

STATE OF MINNESOTA

Office of the State Auditor



Rebecca Otto
State Auditor

COTTONWOOD COUNTY
WINDOM, MINNESOTA

FOR THE YEAR ENDED DECEMBER 31, 2005

Description of the Office of the State Auditor

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

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

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

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

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

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

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

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

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

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**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

Year Ended December 31, 2005



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

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**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

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**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

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**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

ORGANIZATION
2005

Office	Name	Term Expires
Commissioners		
1st District	Gary Sorenson	January 2007
2nd District	Ron Kuecker ¹	January 2009
3rd District	Chuck Severson ²	January 2007
4th District	Norm Holmen	January 2009
5th District	John Oeltjenbruns	January 2007
Officials		
Elected		
Attorney	L. Douglas Storey	January 2007
Auditor/Treasurer	Jan Johnson	January 2007
County Recorder	Mary Ann Anderson	January 2007
Sheriff	Jason Purrington	January 2007
Appointed		
Assessor	Gale Bondhus	Indefinite
Highway Engineer	Ron Gregg	Indefinite
Veterans Service Officer	Todd Dibble	Indefinite
Environmental Officer	Mike Hanson	Indefinite
Emergency Services Director	Mark Marcy	Indefinite
Family Service Director	Craig Myers	Indefinite

¹Chair 2006

²Chair 2005

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REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

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INDEPENDENT AUDITOR'S REPORT

Board of County Commissioners
Cottonwood County

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Cottonwood County as of and for the year ended December 31, 2005, which collectively comprise the County's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the County's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic 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 basic financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Cottonwood County as of December 31, 2005, and the respective changes in financial position and cash flows, where applicable, 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 budgetary comparison schedules 1 through 5 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the basic financial statements of Cottonwood County. The statement and schedules listed as supplementary information in the table of contents are presented for the purpose of additional analysis and are not a required part of the basic financial statements of Cottonwood County. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented 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 October 17, 2006, on our consideration of Cottonwood County's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, 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/Rebecca Otto

/s/Greg Hierlinger

REBECCA OTTO
STATE AUDITOR

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

End of Fieldwork: October 17, 2006

MANAGEMENT'S DISCUSSION AND ANALYSIS

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**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

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

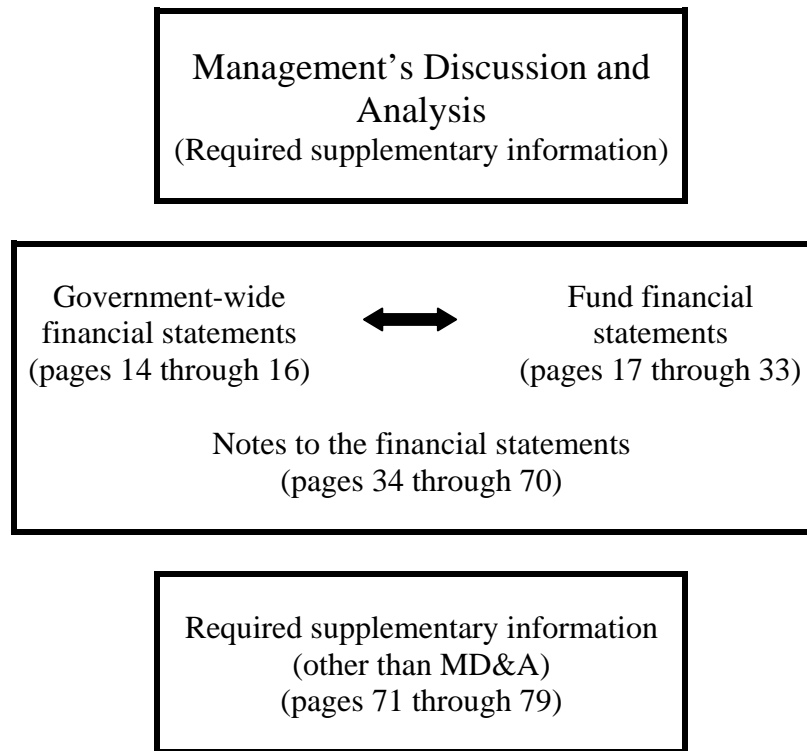
Cottonwood County's Management's Discussion and Analysis (MD&A) provides an overview of the County's financial activities for the fiscal year ended December 31, 2005. Since this information is designed to focus on the current year's activities, resulting changes, and currently known facts, it should be read in conjunction with the financial statements (beginning on page 14).

FINANCIAL HIGHLIGHTS

- Governmental activities' net assets are \$43,669,544, of which \$36,907,263 is invested in capital assets, net of related debt, and \$2,954,037 of the governmental activities net assets are restricted for specific uses.
- Business-type activities have total assets of \$2,488,156. Capital assets represent \$298,461 of business-type net assets of \$903,290.
- Cottonwood County's net assets increased by \$988,137 for the year ended December 31, 2005. Of the increase, \$1,084,726 was in the governmental activities' net assets; \$96,589 represented the decrease in business-type activities' net assets.
- The net cost of governmental activities was \$5,858,206 for the current fiscal year. The net cost was funded by general revenues and other items totaling \$7,049,869.
- Governmental funds' fund balances increased by \$717,106. This increase was due mainly to the increased collection of special assessments, intergovernmental revenue and interest on investments.

OVERVIEW OF THE FINANCIAL STATEMENTS

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



There are two government-wide financial statements. The Statement of Net Assets and the Statement of Activities (on pages 14 through 16) provide information about the activities of the County as a whole and present a longer-term view of the County's finances. Fund financial statements start on page 17. For governmental activities, these statements tell how these services were financed in the short term as well as what remains for future spending. Fund financial statements also report the County's operations in more detail than the government-wide statements by providing information about the County's most significant funds. The remaining statements provide financial information about activities for which the County acts solely as a trustee or agent for the benefit of those outside of the government.

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

Our analysis of the County as a whole begins on page 14. The Statement of Net Assets and the Statement of Activities report information about the County as a whole and about its activities in a way that helps the reader determine whether the County's financial condition has improved or declined as a result of the year's activities. These statements include all assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

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

In the Statement of Net Assets and the Statement of Activities, the County is divided into two kinds of activities:

- Governmental activities--Most of the County's basic services are reported here, including general government, public safety, highways and streets, sanitation, human services, health, culture and recreation, conservation of natural resources, and economic development. Property taxes and state and federal grants finance most of these activities.
- Business-type activities--The County charges a fee to customers to help it cover all or most of the cost of services it provides. The County's solid waste landfill activities are reported here.

Fund Financial Statements

Our analysis of the County's major funds begins on page 17. The fund financial statements provide detailed information about the significant funds--not the County as a whole. Some funds are required to be established by state law and by bond covenants. However, the County Board establishes some funds to help it control and manage money for a particular purpose or to show that it is meeting legal responsibilities for using certain taxes, grants, and other money. The County's two kinds of funds--governmental and proprietary--use different accounting methods.

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

- Proprietary funds--When the County charges customers for the services it provides--whether to outside customers or to other units of the County--these services are generally reported in proprietary funds. Proprietary funds are reported in the same way that all activities are reported in the Statement of Net Assets and the Statement of Activities. In fact, the County's enterprise fund presents the same information as the business-type activities in the government-wide statements but provides more detail and additional information, such as cash flows.

Reporting the County's Fiduciary Responsibilities

The County is the trustee, or fiduciary, over assets that can be used only for the trust beneficiaries based on the trust arrangement. All of the County's fiduciary activities are reported in separate Statements of Fiduciary Net Assets and Changes in Fiduciary Net Assets on pages 32 and 33. We exclude these activities from the County's other financial statements because the County cannot use these assets to finance its operations. The County is responsible for ensuring that the assets reported in these funds are used for their intended purposes.

THE COUNTY AS A WHOLE

The County's combined net assets are \$44,572,834. Looking at the net assets and net expenses of governmental and business-type activities separately, however, two different stories emerge. Our analysis below focuses on the net assets (Table 1) and changes in net assets (Table 2) of the County's governmental and business-type activities.

Table 1
Net Assets

	2005			2004
	Governmental Activities	Business-Type Activities	Total	
Assets				
Current and other assets	\$ 13,923,371	\$ 2,189,695	\$ 16,113,066	\$ 15,163,591
Capital assets	37,180,213	298,461	37,478,674	35,968,715
Total Assets	\$ 51,103,584	\$ 2,488,156	\$ 53,591,740	\$ 51,132,306
Liabilities				
Long-term liabilities	\$ 6,409,674	\$ 1,579,265	\$ 7,988,939	\$ 6,795,241
Other liabilities	1,024,366	5,601	1,029,967	752,368
Total Liabilities	\$ 7,434,040	\$ 1,584,866	\$ 9,018,906	\$ 7,547,609
Net Assets				
Invested in capital assets, net of related debt	\$ 36,907,263	\$ 298,461	\$ 37,205,724	\$ 35,593,715
Restricted	2,954,037	1,368,617	4,322,654	4,842,298
Unrestricted	3,808,244	(763,788)	3,044,456	3,148,684
Total Net Assets	\$ 43,669,544	\$ 903,290	\$ 44,572,834	\$ 43,584,697

Net assets of the County's governmental activities were \$43,669,544. Unrestricted net assets--the part of net assets that can be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation, or other legal requirements--was \$3,808,244 at the end of the year. The net assets of business-type activities were \$903,290.

Table 2
Changes in Net Assets
(in Thousands)

	2005			2004
	Governmental Activities	Business-Type Activities	Total	
Revenues				
Program revenues				
Fees, fines, and charges	\$ 1,138	\$ 382	\$ 1,520	\$ 1,532
Operating grants and contributions	4,125	10	4,135	4,452
Capital grants and contributions	1,778	-	1,778	2,377
General revenues				
Property taxes	4,912	88	5,000	4,699
Other taxes	7	-	7	193
Grants, gifts, and miscellaneous	2,043	-	2,043	1,603
Total Revenues	\$ 14,003	\$ 480	\$ 14,483	\$ 14,856
Expenses				
General government	\$ 1,836	\$ -	\$ 1,836	\$ 1,610
Public safety	1,715	-	1,715	1,495
Highways	3,699	-	3,699	1,736
Sanitation	208	-	208	211
Human services	4,074	-	4,074	4,051
Health	121	-	121	118
Culture and recreation	245	-	245	306
Conservation of natural resources	777	-	777	813
Economic development	18	-	18	4
Interest	206	-	206	177
Landfill	-	596	596	625
Total Expenses	\$ 12,899	\$ 596	\$ 13,495	\$ 11,146
Increase (Decrease) Before Transfers	\$ 1,104	\$ (116)	\$ 988	\$ 3,710
Transfers	(19)	19	-	-
Increase (Decrease) in Net Assets	\$ 1,085	\$ (97)	\$ 988	\$ 3,710
Net Assets - January 1	42,585	1,000	43,585	39,875
Net Assets - December 31	<u>\$ 43,670</u>	<u>\$ 903</u>	<u>\$ 44,573</u>	<u>\$ 43,585</u>

The County's activities increased net assets by 2.2 percent (\$44,572,834 for 2005 compared to \$43,584,697 for 2004).

TOTAL COUNTY REVENUE

Governmental Activities

Revenues for the County's governmental activities were \$14,002,519, while total expenses were \$12,898,332 and transfers out were \$19,461. This reflects a \$1,084,726 increase in net assets for the year ended December 31, 2005.

Business-Type Activities

Revenues of the County's business-type activities (see Table 2) were \$480,198, transfers in were \$19,461, and expenses were \$596,248. Loss of landfill fee revenue is responsible for the \$96,589 decrease in net assets for the year ending December 31, 2005.

Governmental Activities' Expenses

The cost of all governmental activities this year was \$12,898,332. However, as shown in the Statement of Activities on pages 15 and 16, the amount that our taxpayers ultimately financed for these activities through County taxes was \$5,858,206 because some of the cost was paid by those who directly benefited from the programs (\$1,137,233) or by other governments and organizations that subsidized certain programs with grants and contributions (\$5,902,893).

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

Table 3
Governmental Activities
(in Thousands)

	Total Cost of Services 2005	Net Cost of Services 2005
	<hr/>	<hr/>
Human services	\$ 4,074	\$ 1,861
Highways and streets	3,699	371
General government	1,836	1,440
Public safety	1,715	1,413
Conservation of natural resources	777	325
All others	797	448
	<hr/>	<hr/>
Totals	\$ 12,898	\$ 5,858
	<hr/>	<hr/>

THE COUNTY'S FUNDS

As the County completed the year, its governmental funds (as presented in the Balance Sheet on pages 17 through 20) reported a combined fund balance of \$9,556,888, which is above last year's total of \$8,607,913. The governmental funds change in fund balance (an increase of \$948,975 for 2005) represents an 11 percent increase in governmental fund balances. Most of the governmental funds' increase is due to increased special assessment revenue.

General Fund Budgetary Highlights

Over the course of the year, the County Board revised the County's General Fund budget several times. These budget amendments fall into two categories: new information changing original budget estimations and greater than anticipated revenues or costs.

Even with these adjustments, the actual charges to appropriations (expenditures) were \$585,804 above the final budget amounts. The reason for significant variances of actual expenditures from final budget is expenditures made from departments without budgeted expenses.

On the other hand, resources available for appropriation were also \$404,861 above the final budgeted amount. Restoration of certain state appropriations helped to offset unbudgeted expenditures.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At the end of 2005, the County had \$37,478,674 invested in a broad range of capital assets, including land, buildings, highways and streets, and equipment. (See Table 4.) This amount represents a net increase (including additions and deductions) of \$1,509,959, or 4.1 percent, over last year.

Table 4
Changes in Capital Assets During 2005

Governmental Activities

	<u>Beginning Balance</u>	<u>Increase</u>	<u>Decrease</u>	<u>Ending Balance</u>
Capital assets not depreciated				
Land	\$ 311,551	\$ -	\$ -	\$ 311,551
Right of way	697,413	-	-	697,413
Construction in progress	<u>2,084,789</u>	<u>82,095</u>	<u>977,892</u>	<u>1,188,992</u>
Total capital assets not depreciated	<u>\$ 3,093,753</u>	<u>\$ 82,095</u>	<u>\$ 977,892</u>	<u>\$ 2,197,956</u>

	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets depreciated				
Buildings	\$ 4,268,611	\$ 80,406	\$ 279,921	\$ 4,069,096
Machinery and equipment	3,890,563	701,394	238,380	4,353,577
Infrastructure	36,040,563	3,807,374	-	39,847,937
Total capital assets depreciated	<u>\$ 44,199,737</u>	<u>\$ 4,589,174</u>	<u>\$ 518,301</u>	<u>\$ 48,270,610</u>
Less: accumulated depreciation for				
Buildings	\$ 1,458,517	\$ 336,490	\$ 175,955	\$ 1,619,052
Machinery and equipment	2,135,613	928,517	238,380	2,825,750
Infrastructure	8,059,932	783,619	-	8,843,551
Total accumulated depreciation	<u>\$ 11,654,062</u>	<u>\$ 2,048,626</u>	<u>\$ 414,335</u>	<u>\$ 13,288,353</u>
Total capital assets depreciated, net	<u>\$ 32,545,675</u>	<u>\$ 2,540,548</u>	<u>\$ 103,966</u>	<u>\$ 34,982,257</u>
Governmental Activities Capital Assets, Net	<u>\$ 35,639,428</u>	<u>\$ 2,622,643</u>	<u>\$ 1,081,858</u>	<u>\$ 37,180,213</u>

Business-Type Activities

	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets not depreciated				
Land	\$ 163,882	\$ -	\$ -	\$ 163,882
Capital assets depreciated				
Buildings	\$ 23,700	\$ -	\$ -	\$ 23,700
Machinery and equipment	425,095	-	-	425,095
Total capital assets depreciated	<u>\$ 448,795</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 448,795</u>
Less: accumulated depreciation for				
Buildings	\$ 15,866	\$ 790	\$ -	\$ 16,656
Machinery and equipment	267,524	30,036	-	297,560
Total accumulated depreciation	<u>\$ 283,390</u>	<u>\$ 30,826</u>	<u>\$ -</u>	<u>\$ 314,216</u>
Total capital assets depreciated, net	<u>\$ 165,405</u>	<u>\$ (30,826)</u>	<u>\$ -</u>	<u>\$ 134,579</u>
Business-Type Activities Capital Assets, Net	<u>\$ 329,287</u>	<u>\$ (30,826)</u>	<u>\$ -</u>	<u>\$ 298,461</u>

The capital asset events this year were primarily the addition of roads and bridges (infrastructure) and the purchase of highway equipment.

The County's fiscal year 2005 capital budget called for it to spend \$1,840,000 on highway and bridge construction and \$275,000 on equipment purchases, all to be financed with resources on hand in existing County funds. For the other projects, it used resources on hand in the County's Road and Bridge Fund.

Debt

At the end of the current fiscal year, the County had total outstanding debt of \$7,988,939, versus \$6,795,241 last year--an increase of 17.6 percent--as shown in Table 5.

Table 5
Changes in Outstanding Debt During 2005

Governmental Activities

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Bonds payable (fund liquidating the debt)					
General obligation bonds (General)	\$ 375,000	\$ -	\$ 185,000	\$ 190,000	\$ 190,000
Tax increment (Debt Service)	930,000	-	545,000	385,000	190,000
Special assessment debt with government commitment (Ditch)	2,280,000	1,900,000	150,000	4,030,000	150,000
Less: unamortized discount	(1,540)	(32,300)	(2,998)	(30,842)	(2,998)
Total bonds payable	\$ 3,583,460	\$ 1,867,700	\$ 877,002	\$ 4,574,158	\$ 527,002
Loans payable	1,179,450	168,534	116,979	1,231,005	118,008
Compensated absences	477,815	43,746	-	521,561	41,620
Governmental Activities Long-Term Liabilities	<u>\$ 5,240,725</u>	<u>\$ 2,079,980</u>	<u>\$ 993,981</u>	<u>\$ 6,326,724</u>	<u>\$ 686,630</u>

Business-Type Activities

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Bonds payable					
General obligation bonds	\$ 520,000	\$ -	\$ 145,000	\$ 375,000	\$ 150,000
Less: unamortized discount	(6,079)	-	(2,356)	(3,723)	(1,241)
Total bonds payable	\$ 513,921	\$ -	\$ 142,644	\$ 371,277	\$ 148,759
Estimated liability for landfill closure and postclosure care	1,029,392	166,093	-	1,195,485	-
Compensated absences	11,203	1,300	-	12,503	-
Business-Type Activities Long-Term Liabilities	<u>\$ 1,554,516</u>	<u>\$ 167,393</u>	<u>\$ 142,644</u>	<u>\$ 1,579,265</u>	<u>\$ 148,759</u>

New debt resulted mainly from issuance of refunding bonds on existing debt.

The County's general obligation bond rating is currently an A3. This rating is assigned by national rating agencies. The state limits the amount of net debt that counties can issue to two percent of the market value of all taxable property (\$1,069,348,100) in the county. The County's outstanding net debt (\$7,988,939) is significantly below this state-imposed limit.

The County does not purchase commercial insurance for employee health and dental coverage and has claims and judgments of \$73,011 outstanding at year-end, compared with \$98,353 last year. Other obligations include accrued vacation pay and sick leave payable.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

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

- Cottonwood County is anticipating no reduction of state aids to local governments. The County will be able to maintain a stable service environment if no state reductions are implemented.
- County General Fund expenditures for 2006 are budgeted to increase 6.2 percent from 2005.
- Property taxes levied have increased 3.48 percent for 2006.

CONTACTING THE COUNTY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the County's finances and to show the County's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the County's Auditor/Treasurer, Jan Johnson, Cottonwood County Courthouse, 900 - 3rd Avenue, Windom, Minnesota 56101.

BASIC FINANCIAL STATEMENTS

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GOVERNMENT-WIDE FINANCIAL STATEMENTS

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**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

EXHIBIT 1

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

	<u>Governmental Activities</u>	<u>Business-Type Activities</u>	<u>Total</u>
<u>Assets</u>			
Cash and pooled investments	\$ 9,992,744	\$ 792,550	\$ 10,785,294
Receivables - net	3,737,493	28,528	3,766,021
Inventories	153,489	-	153,489
Prepaid items	8,221	-	8,221
Restricted assets			
Cash and pooled investments	-	1,367,482	1,367,482
Taxes receivable - prior	-	1,135	1,135
Deferred charges	31,424	-	31,424
Capital assets			
Non-depreciable capital assets	2,197,956	163,882	2,361,838
Depreciable capital assets - net of accumulated depreciation	34,982,257	134,579	35,116,836
Total Assets	\$ 51,103,584	\$ 2,488,156	\$ 53,591,740
<u>Liabilities</u>			
Accounts payable and other current liabilities	\$ 877,861	\$ 5,601	\$ 883,462
Accrued interest payable	78,838	-	78,838
Unearned revenue	67,667	-	67,667
Long-term liabilities			
Due within one year	705,684	148,759	854,443
Due in more than one year	5,703,990	1,430,506	7,134,496
Total Liabilities	\$ 7,434,040	\$ 1,584,866	\$ 9,018,906
<u>Net Assets</u>			
Invested in capital assets - net of related debt	\$ 36,907,263	\$ 298,461	\$ 37,205,724
Restricted for			
Public safety	108,073	-	108,073
Highways and streets	665,636	-	665,636
Debt service	2,141,747	2,304	2,144,051
Postclosure	-	1,366,313	1,366,313
Other purposes	38,581	-	38,581
Unrestricted	3,808,244	(763,788)	3,044,456
Total Net Assets	\$ 43,669,544	\$ 903,290	\$ 44,572,834

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

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

	Expenses	Fees, Charges, Fines, and Other
Functions/Programs		
Governmental activities		
General government	\$ 1,836,247	\$ 283,510
Public safety	1,714,960	114,089
Highways and streets	3,699,008	48,956
Sanitation	207,353	212,214
Human services	4,074,207	310,619
Health	120,871	-
Culture and recreation	244,439	31,333
Conservation of natural resources	776,688	136,512
Economic development	18,014	-
Interest	205,444	-
Administrative charges	1,101	-
	\$ 12,898,332	\$ 1,137,233
Business-type activities		
Landfill	596,248	382,416
	\$ 13,494,580	\$ 1,519,649

General Revenues

Property taxes
Mortgage registry and deed tax
Grants and contributions not restricted to specific programs
Gifts and contributions
Investment income
Miscellaneous

Transfers

Total general revenues and transfers

Change in net assets

Net Assets - Beginning

Net Assets - Ending

EXHIBIT 2

Program Revenues		Net (Expense) Revenue and Changes in Net Assets		
Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-Type Activities	Total
\$ 113,214	\$ -	\$ (1,439,523)	\$ -	\$ (1,439,523)
138,019	50,000	(1,412,852)	-	(1,412,852)
1,551,105	1,727,695	(371,252)	-	(371,252)
49,079	-	53,940	-	53,940
1,902,546	-	(1,861,042)	-	(1,861,042)
-	-	(120,871)	-	(120,871)
55,622	-	(157,484)	-	(157,484)
315,613	-	(324,563)	-	(324,563)
-	-	(18,014)	-	(18,014)
-	-	(205,444)	-	(205,444)
-	-	(1,101)	-	(1,101)
\$ 4,125,198	\$ 1,777,695	\$ (5,858,206)	\$ -	\$ (5,858,206)
10,306	-	-	(203,526)	(203,526)
\$ 4,135,504	\$ 1,777,695	\$ (5,858,206)	\$ (203,526)	\$ (6,061,732)
		\$ 4,912,415	\$ 87,476	\$ 4,999,891
		7,160	-	7,160
		1,582,688	-	1,582,688
		51,792	-	51,792
		266,383	-	266,383
		141,955	-	141,955
		(19,461)	19,461	-
		\$ 6,942,932	\$ 106,937	\$ 7,049,869
		\$ 1,084,726	\$ (96,589)	\$ 988,137
		42,584,818	999,879	43,584,697
		\$ 43,669,544	\$ 903,290	\$ 44,572,834

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FUND FINANCIAL STATEMENTS

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GOVERNMENTAL FUNDS

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

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

	General	Road and Bridge
<u>Assets</u>		
Cash and pooled investments	\$ 5,449,572	\$ 542,668
Petty cash and change funds	3,000	-
Undistributed cash in agency funds	36,100	11,215
Cash with escrow agent	-	-
Taxes receivable		
Prior	26,410	11,024
Special assessments receivable		
Prior	21,289	-
Noncurrent	905,268	-
Accounts receivable	18,739	-
Accrued interest receivable	50,520	-
Loans receivable - net	35,000	-
Due from other funds	57	2,128
Due from other governments	27,186	1,027,354
Inventories	-	153,489
Advances to other funds	54,938	-
Prepaid items	8,221	-
	\$ 6,636,300	\$ 1,747,878
Total Assets	\$ 6,636,300	\$ 1,747,878

EXHIBIT 3

Family Services	Ditch	Building	Debt Service	Total Governmental Funds
\$ 953,073	\$ 646,841	\$ 185,709	\$ 302,565	\$ 8,080,428
-	-	-	-	3,000
19,755	2,474	590	2,373	72,507
-	1,836,809	-	-	1,836,809
19,069	-	458	2,304	59,265
-	114	-	-	21,403
-	1,388,363	-	-	2,293,631
16,069	-	-	-	34,808
-	-	-	-	50,520
-	-	-	-	35,000
-	-	-	-	2,185
188,326	-	-	-	1,242,866
-	-	-	-	153,489
-	-	-	-	54,938
-	-	-	-	8,221
\$ 1,196,292	\$ 3,874,601	\$ 186,757	\$ 307,242	\$ 13,949,070

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

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

	General	Road and Bridge
<u>Liabilities and Fund Balances</u>		
Liabilities		
Accounts payable	\$ 33,149	\$ 66,273
Salaries payable	12,616	36,932
Contracts payable	-	369,159
Due to other funds	2,128	-
Due to other governments	38,796	3,557
Deferred revenue - unavailable	952,967	1,026,256
Deferred revenue - unearned	48,919	-
Advances from other funds	-	-
	\$ 1,088,575	\$ 1,502,177
Fund Balances		
Reserved for		
Encumbrances	\$ 21,899	\$ 16,901
Inventories	-	153,489
Advances to other funds	54,938	-
Sheriff's contingency	2,545	-
Debt service	-	-
Enhanced 911	105,528	-
Loans receivable - net	35,000	-
Prepaid items	8,221	-
Missing heirs	3,425	-
Law library	37,614	-
Highway allotments	-	43,871
Recorder's technology fund	21,175	-
Recorder's compliance fund	13,981	-
Canteen fund	10,134	-
Transportation	7,073	-
Cash with escrow agent	-	-
Septic/sewer loans	345,767	-
Unreserved		
Undesignated	4,880,425	31,440
	\$ 5,547,725	\$ 245,701
Total Liabilities and Fund Balances	\$ 6,636,300	\$ 1,747,878

EXHIBIT 3
(Continued)

Family Services	Ditch	Building	Debt Service	Total Governmental Funds
\$ 205,882	\$ 5,198	\$ 5,215	\$ -	\$ 315,717
14,248	-	-	-	63,796
-	418	-	-	369,577
57	-	-	-	2,185
85,850	568	-	-	128,771
19,069	1,388,477	458	2,304	3,389,531
18,748	-	-	-	67,667
-	54,938	-	-	54,938
\$ 343,854	\$ 1,449,599	\$ 5,673	\$ 2,304	\$ 4,392,182
\$ -	\$ 12,775	\$ -	\$ -	\$ 51,575
-	-	-	-	153,489
-	-	-	-	54,938
-	-	-	-	2,545
-	-	-	304,938	304,938
-	-	-	-	105,528
-	-	-	-	35,000
-	-	-	-	8,221
-	-	-	-	3,425
-	-	-	-	37,614
-	-	-	-	43,871
-	-	-	-	21,175
-	-	-	-	13,981
-	-	-	-	10,134
-	-	-	-	7,073
-	1,836,809	-	-	1,836,809
-	-	-	-	345,767
852,438	575,418	181,084	-	6,520,805
\$ 852,438	\$ 2,425,002	\$ 181,084	\$ 304,938	\$ 9,556,888
\$ 1,196,292	\$ 3,874,601	\$ 186,757	\$ 307,242	\$ 13,949,070

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**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

EXHIBIT 4

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

Fund balances - total governmental funds (Exhibit 3)	\$	9,556,888
Amounts reported for governmental activities in the statement of net assets are different because:		
Capital assets, net of accumulated depreciation, used in governmental activities are not financial resources and, therefore, are not reported in the governmental funds.		37,180,213
Other long-term assets are not available to pay for current period expenditures and, therefore, are deferred in the governmental funds.		3,389,531
Long-term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported in the governmental funds.		
General obligation bonds	\$ (4,605,000)	
Capital leases	(82,950)	
Loans payable	(1,231,005)	
Compensated absences	(521,561)	
Accrued interest payable	(78,838)	
Unamortized discount on general obligation refunding bonds	30,842	
Deferred debt issuance charges	31,424	
	(6,457,088)	
Net assets of governmental activities (Exhibit 1)	\$	<u>43,669,544</u>

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

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

	General	Road and Bridge
Revenues		
Taxes	\$ 2,374,826	\$ 839,150
Special assessments	384,639	-
Licenses and permits	8,415	-
Intergovernmental	1,853,299	3,226,287
Charges for services	297,659	29,694
Gifts and contributions	700	-
Investment earnings	234,844	-
Miscellaneous	275,129	18,573
	\$ 5,429,511	\$ 4,113,704
Expenditures		
Current		
General government	\$ 1,833,974	\$ -
Public safety	1,691,012	-
Highways and streets	-	5,012,439
Sanitation	205,455	-
Human services	-	-
Health	13,178	-
Culture and recreation	195,795	-
Conservation of natural resources	615,973	-
Economic development	18,014	-
Intergovernmental	107,693	254,034
Debt service		
Principal	661,979	-
Interest	34,486	-
Bond issuance costs	-	-
Administrative (fiscal) charges	476	-
	\$ 5,378,035	\$ 5,266,473
Excess of Revenues Over (Under) Expenditures	\$ 51,476	\$ (1,152,769)
Other Financing Sources (Uses)		
Transfers in	\$ 27,000	\$ 2,038
Transfers out	(57,374)	-
Proceeds from sale of refunding bonds	-	-
Discount on bonds issued	-	-
Proceeds from capital lease	82,950	-
Loans issued	145,140	-
	\$ 197,716	\$ 2,038
Net Change in Fund Balances	\$ 249,192	\$ (1,150,731)

EXHIBIT 5

Family Services	Ditch	Building	Debt Service	Total Governmental Funds
\$ 1,480,286	\$ -	\$ 44,225	\$ 177,504	\$ 4,915,991
-	228,297	-	-	612,936
-	-	-	-	8,415
2,080,573	-	5,153	20,524	7,185,836
32,500	-	-	-	359,853
-	-	-	-	700
-	31,539	-	-	266,383
278,119	-	73,209	-	645,030
\$ 3,871,478	\$ 259,836	\$ 122,587	\$ 198,028	\$ 13,995,144
\$ -	\$ -	\$ 42,503	\$ -	\$ 1,876,477
-	-	-	-	1,691,012
-	-	-	-	5,012,439
-	-	-	-	205,455
4,049,426	-	-	-	4,049,426
-	-	-	-	13,178
-	-	-	-	195,795
-	99,189	-	-	715,162
-	-	-	-	18,014
-	-	-	-	361,727
-	150,000	-	185,000	996,979
-	142,199	-	14,032	190,717
-	26,885	-	-	26,885
-	547	-	78	1,101
\$ 4,049,426	\$ 418,820	\$ 42,503	\$ 199,110	\$ 15,354,367
\$ (177,948)	\$ (158,984)	\$ 80,084	\$ (1,082)	\$ (1,359,223)
\$ -	\$ 3,649	\$ -	\$ 5,226	\$ 37,913
-	-	-	-	(57,374)
-	1,900,000	-	-	1,900,000
-	(32,300)	-	-	(32,300)
-	-	-	-	82,950
-	-	-	-	145,140
\$ -	\$ 1,871,349	\$ -	\$ 5,226	\$ 2,076,329
\$ (177,948)	\$ 1,712,365	\$ 80,084	\$ 4,144	\$ 717,106

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

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

	General	Road and Bridge
Fund Balances - January 1, as previously reported	\$ 5,039,916	\$ 1,423,180
Prior period adjustment (Note 1.E.)	258,617	-
Fund Balances - January 1, as restated	\$ 5,298,533	\$ 1,423,180
Increase (decrease) in reserved for inventories	\$ -	\$ (26,748)
Fund Balances - December 31	\$ 5,547,725	\$ 245,701

EXHIBIT 5
(Continued)

Family Services	Ditch	Building	Debt Service	Total Governmental Funds
\$ 1,030,386	\$ 712,637	\$ 101,000	\$ 300,794	\$ 8,607,913
-	-	-	-	258,617
\$ 1,030,386	\$ 712,637	\$ 101,000	\$ 300,794	\$ 8,866,530
\$ -	\$ -	\$ -	\$ -	\$ (26,748)
\$ 852,438	\$ 2,425,002	\$ 181,084	\$ 304,938	\$ 9,556,888

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

EXHIBIT 6

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

Net change in fund balances - total governmental funds (Exhibit 5) \$ 717,106

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

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

Deferred revenue - December 31	\$ 3,389,531	
Deferred revenue - January 1	<u>(2,461,322)</u>	928,209

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. In the statement of activities, only the gain or loss on the disposal of capital assets is reported; whereas, in the governmental funds, the proceeds from the sale increase financial resources. Therefore, the change in net assets differs from the change in fund balance by the net book value of the assets sold.

Expenditures for general capital assets	\$ 3,693,377	
Current year depreciation	(2,048,626)	
Net book value of assets disposed of	<u>(103,966)</u>	1,540,785

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

The net proceeds of new debt are		
Bonds issued	\$ (1,900,000)	
Discount on bonds issued	32,300	
Issuance costs	26,885	
Loans issued	(168,533)	
Capital lease issued	<u>(82,950)</u>	(2,092,298)

Principal repayments		
General obligation bonds	\$ 880,000	
Loans payable	<u>116,979</u>	996,979

Septic/ISTS loans previously reported in the funds as due to other governments are now reported solely in the government-wide statements.		(920,834)
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**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

**EXHIBIT 6
(Continued)**

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

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

Change in accrued interest payable	\$ (6,938)	
Amortization of discounts and deferred issuance charges	(7,789)	
Change in compensated absences	(43,746)	
Change in inventories	(26,748)	(85,221)
	<hr/>	<hr/>
Change in net assets of governmental activities (Exhibit 2)		<u>\$ 1,084,726</u>

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PROPRIETARY FUND

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**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

EXHIBIT 7

**STATEMENT OF FUND NET ASSETS
PROPRIETARY FUND
DECEMBER 31, 2005**

	<u>Landfill Enterprise Fund</u>
<u>Assets</u>	
Current assets	
Cash and pooled investments	\$ 792,550
Accounts receivable - net	28,528
Restricted assets	
Cash and pooled investments	1,366,313
Undistributed cash in agency funds	1,169
Taxes receivable	
Prior	1,135
	1,135
Total current assets	\$ 2,189,695
Noncurrent assets	
Capital assets	
Nondepreciable	\$ 163,882
Depreciable - net	134,579
	298,461
Total noncurrent assets	\$ 298,461
Total Assets	\$ 2,488,156
<u>Liabilities</u>	
Current liabilities	
Accounts payable	\$ 3,209
Salaries payable	2,392
General obligation bonds payable - current	148,759
	154,360
Total current liabilities	\$ 154,360
Noncurrent liabilities	
Compensated absences payable - long-term	\$ 12,503
Estimated liability for landfill closure/postclosure	1,195,485
General obligation bonds payable - long-term	222,518
	1,430,506
Total noncurrent liabilities	\$ 1,430,506
Total Liabilities	\$ 1,584,866
<u>Net Assets</u>	
Invested in capital assets	\$ 298,461
Restricted for postclosure	1,366,313
Restricted for debt service	2,304
Unrestricted	(763,788)
	903,290
Total Net Assets	\$ 903,290

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

EXHIBIT 8

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUND
FOR THE YEAR ENDED DECEMBER 31, 2005**

	Landfill Enterprise Fund
Operating Revenues	
Charges for services	\$ 367,044
Miscellaneous	15,372
	\$ 382,416
Operating Expenses	
Personal services	\$ 69,979
Professional services	8,493
Other services and charges	296,271
Utilities	6,014
Depreciation	30,826
Landfill closure and postclosure costs	166,093
	\$ 577,676
Operating Income (Loss)	\$ (195,260)
Nonoperating Revenues (Expenses)	
Property taxes	\$ 87,476
Intergovernmental	10,306
Interest expense	(18,572)
	\$ 79,210
Income (Loss) Before Transfers	\$ (116,050)
Transfers in	46,461
Transfers out	(27,000)
	\$ (96,589)
Change in Net Assets	\$ (96,589)
Net Assets - January 1	999,879
Net Assets - December 31	\$ 903,290

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

EXHIBIT 9

**STATEMENT OF CASH FLOWS
PROPRIETARY FUND
FOR THE YEAR ENDED DECEMBER 31, 2005
Increase (Decrease) in Cash and Cash Equivalents**

	<u>Landfill Enterprise Fund</u>
Cash Flows from Operating Activities	
Receipts from customers and users	\$ 462,564
Payments to suppliers	(326,532)
Payments to employees	(83,047)
	\$ 52,985
Cash Flows from Noncapital Financing Activities	
Property taxes	\$ 87,427
Intergovernmental	10,306
Transfers in	56,575
Transfers out	(27,000)
	\$ 127,308
Cash Flows from Capital and Related Financing Activities	
Principal paid on long-term debt	\$ (145,000)
Interest paid on long-term debt	(16,216)
	\$ (161,216)
Net Increase (Decrease) in Cash and Cash Equivalents	\$ 19,077
Cash and Cash Equivalents - January 1	2,140,955
Cash and Cash Equivalents - December 31	\$ 2,160,032
Reconciliation of Cash and Cash Equivalents to the Statement of Net Assets - Exhibit 7	
Cash and pooled investments	\$ 792,550
Restricted cash and pooled investments	1,366,313
Undistributed cash in agency funds	1,169
	\$ 2,160,032
Total Cash and Cash Equivalents - December 31	\$ 2,160,032

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

**EXHIBIT 9
(Continued)**

**STATEMENT OF CASH FLOWS
PROPRIETARY FUND
FOR THE YEAR ENDED DECEMBER 31, 2005
Increase (Decrease) in Cash and Cash Equivalents**

	<u>Landfill Enterprise Fund</u>
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities	
Operating income (loss)	\$ (195,260)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities	
Depreciation expense	\$ 30,826
(Increase) decrease in accounts receivable	80,148
Increase (decrease) in accounts payable	(15,754)
Increase (decrease) in salaries payable	(14,368)
Increase (decrease) in landfill closure costs	166,093
Increase (decrease) in compensated absences payable	1,300
Total adjustments	<u>\$ 248,245</u>
Net cash provided by (used in) operating activities	<u>\$ 52,985</u>

FIDUCIARY FUNDS

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**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

EXHIBIT 10

**STATEMENT OF FIDUCIARY NET ASSETS
FIDUCIARY FUNDS
DECEMBER 31, 2005**

	Investment Trust	Agency
<u>Assets</u>		
Cash and pooled investments	\$ 213,539	\$ 807,350
Accrued interest receivable	4,695	-
Total Assets	\$ 218,234	\$ 807,350
<u>Liabilities</u>		
Due to other governments	-	\$ 807,350
<u>Net Assets</u>		
Net assets, held in trust for pool participant	\$ 218,234	

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

EXHIBIT 11

**STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
FIDUCIARY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2005**

	<u>Investment Trust</u>
<u>Additions</u>	
Contributions from participant	\$ 247,241
Investment income	<u>4,695</u>
Total Additions	\$ 251,936
<u>Deductions</u>	
Distributions to participants	<u>230,711</u>
Change in Net Assets	\$ 21,225
Net Assets - January 1	<u>197,009</u>
Net Assets - December 31	<u>\$ 218,234</u>

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

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

1. Summary of Significant Accounting Policies

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

A. Financial Reporting Entity

Cottonwood County was established May 23, 1857, and is an organized county having the powers, duties, and privileges granted counties by Minn. Stat. ch. 373. As required by accounting principles generally accepted in the United States of America, these financial statements present Cottonwood County. 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.

The County participates in joint ventures described in Note 7.B. The County also participates in a jointly-governed organization described in Note 7.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

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

1. Summary of Significant Accounting Policies

B. Basic Financial Statements

1. Government-Wide Statements (Continued)

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

2. Fund Financial Statements

The fund financial statements provide information about the County's funds, including its fiduciary funds. 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 a separate column in the fund financial statements. The County reports all of its funds as major funds.

**COTTONWOOD COUNTY
WINDOM, 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 Family Services Special Revenue Fund is used to account for economic assistance and community social services programs.

The Ditch Special Revenue Fund is used to account for the cost of constructing and maintaining an agricultural drainage ditch system. Financing is provided by special assessments levied against benefited property.

The Building Special Revenue Fund is used to account for the cost of constructing and maintaining County buildings. Financing is provided by taxes levied and rental income.

The Debt Service Fund is used to account for the accumulation of financial resources for, and the payment of, principal, interest, and related costs of general obligation bonds.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

1. Summary of Significant Accounting Policies

B. Basic Financial Statements

2. Fund Financial Statements (Continued)

The County reports the following major enterprise fund:

The Landfill Fund is used to account for the operation, maintenance, and development of the County solid waste landfill.

Additionally, the County reports the following fund types:

The Investment Trust Fund is used to account for the external pooled and non-pooled investments held on behalf of external participants.

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

C. Measurement Focus and Basis of Accounting

The government-wide, 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. 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. Cottonwood County considers all revenues as available if collected within 60 days after the end of the current period. Property and other taxes, licenses, and interest are all considered 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.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

1. Summary of Significant Accounting Policies

C. Measurement Focus and Basis of Accounting (Continued)

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

D. Assets, Liabilities, and Net Assets or Equity

1. 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 be deposited or effectively withdrawn from cash at any time without prior notice or penalty.

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, 2005, based on market prices. Pursuant to Minn. Stat. § 385.07, investment earnings on cash and pooled investments of governmental and fiduciary funds are credited to the General Fund. Other funds received investment earnings based on other state statutes, grant agreements, contracts, and bond covenants. Pooled investment earnings for 2005 were \$233,222.

Included in total cash and pooled investments are the assets held for the Cottonwood County Family Services Collaborative in an external investment pool. For the purposes of financial reporting, the Family Services Collaborative's portion of the County's pool of cash and investments is reported as an investment trust fund. Assets in the pool are reported at fair value based on quoted market prices. The pool is not subject to regulatory oversight, and the fair value of the position in the pool is the same as the pool shares. Fair value amounts are determined at year-end. The County has not provided or obtained any legally binding guarantees to support the value of the pool.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

1. Summary of Significant Accounting Policies

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

3. Receivables and Payables

Activity between funds that is 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 noncurrent 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.

All receivables are shown net of an allowance for uncollectibles.

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

4. Special Assessments Receivable

Special assessments receivable consist of delinquent special assessments and deferred special assessments. All special assessments receivable are shown net of allowance for uncollectibles. No provision has been made for an estimated uncollectible amount.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

1. Summary of Significant Accounting Policies

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

5. 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.

6. 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.

7. 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 County as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Assets or Equity

7. Capital Assets (Continued)

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 is depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Buildings	25 - 75
Building improvements	25
Public domain infrastructure	
Bridges	75
Roads	50
Machinery and equipment	3 - 15

8. 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, proprietary, and fiduciary fund financial statements. A liability for these amounts is reported in the governmental funds only if it has matured, for example, as a result of employee resignations and retirements.

9. 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.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

1. Summary of Significant Accounting Policies

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

10. Long-Term Obligations

In the government-wide financial statements, and in the proprietary 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.

11. 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 that are subject to change.

12. 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.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

1. Summary of Significant Accounting Policies (Continued)

E. Prior Period Adjustment

Fund balance for the General Fund at January 1, 2005, has been restated. The restatement is as follows:

Fund Balance, as previously reported	\$	5,039,916
Correction of an error in the reporting of ISTS loans		258,617
Fund Balance, as Restated	\$	5,298,533

2. Stewardship, Compliance, and Accountability

Excess of Expenditures Over Budget

The following funds had expenditures in excess of budget for the year ended December 31, 2005:

Fund	Expenditures	Budget	Excess
General	\$ 5,378,035	\$ 4,792,231	\$ 585,804
Road and Bridge Special Revenue	5,266,473	4,227,047	1,039,426
Ditch Special Revenue	418,820	284,646	134,174

Deficit Fund Equity

For internal accounting purposes, individual ditch system records are maintained on a basis which shows long-term debt payable, recognizes special assessments as revenues when levied, and does not eliminate interfund transactions. Using this basis of accounting, 8 of 97 drainage systems have deficit unreserved, undesignated fund balances at December 31, 2005. Although this method results in numbers not considered to be in conformity with generally accepted accounting principles (GAAP) for reporting, it provides necessary information by ditch for internal accounting purposes. The following is a summary of fund balances using this non-GAAP basis.

Account balances	\$	550,377
Account balance deficits		(879,541)
Total	\$	(329,164)

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

2. Stewardship, Compliance, and Accountability

Deficit Fund Equity (Continued)

The Ditch Special Revenue Fund’s deficit will be eliminated with future special assessment levies against benefited properties. The County Ditch Fund had a fund balance of \$2,425,002 when reported on the modified accrual basis.

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

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

Government-wide statement of net assets	
Governmental activities	
Cash and pooled investments	\$ 9,992,744
Business-type activities	
Cash and pooled investments	792,550
Cash and pooled investments - restricted assets	1,367,482
Statement of fiduciary net assets	
Cash and pooled investments	<u>1,021,069</u>
 Total Cash and Investments	 <u>\$ 13,173,845</u>

a. Deposits

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

Authorized collateral includes treasury bills, notes and bonds; issues of U.S. government agencies; general obligations rated “A” or better, revenue obligations rated “AA” or better; irrevocable standard letters of credit issued by the Federal Home Loan Bank; and certificates of deposit. Minnesota

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

a. Deposits (Continued)

statutes require that securities pledged as collateral be held in safekeeping in a restricted account at the Federal Reserve Bank or in an account at a trust department of a commercial bank or other financial institution that is not owned or controlled by the financial institution furnishing the collateral.

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a financial institution failure, the County's deposits may not be returned to it. The County does not have a deposit policy for custodial credit risk. As of December 31, 2005, the County's deposits in banks were entirely covered by federal depository insurance or by collateral in accordance with Minnesota statutes.

b. Investments

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

- (1) securities which are direct obligations or are guaranteed or insured issues of the United States, its agencies, its instrumentalities, or organizations created by an act of Congress, except mortgage-backed securities defined as "high risk" by Minn. Stat. § 118A.04, subd. 6;
- (2) mutual funds through shares of registered investment companies provided the mutual fund receives certain ratings depending on its investments;
- (3) general obligations of the State of Minnesota and its municipalities, and in certain state agency and local obligations of Minnesota and other states provided such obligations have certain specified bond ratings by a national bond rating service;

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

b. Investments (Continued)

- (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.

Interest Rate Risk

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

At December 31, 2005, the County had the following investments:

	<u>Fair Value</u>	<u>Less Than 1 Year</u>	<u>1-2 Years</u>
Cash with escrow agent			
U.S. Treasury SLGS	\$ 1,836,809	\$ 4,496	\$ 1,832,313

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

b. Investments (Continued)

Credit Risk

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

Custodial Credit Risk

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The County does not have a policy on custodial credit risk. At December 31, 2005, \$1,836,809 of cash with escrow agent held at Northland Trust Services was subject to custodial credit risk.

Concentration of Credit Risk

The concentration of credit risk is the risk of loss that may be caused by the County's investment in a single issuer. It is the County's policy that U.S. Treasury securities, U.S. Agency securities, and obligations backed by U.S. Treasury and/or U.S. Agency securities, may be held without limit.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments (Continued)

The following table presents the County's cash and investment balances at December 31, 2005, and information relating to potential investment risks:

Investment Type	Credit Risk		Concentration Risk	Interest Rate Risk	Carrying (Fair) Value
	Credit Rating	Rating Agency	Over 5 Percent of Portfolio	Maturity Date	
Cash with escrow agent					
U.S. Treasury securities	N/A	N/A		2/1/2006	\$ 2,217
U.S. Treasury securities	N/A	N/A		8/1/2006	2,279
U.S. Treasury securities	N/A	N/A	45.5%	2/1/2007	1,832,313
Total cash with escrow agent					\$ 1,836,809
Negotiable certificates of deposit	N/A	N/A	N/A	Various	\$ 2,202,095
Total investments					\$ 4,038,904
Checking					2,734,508
Savings					3,825,433
Certificates of deposit					2,572,000
Petty cash					3,000
Total Cash and Investments					\$ 13,173,845

N/A - Not Applicable

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets (Continued)

2. Receivables

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

	Total Receivables	Amounts Not Scheduled for Collection During the Subsequent Year
Governmental Activities		
Taxes	\$ 59,265	\$ -
Special assessments	2,315,034	2,293,631
Accounts	34,808	-
Interest	50,520	-
Loans	35,000	-
Due from other governments	1,242,866	-
Total Governmental Activities	\$ 3,737,493	\$ 2,293,631
Business-Type Activities		
Taxes	\$ 1,135	\$ -
Accounts	28,528	-
Total Business-Type Activities	\$ 29,663	\$ -

Details on Loans Receivable

	Total Receivables
Loans Receivable	
Seed Capital Loan Program	
D&L Welding & Machine	\$ 16,416
Windom Economic Development	25,000
Sew Much More	1,598
Big Bend Snowriders	10,000
Total	\$ 53,014
Less: allowance for uncollectible accounts	(18,014)
Total Loans Receivable	\$ 35,000

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

2. Receivables

Details on Loans Receivable (Continued)

In 1989, Cottonwood County began a Seed Capital Loan Program with funds received from the Blandin Foundation, the Southwest Minnesota Initiative Fund, and local governments to provide low-interest, flexible-term loans for the development of new businesses or the expansion of existing ones. These loans have been made to private enterprises and are offset by deferred revenue.

In 2005, Cottonwood County made a \$10,000 interest-free loan to the Big Bend Snowriders. No schedule of repayment was established.

3. Capital Assets

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

Governmental Activities

	<u>Beginning Balance</u>	<u>Increase</u>	<u>Decrease</u>	<u>Ending Balance</u>
Capital assets not depreciated				
Land	\$ 311,551	\$ -	\$ -	\$ 311,551
Right-of-way	697,413	-	-	697,413
Construction in progress	2,084,789	82,095	977,892	1,188,992
Total capital assets not depreciated	<u>\$ 3,093,753</u>	<u>\$ 82,095</u>	<u>\$ 977,892</u>	<u>\$ 2,197,956</u>
Capital assets depreciated				
Buildings	\$ 4,268,611	\$ 80,406	\$ 279,921	\$ 4,069,096
Machinery and equipment	3,890,563	701,394	238,380	4,353,577
Infrastructure	36,040,563	3,807,374	-	39,847,937
Total capital assets depreciated	<u>\$ 44,199,737</u>	<u>\$ 4,589,174</u>	<u>\$ 518,301</u>	<u>\$ 48,270,610</u>

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

3. Capital Assets

Governmental Activities (Continued)

	<u>Beginning Balance</u>	<u>Increase</u>	<u>Decrease</u>	<u>Ending Balance</u>
Less: accumulated depreciation for				
Buildings	\$ 1,458,517	\$ 336,490	\$ 175,955	\$ 1,619,052
Machinery and equipment	2,135,613	928,517	238,380	2,825,750
Infrastructure	8,059,932	783,619	-	8,843,551
	<u>\$ 11,654,062</u>	<u>\$ 2,048,626</u>	<u>\$ 414,335</u>	<u>\$ 13,288,353</u>
Total accumulated depreciation				
	<u>\$ 11,654,062</u>	<u>\$ 2,048,626</u>	<u>\$ 414,335</u>	<u>\$ 13,288,353</u>
Total capital assets depreciated, net	<u>\$ 32,545,675</u>	<u>\$ 2,540,548</u>	<u>\$ 103,966</u>	<u>\$ 34,982,257</u>
Governmental Activities Capital Assets, Net	<u>\$ 35,639,428</u>	<u>\$ 2,622,643</u>	<u>\$ 1,081,858</u>	<u>\$ 37,180,213</u>

Business-Type Activities

	<u>Beginning Balance</u>	<u>Increase</u>	<u>Decrease</u>	<u>Ending Balance</u>
Capital assets not depreciated				
Land	\$ 163,882	\$ -	\$ -	\$ 163,882
Capital assets depreciated				
Buildings	\$ 23,700	\$ -	\$ -	\$ 23,700
Machinery and equipment	425,095	-	-	425,095
	<u>\$ 448,795</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 448,795</u>
Total capital assets depreciated				
	<u>\$ 448,795</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 448,795</u>
Less: accumulated depreciation for				
Buildings	\$ 15,866	\$ 790	\$ -	\$ 16,656
Machinery and equipment	267,524	30,036	-	297,560
	<u>\$ 283,390</u>	<u>\$ 30,826</u>	<u>\$ -</u>	<u>\$ 314,216</u>
Total accumulated depreciation				
	<u>\$ 283,390</u>	<u>\$ 30,826</u>	<u>\$ -</u>	<u>\$ 314,216</u>
Total capital assets depreciated, net	<u>\$ 165,405</u>	<u>\$ (30,826)</u>	<u>\$ -</u>	<u>\$ 134,579</u>
Business-Type Activities Capital Assets, Net	<u>\$ 329,287</u>	<u>\$ (30,826)</u>	<u>\$ -</u>	<u>\$ 298,461</u>

**COTTONWOOD COUNTY
WINDOM, 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	\$	193,668
Public safety		58,826
Highways and streets, including depreciation of infrastructure assets		1,669,392
Family services		12,439
Culture and recreation		76,501
Conservation of natural resources		33,635
Sanitation		4,165
Total Depreciation Expense - Governmental Activities	\$	2,048,626
Business-Type Activities		
Landfill	\$	30,826

B. Interfund Receivables, Payables, and Transfers

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

1. Due To/From Other Funds

Receivable Fund	Payable Fund	Amount
General	Family Services	\$ 57
Road and Bridge	General	2,128
Total Due To/From Other Funds		\$ 2,185

The outstanding balances between funds result from the time lag between the dates the interfund goods and services were provided and reimbursable expenditures occurred, and when transactions are recorded in the accounting system and when the funds are repaid. All balances are expected to be liquidated in the subsequent year.

**COTTONWOOD COUNTY
WINDOM, 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	Ditch	\$ 54,938

The advance is to provide working capital to a ditch system with low reserves and current operating costs in excess of its revenues. This balance will be paid from future ditch special assessments.

3. Interfund Transfers

Interfund transfers for the year ended December 31, 2005, consisted of the following:

Transfers to General Fund from Landfill Fund	\$ 27,000	Provide funds for recycling
Transfer to Road and Bridge Fund from General Fund	2,038	Provide funding
Transfer to Ditch Fund from General Fund	3,649	Provide funding
Transfer to Debt Service Fund from General Fund	5,226	Provide funding
Transfers to Landfill Fund from General Fund	46,461	Provide funding
Total Interfund Transfers	\$ 84,374	

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

3. Detailed Notes on All Funds (Continued)

C. Liabilities

1. Payables

Payables at December 31, 2005, were as follows:

	Governmental Activities	Business-Type Activities
Accounts	\$ 315,717	\$ 3,209
Salaries	63,796	2,392
Contracts	369,577	-
Due to other governments	128,771	-
Total Payables	\$ 877,861	\$ 5,601

2. Construction Commitments

The government has active construction projects as of December 31, 2005. The projects include the following:

	Spent-to-Date	Remaining Commitment
Governmental Activities		
Roads and bridges	\$ 4,212,043	\$ -
Exhaust extraction system	-	16,901
Ditch improvements	8,359	12,775
Sheriff purchases	-	21,899

3. Postemployment Benefits

Elected Officials' Benefits

Elected County officials and their dependents and surviving spouses are entitled to one year of paid health insurance for every two years of service to the County. There is no maximum number of years for officials elected prior to 1995. Those elected after 1995 are restricted to a maximum of six years of coverage.

This post-service benefit is funded on a pay-as-you-go basis. The County had seven elected officials who were eligible for this benefit in 2005. The total cost for this program totaled \$53,460 in 2005.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities (Continued)

4. Capital Lease

The County has entered into a lease agreement with Alfa-Wireless for financing the upgrade to a 911 Motorola Gold Console in the law enforcement center. This lease agreement qualifies as a capital lease for accounting purposes and, therefore, has been recorded at the present value of their future minimum lease payments as of the inception date. The lease is as follows at December 31, 2005:

<u>Capital Lease</u>	<u>Final Maturity</u>	<u>Installment Amount</u>	<u>Interest Rate (%)</u>	<u>Original Issue Amount</u>	<u>Outstanding Balance December 31, 2005</u>
2005 Motorola Gold Console	2010	\$1,334	.12	<u>\$ 82,950</u>	<u>\$ 82,950</u>

The future minimum lease obligations and the net present value of these minimum lease payments as of December 31, 2005, were as follows:

<u>Year Ending December 31</u>	<u>Governmental Activities</u>
2006	\$ 16,590
2007	16,590
2008	16,590
2009	16,590
2010	<u>18,115</u>
Total minimum lease payments	\$ 84,475
Less: amount representing interest	<u>(1,525)</u>
Present Value of Minimum Lease Payments	<u>\$ 82,950</u>

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities (Continued)

5. Long-Term Debt

Governmental Activities

Bonds Payable

<u>Type of Indebtedness</u>	<u>Final Maturity</u>	<u>Installment Amounts</u>	<u>Average Interest Rate (%)</u>	<u>Original Issue Amount</u>	<u>Outstanding Balance December 31, 2005</u>
General obligation bonds					
2004 G.O. Tax Increment Refunding Bonds	2007	\$190,000 - \$195,000	3.092	\$ 385,000	\$ 385,000
1997 G.O. Correctional Facility Refunding Bonds	2006	\$145,000 - \$190,000	4.782	<u>1,170,000</u>	<u>190,000</u>
Total general obligation bonds				<u>\$ 1,555,000</u>	\$ 575,000
Less: unamortized discount					<u>(1,027)</u>
Total general obligation bonds, net					<u>\$ 573,973</u>
Special assessment bonds with government commitment					
1998 G.O. Drainage Bonds	2020	\$10,000 - \$30,000	4.857	\$ 2,510,000	\$ 1,835,000
2005 G.O. Drainage Crossover Refunding Bonds	2020	\$110,000 - \$175,000	3.5586	1,900,000	1,900,000
2000 G.O. Drainage Bonds	2016	\$15,000 - \$35,000	5.2667	<u>365,000</u>	<u>295,000</u>
Total special assessment bonds with government commitment				<u>\$ 4,775,000</u>	\$ 4,030,000
Less: unamortized discount					<u>(29,815)</u>
Total Governmental Activities, Net					<u>\$ 4,000,185</u>

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities

5. Long-Term Debt

Governmental Activities (Continued)

Loans Payable

In 1996, the County agreed to act as loan and project sponsor for a project loan agreement made under the Clean Water Partnership Law with the State of Minnesota through the Minnesota Pollution Control Agency (PCA) and the Brown-Nicollet-Cottonwood Project Joint Powers Board. The County is required to repay these funds to the PCA. In 1998, additional Ag Well loan funds were received through the Minnesota Department of Agriculture. The loan terms and repayment are similar to those received through the PCA. The County is required to repay the funds to the Minnesota Department of Agriculture. In 2000, the County entered into the Watonwan Watershed Project loan program with \$370,000 available for site-specific groundwater improvement projects. All loans are secured by special assessments placed on the individual parcels requesting repair of a failing system. Loan payments are reported in the General Fund.

Business-Type Activities

Bonds Payable

<u>Type of Indebtedness</u>	<u>Final Maturity</u>	<u>Installment Amounts</u>	<u>Average Interest Rate (%)</u>	<u>Original Issue Amount</u>	<u>Outstanding Balance December 31, 2005</u>
General obligation bonds					
Series 2004 G.O. Landfill Bonds	2009	\$70,000 - \$75,000	2.8688	\$ 365,000	\$ 295,000
Series 1999A G.O. Landfill Bonds	2006	\$65,000 - \$80,000	4.0539	<u>360,000</u>	<u>80,000</u>
Total general obligation landfill bonds				<u>\$ 725,000</u>	\$ 375,000
Less: unamortized discount					<u>(3,723)</u>
Total General Obligation Landfill Bonds, Net					<u>\$ 371,277</u>

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities (Continued)

6. Debt Service Requirements

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

Governmental Activities

Year Ending December 31	General Obligation Bonds		Special Assessment Bonds	
	Principal	Interest	Principal	Interest
2006	\$ 380,000	\$ 13,748	\$ 150,000	\$ 101,540
2007	195,000	3,169	1,980,000	80,591
2008	-	-	170,000	61,080
2009	-	-	175,000	56,895
2010	-	-	160,000	52,468
2011 - 2015	-	-	780,000	188,384
2016 - 2020	-	-	615,000	58,022
Total	\$ 575,000	\$ 16,917	\$ 4,030,000	\$ 598,980

Year Ending December 31	Loans Payable	
	Principal	Interest
2006	\$ 142,775	\$ 9,605
2007	148,737	9,701
2008	154,869	9,626
2009	126,609	8,385
2010	93,375	7,120
2011 - 2015	443,134	16,407
2016 - 2020	99,054	357
2021 - 2025	22,452	-
Total	\$ 1,231,005	\$ 61,201

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities

6. Debt Service Requirements (Continued)

Business-Type Activities

Year Ending December 31	General Obligation Bonds	
	Principal	Interest
2006	\$ 150,000	\$ 9,125
2007	75,000	5,681
2008	75,000	3,563
2009	75,000	1,219
Total	<u>\$ 375,000</u>	<u>\$ 19,588</u>

7. Changes in Long-Term Liabilities

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

Governmental Activities

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Bonds payable (fund liquidating the debt)					
General obligation bonds (General)	\$ 375,000	\$ -	\$ 185,000	\$ 190,000	\$ 190,000
Tax increment (Debt Service)	930,000	-	545,000	385,000	190,000
Special assessment debt with government commitment (Ditch)	2,280,000	1,900,000	150,000	4,030,000	150,000
Less: unamortized discount	<u>(1,540)</u>	<u>(32,300)</u>	<u>(2,998)</u>	<u>(30,842)</u>	<u>(2,998)</u>
Total bonds payable	\$ 3,583,460	\$ 1,867,700	\$ 877,002	\$ 4,574,158	\$ 527,002
Loans payable	1,179,450	168,534	116,979	1,231,005	118,008
Compensated absences	<u>477,815</u>	<u>43,746</u>	<u>-</u>	<u>521,561</u>	<u>41,620</u>
Governmental Activities Long-Term Liabilities	<u>\$ 5,240,725</u>	<u>\$ 2,079,980</u>	<u>\$ 993,981</u>	<u>\$ 6,326,724</u>	<u>\$ 686,630</u>

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities

7. Changes in Long-Term Liabilities (Continued)

Business-Type Activities

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Bonds payable					
General obligation bonds	\$ 520,000	\$ -	\$ 145,000	\$ 375,000	\$ 150,000
Less: unamortized discount	(6,079)	-	(2,356)	(3,723)	(1,241)
Total bonds payable	\$ 513,921	\$ -	\$ 142,644	\$ 371,277	\$ 148,759
Estimated liability for landfill closure and postclosure care	1,029,392	166,093	-	1,195,485	-
Compensated absences	11,203	1,300	-	12,503	-
Business-Type Activities Long-Term Liabilities	<u>\$ 1,554,516</u>	<u>\$ 167,393</u>	<u>\$ 142,644</u>	<u>\$ 1,579,265</u>	<u>\$ 148,759</u>

8. Advance Crossover Refunding of Debt

On February 1, 2005, Cottonwood County issued General Obligation Drainage Crossover Refunding Bonds, Series 2005A, in the amount of \$1,900,000, with interest rates of 2.35 percent to 4.10 percent to advance crossover refund the following issues:

The General Obligation Drainage Bonds, Series 1998, dated May 1, 1998, maturing after February 1, 2007--the balance of the outstanding maturities to be refunded is \$1,575,000, and interest rates are 4.60 percent to 5.00 percent.

The General Obligation Drainage Bonds, Series 2000A, dated April 1, 2000, maturing after February 1, 2007--the balance of the outstanding maturities to be refunded is \$255,000, and interest rates are 5.30 percent to 5.65 percent.

The proceeds from the bonds were placed with an escrow agent in an irrevocable trust from which U.S. Treasury securities were purchased. The County is responsible for the principal and interest on the original issue through February 1, 2007. The refunded bonds will be called and paid by the escrow agent on February 1, 2007. The escrow agent will pay the interest due on the 2004 bonds

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities

8. Advance Crossover Refunding of Debt (Continued)

through February 1, 2007; thereafter, the County will be responsible for the payment of debt service. The principal balance of both the original issues and the refunding issue will be shown on the balance sheet until the call date of the refunded bonds, at which time the 1998 bonds and the Series 2000A bonds will be paid, and the liability for those bonds will be removed.

The General Obligation Drainage Crossover Refunding Bonds, Series 2005A, were issued at a discount of \$32,300 and, after paying debt issuance costs of \$26,885, the net proceeds were \$1,840,815. The County deposited \$1,756 of excess proceeds into the Debt Service Fund for future debt payments.

As a result of the advance crossover refunding, the County reduced its total debt service requirements by \$100,651; the remaining \$1,734,346 of bond proceeds were used to purchase U.S. government securities, and those securities were deposited in an irrevocable trust with an escrow agent to provide debt service payments on the General Obligation Drainage Crossover Refunding Bonds, Series 2005A, until February 1, 2007, at which time the refunded bonds will be paid off. The sale resulted in an economic gain (difference between the present value of the debt service payments on the old and new debt service) of \$75,192.

4. 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 \$1,195,485 landfill closure and postclosure care liability at December 31, 2005, represents the cumulative amount reported to date based on the use of 57 percent of the estimated capacity of the landfill. The County will recognize the remaining estimated cost of closure and

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

4. Landfill Closure and Postclosure Care Costs (Continued)

postclosure care of \$894,903 as the remaining estimated capacity is filled. These amounts are based on what it would cost to perform all closure and postclosure care in 2005. The Board expects to close the landfill in 2035. 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 and, at December 31, 2005, the County has in restricted assets \$1,366,313 for these purposes. Cottonwood 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.

5. 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.

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

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

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

5. Risk Management (Continued)

In November 1988, the County began to self-insure for employee health insurance coverage. The County has retained risk up to \$50,000 stop-loss per person per year (\$1,387,708 aggregate) for the health plan. At December 31, 2005, the amount of the County's liability was \$73,011. This liability is the County's best estimate based on available information.

Liabilities of the fund are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported (IBNRs). The result of the process to estimate the claims liability is not an exact amount as it depends on many complex factors, such as inflation, changes in legal doctrines, and damage awards. Accordingly, claims are re-evaluated periodically to consider the effects of inflation, recent claim settlement trends (including frequency and amount of pay-outs), and other economic and social factors. Changes in the balances of claims liabilities during the past two years are as follows:

	Year Ended December 31	
	2004	2005
Unpaid claims, beginning of fiscal year	\$ 137,456	\$ 98,353
Incurred claims (including IBNRs)	1,344,177	1,362,366
Claims payments	(1,383,280)	(1,387,708)
Unpaid Claims, End of Fiscal Year	\$ 98,353	\$ 73,011

6. Employee Retirement Systems and Pension Plans

A. Defined Benefit Plans

Plan Description

All full-time and certain part-time employees of Cottonwood 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.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

6. Employee Retirement Systems and Pension Plans

A. Defined Benefit Plans

Plan Description (Continued)

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

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

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.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

6. Employee Retirement Systems and Pension Plans

A. Defined Benefit Plans

Plan Description (Continued)

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

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

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 were required to contribute 9.10 and 5.10 percent, respectively, of their annual covered salary in 2005. Contribution rates in the Coordinated Plan increased in 2006 to 5.5 percent. Public Employees Police and Fire Fund members were required to contribute 6.20 percent of their annual covered salary in 2005. That rate increased to 7.00 percent in 2006. Public Employees Correctional Fund members are required to contribute 5.83 percent of their annual covered salary.

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

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

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

6. Employee Retirement Systems and Pension Plans

A. Defined Benefit Plans

Funding Policy (Continued)

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

	Public Employees Retirement Fund	Public Employees Police and Fire Fund	Public Employees Correctional Fund
2005	\$ 171,952	\$ 37,364	\$ 28,009
2004	162,586	32,611	23,920
2003	161,299	28,684	24,410

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

B. Defined Contribution Plan

The Public Employees Defined Contribution Plan is a multiple-employer deferred compensation plan for local government officials, except elected county sheriffs. The plan is established and administered in accordance with Minn. Stat. ch. 353D. The plan is a tax qualified plan under Section 401(a) of the Internal Revenue Code, and all contributions by or on behalf of employees are tax deferred until time of withdrawal.

Plan benefits depend solely on amounts contributed to the plan plus investment earnings, less administrative expenses. Minn. Stat. § 353D.03 specifies the employee and employer contribution rates for those qualified personnel who elect to participate. An eligible elected official who decides to participate contributes five percent of salary, which is matched by the employer.

No vesting period is required to receive benefits in the Defined Contribution Plan. At the time of retirement or termination, the market value of the member's account is distributed to the member or another qualified plan.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

6. Employee Retirement Systems and Pension Plans

B. Defined Contribution Plan (Continued)

The County's contributions for the years ending December 31, 2005, 2004, and 2003, were \$2,032, \$1,710, and \$1,627, respectively, equal to the contractually required contributions for each year as set by state statute.

7. Summary of Significant Contingencies and Other Items

A. Contingent Liabilities

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

B. Joint Ventures

Cottonwood-Jackson Community Health Services Board

The Cottonwood-Jackson Community Health Services Board was established pursuant to Minn. Stat. ch. 145A and a joint powers agreement effective January 1, 1977.

The Cottonwood-Jackson Community Health Services Board is made up of the five elected County Commissioners from both Cottonwood and Jackson Counties. Both counties levy a tax to help support the Health Services Board. For 2004, Cottonwood County contributed \$109,844 to the Health Services Board. For 2005, the Health Services Board had an increase in net assets of \$47,020 from operations. At December 31, 2005, total net assets were \$335,177.

Complete financial statements for the Health Services Board can be obtained at 503 Fourth Street, Jackson, Minnesota 56143.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

7. Summary of Significant Contingencies and Other Items

B. Joint Ventures (Continued)

Southwestern Minnesota Adult Mental Health Consortium Board

In November 1997, the County entered into a joint powers agreement with several other governmental entities to create the Southwestern Minnesota Adult Mental Health Consortium Board under the authority of Minn. Stat. § 471.59. The Board is headquartered in Windom, Minnesota, where Cottonwood County acts as fiscal host.

The Board shall take actions and enter into such agreements as may be necessary to plan and develop within the Southwestern Minnesota Adult Mental Health Consortium Board's geographic jurisdiction, a system of care that will serve the needs of adults with serious and persistent mental illness. The governing board is composed of one board member from each of the participating counties.

Financing is provided by state proceeds or appropriations for the development of the system of care.

The following is a summary of the Board's annual financial report for the year ended December 31, 2003 (the latest information available):

Total assets	\$	220,978
Total liabilities		5,230
Total equity		215,748
Total revenues		889,414
Total expenditures		856,904
Net increase to fund balance		32,510

The Board reported no long-term obligations at December 31, 2003. A complete financial report of the Southwestern Minnesota Adult Mental Health Consortium Board can be obtained at the Cottonwood County Family Services Agency, Windom, Minnesota 56101.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

7. Summary of Significant Contingencies and Other Items

B. Joint Ventures (Continued)

Red Rock Rural Water System

The Red Rock Rural Water System was established pursuant to Minn. Stat. ch. 116A through a joint powers agreement pursuant to Minn. Stat. § 471.59 and under the jurisdiction of the Fifth Judicial District. The participating Counties of Brown, Cottonwood, Lyon, Murray, Redwood, and Watonwan have agreed to guarantee their share of debt arising within each respective county. The Red Rock Rural Water System provides water for participating rural water users and cities within the water district.

The Red Rock Rural Water System is governed by a nine-member board appointed for terms of three years by the District Court.

Each county is responsible for levying and collecting the special assessments from the benefited properties within the county. A bond issue and notes payable are shown as long-term debt on the financial statements of the Red Rock Rural Water System. Outstanding bonds at December 31, 2004 (the latest information available), were \$6,425,534, and notes payable were \$267,419. Fund balance was \$1,443,112.

A complete financial report can be obtained at 305 West Whited Street, Jeffers, Minnesota 56145.

C. Jointly-Governed Organization

Cottonwood County, in conjunction with other governmental entities and various private organizations, has formed the jointly-governed organization listed below:

Family Service Collaborative

The Family Service Collaborative was established to create opportunities to enhance family strengths and support through service coordination and access to informal communication. Cottonwood County has no operational or financial control over the Collaborative.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

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

D. Agriculture Best Management Loan Program

The County has entered into an agreement with the Minnesota Department of Agriculture and two local lending institutions to jointly administer a loan program to individuals to implement projects that prevent or mitigate non-point source water pollution. While the County is not liable for repayment of the loans in any manner, it does have certain responsibilities under the agreement.

8. Tax Increment Financing

Name of District:	Ethanol Tax Increment Financing District, No. 1-1
Type of District:	Economic Development
Authorizing Law:	§§ 469.001 to 469.047 and 469.174 to 469.179
Date Established:	May 7, 1996
Duration of District:	11 years
Original Tax Capacity:	\$884
Current Tax Capacity:	\$158,653
Captured Tax Capacity Retained by Authority:	\$157,704
Total G.O. Taxable Tax Increment Bonds Issued:	\$1,645,000
Amounts Redeemed:	\$1,260,000
Outstanding Bonds at December 31, 2005:	\$385,000

The project in this District is Ethanol 2000 (Ethanol Production Plant). No other tax increment obligations were issued on behalf of private entities for facilities located in the District.

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REQUIRED SUPPLEMENTARY INFORMATION

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**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

Schedule 1

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

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Revenues				
Taxes	\$ 2,604,004	\$ 2,604,004	\$ 2,374,826	\$ (229,178)
Special assessments	377,741	377,741	384,639	6,898
Licenses and permits	5,456	5,456	8,415	2,959
Intergovernmental	1,483,609	1,483,609	1,853,299	369,690
Charges for services	242,200	242,200	297,659	55,459
Gifts and contributions	-	-	700	700
Investment earnings	167,650	167,650	234,844	67,194
Miscellaneous	143,990	143,990	275,129	131,139
Total Revenues	\$ 5,024,650	\$ 5,024,650	\$ 5,429,511	\$ 404,861
Expenditures				
Current				
General government				
Commissioners	\$ 237,629	\$ 237,629	\$ 237,473	\$ 156
Courts	10,200	10,200	12,375	(2,175)
Law library	18,500	18,500	11,146	7,354
Auditor/treasurer	385,519	407,519	361,032	46,487
Assessor	219,088	223,088	206,993	16,095
Elections	32,724	32,724	26,385	6,339
Attorney	237,722	237,722	249,869	(12,147)
Recorder	162,035	165,035	163,277	1,758
Buildings and plant	78,482	83,482	86,498	(3,016)
Veterans service officer	88,419	88,419	90,945	(2,526)
Transit	101,535	101,535	117,179	(15,644)
Other general government	375,997	316,011	270,802	45,209
Total general government	\$ 1,947,850	\$ 1,921,864	\$ 1,833,974	\$ 87,890
Public safety				
Sheriff	\$ 637,076	\$ 637,076	\$ 811,089	\$ (174,013)
Emergency services	118,179	118,179	77,351	40,828
Coroner	4,000	4,000	10,537	(6,537)
Safety program	3,800	3,800	2,937	863
Jail	674,701	674,701	666,132	8,569
Probation and parole	111,338	111,838	122,966	(11,128)
Total public safety	\$ 1,549,094	\$ 1,549,594	\$ 1,691,012	\$ (141,418)
Sanitation				
Recycling	\$ 235,651	\$ 253,151	\$ 205,455	\$ 47,696

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

Schedule 1
(Continued)

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

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Expenditures				
Current (Continued)				
Health				
Community health	\$ 1,725	\$ 1,725	\$ 5,653	\$ (3,928)
Food, beverage, and lodging	9,425	9,425	7,525	1,900
Total health	\$ 11,150	\$ 11,150	\$ 13,178	\$ (2,028)
Culture and recreation				
Parks	\$ 71,333	\$ 83,333	\$ 90,089	\$ (6,756)
Minnesota trails	-	-	55,622	(55,622)
Regional library	49,200	49,200	49,984	(784)
Other	400	400	100	300
Total culture and recreation	\$ 120,933	\$ 132,933	\$ 195,795	\$ (62,862)
Conservation of natural resources				
Extension	\$ 123,063	\$ 123,063	\$ 101,460	\$ 21,603
Soil and water conservation	91,678	91,678	89,855	1,823
Water quality loan program	-	-	157,644	(157,644)
ISTS pilot project	55,275	55,275	58,786	(3,511)
Water planning	87,894	87,894	74,997	12,897
Des Moines River project	-	-	11,444	(11,444)
Environmental services	112,690	114,190	121,787	(7,597)
Total conservation of natural resources	\$ 470,600	\$ 472,100	\$ 615,973	\$ (143,873)
Economic development				
Other	\$ 7,950	\$ 7,950	\$ 18,014	\$ (10,064)
Intergovernmental				
Health	\$ 111,593	\$ 111,593	\$ 107,693	\$ 3,900
Debt service				
Principal	\$ 291,011	\$ 291,011	\$ 661,979	\$ (370,968)
Interest	\$ 40,885	\$ 40,885	\$ 34,486	\$ 6,399
Administrative (fiscal) charges	\$ -	\$ -	\$ 476	\$ (476)
Total Expenditures	\$ 4,786,717	\$ 4,792,231	\$ 5,378,035	\$ (585,804)
Excess of Revenues Over (Under) Expenditures	\$ 237,933	\$ 232,419	\$ 51,476	\$ (180,943)

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

Schedule 1
(Continued)

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

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Other Financing Sources (Uses)				
Transfers in	\$ -	\$ -	\$ 27,000	\$ 27,000
Transfers out	(237,933)	(235,919)	(57,374)	178,545
Proceeds from capital lease	-	-	82,950	82,950
Loans issued	-	-	145,140	145,140
Total Other Financing Sources (Uses)	\$ (237,933)	\$ (235,919)	\$ 197,716	\$ 433,635
Net Change in Fund Balance	\$ -	\$ (3,500)	\$ 249,192	\$ 252,692
Fund Balance - January 1, as previously reported	\$ 5,039,916	\$ 5,039,916	\$ 5,039,916	\$ -
Prior period adjustment (Note 1.E.)	258,617	258,617	258,617	-
Fund Balance - January 1, as restated	\$ 5,298,533	\$ 5,298,533	\$ 5,298,533	\$ -
Fund Balance - December 31	\$ 5,298,533	\$ 5,295,033	\$ 5,547,725	\$ 252,692

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

Schedule 2

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

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Revenues				
Taxes	\$ 947,625	\$ 947,625	\$ 839,150	\$ (108,475)
Intergovernmental	3,183,623	3,183,623	3,226,287	42,664
Charges for services	30,000	30,000	29,694	(306)
Miscellaneous	60,800	60,800	18,573	(42,227)
Total Revenues	\$ 4,222,048	\$ 4,222,048	\$ 4,113,704	\$ (108,344)
Expenditures				
Current				
Highways and streets				
Administration	\$ 223,818	\$ 223,818	\$ 188,240	\$ 35,578
Maintenance	1,094,106	1,094,106	933,141	160,965
Construction	2,010,603	2,010,603	3,168,158	(1,157,555)
Equipment and maintenance shops	898,520	898,520	722,900	175,620
Total highways and streets	\$ 4,227,047	\$ 4,227,047	\$ 5,012,439	\$ (785,392)
Intergovernmental				
Highways and streets	-	-	254,034	(254,034)
Total Expenditures	\$ 4,227,047	\$ 4,227,047	\$ 5,266,473	\$ (1,039,426)
Excess of Revenues Over (Under) Expenditures	\$ (4,999)	\$ (4,999)	\$ (1,152,769)	\$ (1,147,770)
Other Financing Sources (Uses)				
Transfers in	-	-	2,038	2,038
Net Change in Fund Balance	\$ (4,999)	\$ (4,999)	\$ (1,150,731)	\$ (1,145,732)
Fund Balance - January 1	1,423,180	1,423,180	1,423,180	-
Increase (decrease) in reserved for inventories	-	-	(26,748)	(26,748)
Fund Balance - December 31	\$ 1,418,181	\$ 1,418,181	\$ 245,701	\$ (1,172,480)

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

Schedule 3

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

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Revenues				
Taxes	\$ 1,671,877	\$ 1,671,877	\$ 1,480,286	\$ (191,591)
Intergovernmental	2,212,714	2,212,714	2,080,573	(132,141)
Charges for services	20,000	20,000	32,500	12,500
Miscellaneous	182,215	182,215	278,119	95,904
Total Revenues	\$ 4,086,806	\$ 4,086,806	\$ 3,871,478	\$ (215,328)
Expenditures				
Current				
Human services				
Income maintenance	\$ 980,962	\$ 993,553	\$ 966,246	\$ 27,307
Social services	3,105,844	3,127,285	3,083,180	44,105
Total Expenditures	\$ 4,086,806	\$ 4,120,838	\$ 4,049,426	\$ 71,412
Net Change in Fund Balance	\$ -	\$ (34,032)	\$ (177,948)	\$ (143,916)
Fund Balance - January 1	1,030,386	1,030,386	1,030,386	-
Fund Balance - December 31	\$ 1,030,386	\$ 996,354	\$ 852,438	\$ (143,916)

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

Schedule 4

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

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Revenues				
Special assessments	\$ 284,646	\$ 284,646	\$ 228,297	\$ (56,349)
Investment earnings	-	-	31,539	31,539
Total Revenues	\$ 284,646	\$ 284,646	\$ 259,836	\$ (24,810)
Expenditures				
Current				
Conservation of natural resources				
Other	\$ 26,000	\$ 26,000	\$ 99,189	\$ (73,189)
Debt service				
Principal	150,000	150,000	150,000	-
Interest	108,646	108,646	142,199	(33,553)
Bond issuance costs	-	-	26,885	(26,885)
Administrative (fiscal) charges	-	-	547	(547)
Total Expenditures	\$ 284,646	\$ 284,646	\$ 418,820	\$ (134,174)
Excess of Revenues Over (Under) Expenditures	\$ -	\$ -	\$ (158,984)	\$ (158,984)
Other Financing Sources (Uses)				
Transfers in	\$ -	\$ -	\$ 3,649	\$ 3,649
Proceeds from sale of refunding bonds	-	-	1,900,000	1,900,000
Discounts on bonds issued	-	-	(32,300)	(32,300)
Total Other Financing Sources (Uses)	\$ -	\$ -	\$ 1,871,349	\$ 1,871,349
Net Change in Fund Balance	\$ -	\$ -	\$ 1,712,365	\$ 1,712,365
Fund Balance - January 1	712,637	712,637	712,637	-
Fund Balance - December 31	\$ 712,637	\$ 712,637	\$ 2,425,002	\$ 1,712,365

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

Schedule 5

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

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Revenues				
Taxes	\$ 50,000	\$ 50,000	\$ 44,225	\$ (5,775)
Intergovernmental	-	-	5,153	5,153
Miscellaneous	37,810	37,810	73,209	35,399
Total Revenues	\$ 87,810	\$ 87,810	\$ 122,587	\$ 34,777
Expenditures				
Current				
General government				
Buildings and plant	87,810	87,810	42,503	45,307
Net Change in Fund Balance	\$ -	\$ -	\$ 80,084	\$ 80,084
Fund Balance - January 1	101,000	101,000	101,000	-
Fund Balance - December 31	\$ 101,000	\$ 101,000	\$ 181,084	\$ 80,084

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**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

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

1. General Budget Policies

The Cottonwood County Board adopts estimated revenue and expenditure budgets for the General Fund, certain special revenue funds, and the Debt Service Fund. The expenditure budget is approved at the fund level.

The budgets may be amended or modified at any time by the County Board. Comparisons of final budgeted revenues and expenditures to actual are presented in the required supplementary information for the General Fund and budgeted special revenue funds.

2. Budget Basis of Accounting

Budgets are adopted on a basis consistent with generally accepted accounting principles.

3. Budget Amendments

The expenditure budget in the General Fund was amended as follows:

	<u>Original Budget</u>	<u>Increase (Decrease)</u>	<u>Final Budget</u>
General Fund	\$ 4,786,717	\$ 5,514	\$ 4,792,231
Family Services Fund	4,086,806	34,032	4,120,838

4. General Fund Budgetary Highlights

Over the course of the year, the County Board revised the County's General Fund and the Family Services Fund budgets several times. These budget amendments fall into two categories: new information changing original budget estimations and greater than anticipated revenues or costs.

Even with these adjustments, the actual charges to appropriations (expenditures) were \$585,804 above the final budget amounts. Reasons for significant variances of actual expenditures from final budget include expenditures made from departments without budgeted expenses and higher than anticipated overtime in the Law Enforcement Department.

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

4. General Fund Budgetary Highlights (Continued)

On the other hand, resources available for appropriation were also \$404,861 above the final budgeted amount. Greater than expected collections for certain fees offset reductions in anticipated investment earnings and state appropriations.

5. Excess of Expenditures Over Budget

<u>Fund</u>	<u>Expenditures</u>	<u>Budget</u>	<u>Excess</u>
General	\$ 5,378,035	\$ 4,792,231	\$ 585,804
Road and Bridge	5,266,473	4,227,047	1,039,426
Ditch	418,820	284,646	134,174

SUPPLEMENTARY INFORMATION

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**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

Schedule 6

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

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Revenues				
Taxes	\$ 199,158	\$ 199,158	\$ 177,504	\$ (21,654)
Intergovernmental	-	-	20,524	20,524
Total Revenues	\$ 199,158	\$ 199,158	\$ 198,028	\$ (1,130)
Expenditures				
Debt service				
Principal	\$ 185,000	\$ 185,000	\$ 185,000	\$ -
Interest	14,158	14,158	14,032	126
Administrative (fiscal) charges	-	-	78	(78)
Total Expenditures	\$ 199,158	\$ 199,158	\$ 199,110	\$ 48
Excess of Revenues Over (Under) Expenditures	\$ -	\$ -	\$ (1,082)	\$ (1,178)
Other Financing Sources (Uses)				
Transfers in	-	-	5,226	5,226
Net Change in Fund Balance	\$ -	\$ -	\$ 4,144	\$ 4,048
Fund Balance - January 1	300,794	300,794	300,794	-
Fund Balance - December 31	\$ 300,794	\$ 300,794	\$ 304,938	\$ 4,048

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

Statement 1

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

	Balance January 1	Additions	Deductions	Balance December 31
<u>AGENCY</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 15,620	\$ 146,832	\$ 144,772	\$ 17,680
<u>Liabilities</u>				
Due to other governments	\$ 15,620	\$ 146,832	\$ 144,772	\$ 17,680
 <u>MENTAL HEALTH CONSORTIUM</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 82,141	\$ 4,696,285	\$ 4,088,460	\$ 689,966
<u>Liabilities</u>				
Due to other governments	\$ 82,141	\$ 4,696,285	\$ 4,088,460	\$ 689,966
 <u>MORTGAGE REGISTRY</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 16,508	\$ 94,705	\$ 105,640	\$ 5,573
<u>Liabilities</u>				
Due to other governments	\$ 16,508	\$ 94,705	\$ 105,640	\$ 5,573

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

Statement 1
(Continued)

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

	Balance January 1	Additions	Deductions	Balance December 31
<u>STATE DEED TAX</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 10,820	\$ 113,736	\$ 110,398	\$ 14,158
<u>Liabilities</u>				
Due to other governments	\$ 10,820	\$ 113,736	\$ 110,398	\$ 14,158
 <u>TAXES AND PENALTIES</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 69,901	\$ 11,448,176	\$ 11,437,924	\$ 80,153
<u>Liabilities</u>				
Due to other governments	\$ 69,901	\$ 11,448,176	\$ 11,437,924	\$ 80,153
 <u>TOTAL ALL AGENCY FUNDS</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 194,990	\$ 16,499,734	\$ 15,887,194	\$ 807,530
<u>Liabilities</u>				
Due to other governments	\$ 194,990	\$ 16,499,734	\$ 15,887,194	\$ 807,530

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

Schedule 7

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

	Governmental Funds	Landfill Enterprise Fund	Total All Funds
Shared Revenue			
State			
Highway users tax	\$ 3,121,275	\$ -	\$ 3,121,275
County program aid	968,410	-	968,410
PERA rate reimbursement	17,411	-	17,411
Disparity reduction aid	46,857	-	46,857
Police aid	32,611	-	32,611
Enhanced 911	64,218	-	64,218
Market value credit	550,010	10,306	560,316
Total Shared Revenue	\$ 4,800,792	\$ 10,306	\$ 4,811,098
Reimbursement for Services			
State			
Minnesota Department of Human Services	\$ 907,380	\$ -	\$ 907,380
Payments			
Local			
Local	\$ 6,093	\$ -	\$ 6,093
Payments in lieu of taxes	51,792	-	51,792
Total Payments	\$ 57,885	\$ -	\$ 57,885
Grants			
State			
Minnesota Department of Corrections	\$ 26,017	\$ -	\$ 26,017
Public Safety	1,218	-	1,218
Transportation	63,563	-	63,563
Human Services	720,398	-	720,398
Natural Resources	10,622	-	10,622
Veteran Affairs	1,400	-	1,400
Water and Soil Resources Board	50,429	-	50,429
Peace Officer Standards and Training Board	2,820	-	2,820
Office of Environmental Assistance	24,539	-	24,539
Pollution Control Agency	85,761	-	85,761
Total State	\$ 986,767	\$ -	\$ 986,767

**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

Schedule 7
(Continued)

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

	Governmental Funds	Landfill Enterprise Fund	Total All Funds
Grants (Continued)			
Federal			
Department of			
Agriculture	\$ 4,790	\$ -	\$ 4,790
Labor	3,000	-	3,000
Transportation	65,788	-	65,788
Health and Human Services	295,203	-	295,203
Homeland Security	56,580	-	56,580
Environmental Protection Agency	7,651	-	7,651
	\$ 433,012	\$ -	\$ 433,012
Total Federal	\$ 433,012	\$ -	\$ 433,012
Total State and Federal Grants	\$ 1,419,779	\$ -	\$ 1,419,779
Total Intergovernmental Revenue	\$ 7,185,836	\$ 10,306	\$ 7,196,142

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**COTTONWOOD COUNTY
WINDOM, MINNESOTA**

Schedule 8

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

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

INTERNAL CONTROL

PREVIOUSLY REPORTED ITEM NOT RESOLVED

99-1 Internal Accounting Controls

Due to the limited number of office personnel within the various County departments, proper segregation of the accounting functions necessary to ensure adequate internal accounting control is not possible. Although this is not unusual in small departmental situations, 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 internal control point of view.

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

Client's Response:

The County will comply.

ITEM ARISING THIS YEAR

05-1 Checking Account Reconciliation

The County's Bank of the West checking account is out of balance by \$1,259.40 at December 31, 2005. The account has been out of balance since October of 2005 and has continued to be out of balance during all of 2006. This could lead to inaccurate reporting of cash balances and the potential loss of County funds due to bank error.

We recommend that the County take steps to ensure that cash balances reconcile to the bank statements every month.

Client Response:

The County will comply.

II. OTHER FINDINGS AND RECOMMENDATIONS

A. MINNESOTA LEGAL COMPLIANCE

PREVIOUSLY REPORTED ITEMS NOT RESOLVED

01-6 Collateral Assignments

The County did not have documentation demonstrating that it had a perfected interest in pledged collateral with Bank of the West. In a Federal Court decision, the Court ruled that if a municipality fails to perfect a security interest under federal law, its right to such collateral in the event of default is not enforceable. Minn. Stat. § 118A.03, subd. 3, requires the County to obtain an assignment of pledged collateral equal to “at least ten percent more than the amount on deposit plus accrued interest at the close of the business day,” in excess of federal deposit insurance.

The County is not complying with the collateral requirement unless it obtains an enforceable assignment of pledged collateral. To obtain an enforceable assignment under federal law (12 U.S.C. § 1823(e)), the County must obtain a written assignment of collateral which is approved by the depository bank’s board of directors or loan committee and is a continuous official record of the bank.

We recommend that the County obtain the documentation indicating it has perfected a security interest in pledged collateral.

Client’s Response:

The County will comply.

02-2 Undistributed Collections in Taxes and Penalties Agency Fund

At December 31, 2005, undistributed collections in the Taxes and Penalties Agency Fund were \$11,538. The County Auditor/Treasurer could not explain the unreconciled variance.

Minn. Stat. § 276.111 states that amounts collected from the previous settlement date to December 31 should be settled “to each of the taxing districts on or before January 25. . . .” This statute goes on to say, “Interest accrues at an annual rate of eight percent and must be paid to the taxing district if this final settlement amount is not paid by January 25.”

We recommend that the County comply with the provisions of Minn. Stat. § 276.111.

Client’s Response:

The County will comply.

ITEM ARISING THIS YEAR

05-2 Depository Pledge Agreement

The County does not have Depository Pledge Agreements with any of the banks that pledge collateral.

We recommend that the County execute security agreements with all banks. The pledge agreement should be consistent with the language of Minn. Stat. § 118A.03.

Client’s Response:

The County will comply.

B. MANAGEMENT PRACTICES

PREVIOUSLY REPORTED ITEMS NOT RESOLVED

96-6 County Ditch Fund Deficits

Eight of the 97 individual ditch systems had deficit fund balances as of December 31, 2005, totaling \$879,541, which is an increase from the \$698,732 reported in the prior audit. The largest fund balance deficit of \$563,181, in Sinking Ditch 9 Improvement, is an increase from \$438,057 reported in the prior year. The increasing deficit indicates that assessments are not sufficient to cover bond principal and interest payments.

Minn. Stat. § 103E.735, subd. 1, provides that a fund balance to be used for repairs may be established for any drainage system, not to exceed 20 percent of the assessed benefits of the ditch system or \$40,000, whichever is larger.

We recommend the County eliminate the ditch fund balance deficits by levying assessments pursuant to Minn. Stat. § 103E.735, subd. 1, which permits the accumulation of a surplus balance to provide for the repair and maintenance costs of a ditch system and repay the General Fund for the loans advanced to the County Ditch Special Revenue Fund.

Client's Response:

The County is currently levying assessments to eliminate deficit ditch balances.

00-3

Budgeting Procedures

Although the County adopts a formal budget, expenditure estimates and the annual budget appropriations to the various operational funds within the County are not always clear. The County adopts the budget in summary form. In addition, the summary budget on file did not agree with the expenditure guidelines in the accounting system and not all budget amendments were shown in the Board minutes.

Generally accepted accounting principles and the County Financial Accounting and Reporting Standards recommend that the expenditure estimates and the annual budget be appropriated to the various operational entities within the County and that line-item budget detail by fund should be available. The appropriations constitute maximum expenditure authorizations during the fiscal year and cannot legally be exceeded unless subsequently amended by the County Board. Good budget accounting requires: (1) an annual budget be adopted by every governmental unit; (2) the accounting system provide the basis for appropriate budgetary control; and (3) a common terminology and classification that can be used consistently throughout budgets, accounts, and financial reports of each fund. The County Board should adopt an accurate budget, and it should be followed by the County. The adopted budget should be designed so that comparisons can be made between current year and budget year. Any amendments to the budget should be Board approved and documented in the Board minutes.

We recommend that the County implement procedures to improve its budgetary accounting by including in the County Board minutes the amounts approved for each fund's revenues and expenditures budget. We also recommend that any changes to the original budget be approved by formal Board resolution and be so documented.

Client's Response:

The County will comply.

01-15

Payroll System

Payroll is processed on an automatic pay system for regular full-time employees of the Family Services Fund. There is no lag time from the time worked to the time paid. Family Services employees are paid on the 15th and the last day of the month. The Board approves an annual salary, and the employees are paid one-twenty-fourth of the salary each paycheck. However, employees still earn and are paid for overtime and compensatory time.

In a positive payroll system, employees are paid for the hours worked in a completed pay period and report on time sheets that have been signed by the employee and approved by the supervisor. A positive payroll system generally requires the use of a hold-back period to allow for processing time and provides additional assurance that employees are paid only for those hours that have been worked.

We recommend that the County implement a positive payroll system where wages are not paid until payroll information for a completed pay period has been received and reviewed for the Family Services Fund. A hold-back period should be established to allow for processing.

Client's Response:

The County has implemented positive payroll in the Revenue and Road and Bridge Funds. The Family Services Fund remains as the only non-positive payroll Department.

C. OTHER ITEM FOR CONSIDERATION

Other Postemployment Benefits (OPEB)

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

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

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

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

Schedule 8
(Continued)

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

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OTHER REQUIRED REPORT

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REBECCA OTTO
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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Board of County Commissioners
Cottonwood County

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Cottonwood County as of and for the year ended December 31, 2005, and have issued our report thereon dated October 17, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Cottonwood County's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted matters involving internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the County's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable conditions are described in the accompanying Schedule of Findings and Recommendations as items 99-1 and 05-1.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we do not believe the reportable condition indicated above is a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Cottonwood County's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Minnesota Legal Compliance

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

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

The results of our tests indicate that, for the items tested, Cottonwood County complied with the material terms and conditions of applicable legal provisions, except as described in the Schedule of Findings and Recommendations as items 01-6, 02-2, and 05-2.

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

/s/Rebecca Otto

REBECCA OTTO
STATE AUDITOR

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

End of Fieldwork: October 17, 2006