness	Final Maturity	Installment Amounts	Interest Rates (%)	Original Issue Amount	Outstanding Balance December 31, 2004
General obligation bonds					
1996 G.O. Veterans Home Bonds	2016	\$50,000 - \$130,000	5.50 - 6.00	\$ 1,500,000	\$ 1,150,000
2004 Veterans Home Refunding Bonds	2016	\$90,000 - \$125,000	2.05 - 3.70	1,050,000	1,050,000
Total General Obligation Bonds				<u>\$ 2,550,000</u>	<u>\$ 2,200,000</u>
Revenue bonds					
2002 Government Services Building Lease HRA Revenue Bonds	2019	\$490,000 - \$930,000	4.9431	<u>\$ 9,995,000</u>	<u>\$ 9,995,000</u>

8. Debt Service Requirements

Debt service requirements at December 31, 2004, were as follows:

Governmental Activities

Year Ending December 31	General Obligation Bonds		Revenue Bonds	
	Principal	Interest	Principal	Interest
2005	\$ 70,000	\$ 86,298	\$ 490,000	\$ 443,963
2006	75,000	92,983	450,000	425,163
2007	175,000	87,747	530,000	405,563
2008	170,000	81,298	555,000	383,863
2009	180,000	74,365	580,000	360,438
2010 - 2014	1,040,000	243,538	3,260,000	1,397,914
2015 - 2019	490,000	24,308	4,130,000	534,894
Total	<u>\$ 2,200,000</u>	<u>\$ 690,537</u>	<u>\$ 9,995,000</u>	<u>\$ 3,951,798</u>

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities (Continued)

9. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2004, was as follows:

Governmental Activities

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Bonds payable					
General obligation bonds	\$ 1,215,000	\$ 1,050,000	\$ 65,000	\$ 2,200,000	\$ 70,000
Revenue bonds	9,995,000	-	-	9,995,000	490,000
Total bonds payable	\$ 11,210,000	\$ 1,050,000	\$ 65,000	\$ 12,195,000	\$ 560,000
Capital leases	224,438	-	88,496	135,942	75,853
Compensated absences	2,873,058	2,039,769	1,398,596	3,514,231	816,652
Governmental Activity Long-Term Liabilities	<u>\$ 14,307,496</u>	<u>\$ 3,089,769</u>	<u>\$ 1,552,092</u>	<u>\$ 15,845,173</u>	<u>\$ 1,452,505</u>

Business-Type Activities

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Compensated absences	\$ 172,404	\$ 113,503	\$ 63,067	\$ 222,840	\$ 55,172

4. Employee Retirement Systems and Pension Plans

A. Plan Description

All full-time and certain part-time employees of Otter Tail 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

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

4. Employee Retirement Systems and Pension Plans

A. Plan Description (Continued)

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.

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. 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.

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

4. Employee Retirement Systems and Pension Plans

A. Plan Description (Continued)

That report may be obtained on the web at 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 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. Public Employees Police and Fire Fund members are required to contribute 6.20 percent of their annual covered salary. 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:

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

The County's contributions for the years ending December 31, 2004, 2003, and 2002, 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
2004	\$ 733,288	\$ 146,049	\$ 114,758
2003	724,675	141,971	110,241
2002	670,514	138,909	100,027

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

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

5. Landfill Closure and Postclosure Care Costs

State and federal laws and regulations require the County to place a final cover on its landfill site when it stops accepting waste and to perform certain maintenance and monitoring functions at the site for 30 years after closure. Although closure and postclosure care costs will be paid only near or after the date that the landfill stops accepting waste, the Board reports a portion of these closure and postclosure care costs as an operating expense in each period based on landfill capacity used as of each balance sheet date. The \$831,741 landfill closure and postclosure care liability at December 31, 2004, represents the cumulative amount reported to date based on the use of 68 percent of the estimated capacity of the landfill. The County will recognize the remaining estimated cost of closure and postclosure care of \$193,552 as the remaining estimated capacity is filled. These amounts are based on what it would cost to perform all closure and postclosure care in 2004. The Board expects to close the landfill in 2113. Actual cost may be higher due to inflation, changes in technology, or changes in regulations.

The County is required by state and federal laws and regulations to make annual contributions to a trust to finance closure and postclosure care. The Board is in compliance with these requirements. At December 31, 2004, investments of \$1,017,178 are held for these purposes. These are reported as restricted assets on the balance sheet. Otter Tail County expects that future inflation costs will be paid from investment earnings on these annual contributions. However, if investment earnings are inadequate or additional postclosure care requirements are determined (due to changes in technology or applicable laws and regulations, for example), these costs may need to be covered by charges to future landfill users or from future tax revenue.

6. 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. The County self-insures for employee health and dental coverage. 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.

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

6. Risk Management (Continued)

The Workers' Compensation Division of the 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. The MCIT participates in the Workers' Compensation Reinsurance Association with coverage at \$720,000 and \$760,000 per claim in 2004 and 2005, respectively. Should the MCIT Workers' Compensation Division liabilities exceed assets, the MCIT may assess the County in a method and amount to be determined by the MCIT.

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

7. Conduit Debt

In 2001, the Lake Region Healthcare Corporation issued a \$6,000,000 Health Care Facilities Revenue Note, Series 2001, to finance the remodeling and equipping of the Corporation's nursing home and 108-bed hospital and the remodeling of a portion of the Corporation's nursing home for use as an inpatient rehabilitation unit. The project is deemed to be in the public interest. The note is secured by the property financed through a series of loan agreements and is payable solely from revenues of the entity. Neither the County, the state, nor any political subdivision thereof is obligated in any manner for repayment of the note. Accordingly, the note is not reported as liability in the accompanying financial statements. As of December 31, 2004, the outstanding principal amount payable was \$5,646,248.

8. Summary of Significant Contingencies and Other Items

A. Contingent Liabilities

In 2001, the city of Perham issued \$8,215,000 of general obligation bonds to finance or refinance the retrofitting and equipping of the existing municipal solid waste combustion facility. The bonds are payable primarily from the revenues derived from the project; however, if these revenues are not sufficient for the payment of the bonds, then the City shall levy and certify to the County Auditor for collection in the following year a tax at least five percent in excess of the amounts adequate to make good the deficiency. The County has entered into an agreement for waste deliveries to the

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

8. Summary of Significant Contingencies and Other Items

A. Contingent Liabilities (Continued)

Perham solid waste facility. Under this agreement, the County has agreed to make payments of its respective share of debt service payments to the City to provide for additional security for the bonds. The possibility that the County may be required to make expenditures for this debt and the amount that may be required cannot be determined at this time.

Amounts received or receivable from grant agencies are subject to audit and adjustment by grantor agencies, principally the federal government. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount, if any, of the expenditures that may be disallowed by the grantor cannot be determined at this time, although the County expects such amounts, if any, to be immaterial.

The County, in connection with the normal conduct of its affairs, is involved in various judgments, claims, and litigations; it is expected that the final settlement of these matters will not materially affect the financial statements of the county.

B. Joint Ventures

West Central Area Agency on Aging

The West Central Area Agency on Aging was established June 2, 1992, by a joint powers agreement among Becker, Clay, Douglas, Grant, Otter Tail, Pope, Stevens, Traverse, and Wilkin Counties. The agreement was established to administer all aspects of the Older Americans Act by providing programs to meet the needs of the elderly in the nine-county area. Each county may be assessed a proportional share of the 25 percent of the administrative costs incurred in the carrying out of this agreement. Each county's proportional share of this 25 percent of the administrative costs will be based upon the number of persons age 60 or older living within that county.

Any county may withdraw by providing notice to the chair of the Board 90 days prior to the beginning of the fiscal year. The chair shall forward a copy to each of the counties. Withdrawal shall not act to discharge any liability incurred or chargeable to any county before the effective date of withdrawal.

Control is vested in the West Central Board on Aging. The Board consists of one commissioner from each of the counties. The County Commissioners of the county he or she represents appoint each member of the Board.

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

8. Summary of Significant Contingencies and Other Items

B. Joint Ventures

West Central Area Agency on Aging (Continued)

Complete financial information can be obtained from:

Area Agency on Aging
P. O. Box 726
Fergus Falls, Minnesota 56537

Minnesota River Basin

The Minnesota River Basin Joint Powers Board was established July 12, 1995, by an agreement between Otter Tail County and 30 other counties. The agreement was made to promote orderly water quality improvement and management of the Minnesota River Watershed. Each county is responsible for its proportionate share of the administrative budget and for its share of benefits from any special project.

In the event of termination of the agreement, all property, real and personal, held by the Joint Powers Board shall be distributed by resolution of the policy committee to best accomplish the continuing purpose of the project.

Control is vested in an Executive Board of five officers elected from the membership of the Joint Powers Board, consisting of one representative and alternative from each county Board of Commissioners included in this agreement.

During 2004, Otter Tail County did not contribute any funds to the Joint Powers Board.

Separate financial information can be obtained from:

Minnesota River Basin Joint Powers Board
Administration Building No. 14
600 East 4th Street
Chaska, Minnesota 55318

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

8. Summary of Significant Contingencies and Other Items

B. Joint Ventures (Continued)

West Central Minnesota Drug Task Force

The West Central Minnesota Drug Task Force was established in 1996 under the authority of the Joint Powers Act, pursuant to Minn. Stat. § 471.59, and includes Becker, Clay, Douglas, Grant, Otter Tail, and Todd Counties, and the Cities of Alexandria, Breckenridge, Detroit Lakes, Fargo, Fergus Falls, Moorhead, Pelican Rapids, Perham, and Wahpeton. The Task Force's objectives are to detect, investigate, and apprehend controlled substance offenders in the six-county area.

Control of the Task Force is vested in a Board of Directors. The Board of Directors consists of department heads or a designee from each participating full-time member agency. In the event of dissolution of the Task Force, the equipment will be divided and returned to the appropriate agencies. If only one agency terminates its agreement and the unit continues, all equipment will remain with the Task Force.

Beginning January 1, 2003, fiscal agent responsibilities for the Task Force were transferred to Douglas County from Otter Tail County. Financing and equipment will be provided by the full-time and associate member agencies. Otter Tail County did not contribute any funds to this organization in 2004.

Pomme de Terre River Association

The Pomme de Terre River Association Joint Powers Board was established August 11, 1981, by an agreement between Otter Tail County and five other counties and their respective soil and water conservation districts. The agreement was made to develop and implement plans to protect property from damage of flooding, control erosion of land, protect streams and lakes from sedimentation and pollution, and maintain or improve the quality of water in the streams, lakes, and ground water lying within the boundaries of the watershed of the Pomme de Terre River. Administrative costs are apportioned equally to the soil and water conservation districts based on actual costs.

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

8. Summary of Significant Contingencies and Other Items

C. Jointly-Governed Organizations

Otter Tail County, in conjunction with other governmental entities and various private organizations, have formed the jointly-governed organizations listed below:

District IV Transportation Planning

Otter Tail County and 13 other cities and counties entered into a joint powers agreement to establish the District IV Transportation Planning Joint Powers Board, effective December 11, 1996, and empowered under Minn. Stat. § 471.59. The purpose of the Board is to develop a multi-modal transportation plan for the geographical jurisdiction of the member cities and counties. The Board is composed of 14 members, with one member appointed by each member city and county.

Otter Tail County Family Services Collaborative

The Otter Tail County Family Services Collaborative was established in 1999 under the authority of Minn. Stat. §§ 124D.23 and 245.491. The Collaborative includes the Otter Tail County Human Services Board, Court Services, Public Health, and Social Services, nine school districts within the County, and ten private agencies. The purpose of the Collaborative is to establish an integrated fund to support interventions, services, and programs for children and families in the County.

Control of the Otter Tail County Family Services Collaborative is vested in a Board of Directors comprised of one representative from each participating agency. The representatives come from the elected board of the governmental entities and from the boards of the private agencies.

Any party may withdraw from the agreement by the passage of a resolution by its governing board declaring its intent to withdraw. A party exercising its option to withdraw shall remain liable for financial obligations incurred prior to its withdrawal and shall not be entitled to a refund of contributions to the integrated fund. Upon termination of the agreement, any surplus funds will be distributed by resolution of the governing board in accordance with law in a manner to best accomplish the continuing purposes of the Collaborative.

**OTTER TAIL COUNTY
FERGUS FALLS, MINNESOTA**

8. Summary of Significant Contingencies and Other Items

C. Jointly-Governed Organizations

Otter Tail County Family Services Collaborative (Continued)

Financing is provided by state and federal grants and cash and in-kind contributions from its member parties. Otter Tail County, in an agent capacity, reports the cash transactions of the Collaborative as an agency fund on its financial statements. During 2003, the County did not contribute any funds to the Collaborative.

REQUIRED SUPPLEMENTARY INFORMATION

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**ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA**

Schedule 1

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2004**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Revenues				
Intergovernmental	\$ 15,337,216	\$ 15,687,216	\$ 16,229,200	\$ 541,984
Charges for services	1,170,741	1,170,741	669,723	(501,018)
Miscellaneous	-	-	312,909	312,909
Total Revenues	\$ 16,507,957	\$ 16,857,957	\$ 17,211,832	\$ 353,875
Expenditures				
Current				
Administration				
Administrative support services	\$ 1,619,754	\$ 1,619,754	\$ 941,814	\$ 677,940
Research and evaluation	209,176	209,176	192,092	17,084
Staff development	96,247	96,247	76,053	20,194
Work release program	-	-	(12,063)	12,063
Arrowhead Council of Churches	24,924	24,924	24,924	-
Women offenders program	165,000	165,000	136,153	28,847
Use of institutions	100,000	100,000	57,420	42,580
Total administration	\$ 2,215,101	\$ 2,215,101	\$ 1,416,393	\$ 798,708
Court and Field Services				
Probation	\$ 7,573,356	\$ 7,982,855	\$ 7,305,254	\$ 677,601
Community service program	-	-	-	-
St. Louis County data processing charges	65,811	65,811	61,884	3,927
Intensive day treatment program	-	-	162,640	(162,640)
Carlton County work crew	13,468	13,468	133	13,335
Short-term consequences	53,872	53,872	49,753	4,119
Sentence to service	186,030	186,030	213,177	(27,147)
Juvenile restitution	2,275	2,275	8,116	(5,841)
Probation fees	62,709	62,709	61,218	1,491
Total court and field services	\$ 7,957,521	\$ 8,367,020	\$ 7,862,175	\$ 504,845
Northeast Regional Corrections Center				
Administration	\$ 3,458,627	\$ 3,458,627	\$ 3,987,241	\$ (528,614)
Special education	168,135	168,135	166,491	1,644
Basic education	112,720	112,720	99,893	12,827
Vocational education	129,679	129,679	126,630	3,049
Total Northeast Regional Corrections Center	\$ 3,869,161	\$ 3,869,161	\$ 4,380,255	\$ (511,094)
Arrowhead Juvenile Center				
Administration	\$ 2,816,174	\$ 2,851,674	\$ 2,958,427	\$ (106,753)
Temporary Hold	-	-	8,333	(8,333)
Total Arrowhead Juvenile Center	\$ 2,816,174	\$ 2,851,674	\$ 2,966,760	\$ (115,086)

**ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA**

***Schedule 1
(Continued)***

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2004**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Expenditures (Continued)				
Capital Outlay				
Northeast Regional Corrections Center	\$ -	\$ -	\$ 12,950	\$ (12,950)
Arrowhead Juvenile Center	-	-	177,616	(177,616)
Total capital outlay	\$ -	\$ -	\$ 190,566	\$ (190,566)
Debt service				
Principal	\$ -	\$ -	\$ 8,823	\$ (8,823)
Interest	-	-	94	(94)
Total Expenditures	\$ 16,857,957	\$ 17,302,956	\$ 16,825,066	\$ 477,890
Excess of Revenues Over (Under) Expenditures	\$ (350,000)	\$ (444,999)	\$ 386,766	\$ 831,765
Fund Balance - January 1	3,137,328	3,137,328	3,137,328	-
Increase (decrease) in reserved for inventory	-	-	(2,537)	(2,537)
Fund Balance - December 31	\$ 2,787,328	\$ 2,692,329	\$ 3,521,557	\$ 829,228

**ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA**

**NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION
AS OF AND FOR THE YEAR ENDED DECEMBER 31, 2004**

Budgetary Data

The Arrowhead Regional Corrections Board adopts annual revenue and expenditure budgets for the General Fund on a basis consistent with generally accepted accounting principles. The budget is subject to approval by member counties and the State of Minnesota.

On or before mid-June of each year, all divisions submit requests for appropriations to the Executive Director so that a budget can be prepared. Before September 15, the proposed budget is presented to the Board for review and approval.

The appropriated budget is prepared by each division of Arrowhead Regional Corrections. Department Heads may make transfers of appropriations within a department. Transfers of appropriations between departments require Board approval. The legal level of budgetary control (the level at which expenditures may not legally exceed the budget) is at the divisional level. During the year, the Board made supplemental budgetary appropriations of \$350,000 to the Revenues and \$444,999 to the Expenditures in the General Fund.

Encumbrance accounting, under which commitments for the expenditure of monies are recorded in order to reserve that portion of the applicable appropriation, is employed as an extension of formal budgetary integration in the General Fund. Encumbrances (purchase orders, and contracts) outstanding at year-end are reported as reservations of fund balances and provide authority for the carryover of appropriations to the subsequent year in order to complete these transactions. There were no encumbrances reported at December 31, 2004.

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SUPPLEMENTARY INFORMATION

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**ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA**

Schedule 2

**SCHEDULE OF INTERGOVERNMENTAL REVENUE
FOR THE YEAR ENDED DECEMBER 31, 2004**

Shared Revenue	
State	
PERA rate reimbursement	\$ <u>44,163</u>
Member Contributions	
Shared operations	
Carlton County	\$ 896,118
Cook County	138,921
Koochiching County	177,290
Lake County	206,660
St. Louis County	8,644,074
Local contributions	<u>74,863</u>
Total shared operations	\$ <u>10,137,926</u>
Grants	
State	
Minnesota Department/Board of Education	\$ <u>221,810</u>
Minnesota Department of Corrections	
Court and field services	
Caseload/workload reductions grant	\$ 966,979
Intensive supervision grant	154,290
Sex offender grant	359,374
Felony caseload reductions grant	102,259
Remote electronic monitoring	<u>27,787</u>
Total Court and Field Services	\$ <u>1,610,689</u>
Arrowhead Juvenile Center Sex offender grant	<u>13,325</u>
Community Corrections Act Subsidy	<u>3,781,675</u>
Total Minnesota Department of Corrections	\$ <u>5,405,689</u>
Total State Grants	\$ <u>5,627,499</u>
Federal	
Department of	
Agriculture	\$ 53,353
Justice	353,263
Education	<u>12,996</u>
Total Federal Grants	\$ <u>419,612</u>
Total State and Federal Grants	\$ <u>6,047,111</u>
Total Intergovernmental Revenue	\$ <u>16,229,200</u>

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**ARROWHEAD REGIONAL CORRECTIONS
DULUTH, MINNESOTA**

Schedule 3

SCHEDULE OF FINDINGS AND RECOMMENDATIONS
FOR THE YEAR ENDED DECEMBER 31, 2004

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

INTERNAL CONTROL

PREVIOUSLY REPORTED ITEM NOT RESOLVED

96-2 Segregation of Duties

Due to the limited number of office personnel within the Arrowhead Regional Corrections, segregation of accounting functions necessary to insure adequate internal accounting control is not possible. This is not unusual in operations the size of Arrowhead Regional Corrections; however, management should constantly be aware of this condition and realize that the concentration of duties and responsibilities in a limited number of individuals is not desirable from an accounting point of view.

We recommend that Arrowhead Regional Corrections' management be aware of the lack of segregation of the accounting functions and enact oversight procedures to ensure that the internal control policies and procedures are being implemented by the staff.

Client's Response:

Arrowhead Regional Corrections' management is aware of the lack of segregation of accounting functions as a result of our limited number of office personnel. Internal control policies and procedures will continue to be followed by Corrections' staff.

II. OTHER FINDINGS AND RECOMMENDATIONS

OTHER ITEM FOR CONSIDERATION

Other Postemployment Benefits

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

Schedule 3
(Continued)

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, like what GASB Statements 25 and 27 did for governmental 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 Arrowhead Regional Corrections Board will need to address in order to comply with the statements are:

- Determine if the employees are provided OPEB.
- If OPEB are being provided, the Board will have to decide whether it will advance fund the benefits or pay for them on a pay-as-you-go basis.
- If OPEB are being provided, the Board will have to decide whether to establish a trust to fund the OPEB.
- In order to determine annual costs and liabilities that need to be recognized, the Board will have to decide whether to hire an actuary.

If applicable for Arrowhead Regional Corrections, GASB Statements 43 and 45 would be implemented for years ended December 31, 2006 and 2007, respectively.



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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**

Arrowhead Regional Corrections Board
Duluth, Minnesota

We have audited the financial statements of the governmental activities and the General Fund of Arrowhead Regional Corrections as of and for the year ended December 31, 2004, and have issued our report thereon dated September 2, 2005. 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 Arrowhead Regional Corrections' 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 a matter involving the internal control over financial reporting 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 financial reporting that, in our judgment, could adversely affect Arrowhead Regional Corrections' ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable condition is described in the accompanying Schedule of Findings and Recommendations as item 96-2.

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 believe that the reportable condition indicated above is not a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Arrowhead Regional Corrections' 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 Arrowhead Regional Corrections complied with the material terms and conditions of applicable legal provisions.

This report is intended solely for the information and use of the Arrowhead Regional Corrections Board and management 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: September 2, 2005