

STATE OF MINNESOTA

Office of the State Auditor



Rebecca Otto
State Auditor

LAKE COUNTY
TWO HARBORS, MINNESOTA

FOR THE YEAR ENDED DECEMBER 31, 2008

Description of the Office of the State Auditor

The mission of the Office of the State Auditor is to oversee local government finances for Minnesota taxpayers by helping to ensure financial integrity and accountability in local governmental financial activities.

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 160 financial and compliance audits per year and has oversight responsibilities for over 3,300 local units of government throughout the state. The office currently maintains five divisions:

Audit Practice - conducts financial and legal compliance audits of 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 approximately 730 public pension funds; and

Tax Increment Financing - 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 Employees Retirement Association Board, Minnesota Housing Finance Agency, and the Rural Finance Authority Board.

Office of the State Auditor
525 Park Street, Suite 500
Saint Paul, Minnesota 55103
(651) 296-2551
state.auditor@state.mn.us
www.auditor.state.mn.us

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

For the Year Ended December 31, 2008



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

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

**ORGANIZATION
DECEMBER 31, 2008**

			<u>Term Expires</u>
Elected			
Commissioner	Thomas Clifford	District 1	January 2009
Commissioner	Derrick Goutermont	District 2	January 2011
Commissioner	Scott Larson	District 3	January 2009
Commissioner	Paul Bergman	District 4	January 2011
Commissioner	Lenore Johnson	District 5	January 2009
Attorney	Russell H. Conrow		January 2011
Auditor/Treasurer	Steven R. McMahon		January 2011
Recorder	Erica Koski		January 2011
Sheriff	Carey Johnson		January 2011
Appointed			
Assessor	Jack Rennick		December 2012
Examiner of Titles	David Adams (St. Louis County)		Indefinite
Health Officer	Harold B. Leppink, M.D.		Indefinite
Highway Engineer	Alan Goodman		May 2012
Veterans Service Officer	George Scheidt		September 2012
Clerk of the Board	Wilma Rahn		Indefinite
County Coordinator	Matthew Huddleston		Indefinite
Human Services			
Board Members	Thomas Clifford		January 2009
	Derrick Goutermont		January 2011
	Scott Larson		January 2009
	Paul Bergman		January 2011
	Lenore Johnson		January 2009
	Kathy Goedel		Indefinite
	Christine Johnson		Indefinite
Director	Dennis Henkel		Indefinite
Nursing Home			
Board Members	Thomas Clifford		December 2009
	Derrick Goutermont		December 2011
	Scott Larson		January 2009
	Paul Bergman		December 2011
	Lenore Johnson		January 2009
	Kathy Goedel		Indefinite
	Deade Johnson		Indefinite
Administrator	Susan Johnson		Indefinite

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REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA

OFFICE OF THE STATE AUDITOR

SUITE 500
525 PARK STREET
SAINT PAUL, MN 55103-2139

(651) 296-2551 (Voice)
(651) 296-4755 (Fax)
state.auditor@state.mn.us (E-mail)
1-800-627-3529 (Relay Service)

INDEPENDENT AUDITOR'S REPORT

Board of County Commissioners
Lake County

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of Lake County, Minnesota, as of and for the year ended December 31, 2008, including the Nursing Home Enterprise Fund as of and for the year ended September 30, 2008, which collectively comprise the County's basic financial statements. These financial statements are the responsibility of Lake County's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As discussed in Note 4 to the financial statements, during the year ended December 31, 2008, the County adopted Governmental Accounting Standards Board Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of Lake County as of December 31, 2008, including the Nursing Home Enterprise Fund at

September 30, 2008, and the respective changes in financial position and cash flows, where applicable, thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis and the other required supplementary information listed in the table of contents are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the 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 made for the purpose of forming opinions on the financial statements that collectively comprise Lake County's basic financial statements. The supplementary information and other schedule listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued a report dated September 30, 2009, on our consideration of Lake County's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

/s/Rebecca Otto

REBECCA OTTO
STATE AUDITOR

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

September 30, 2009

MANAGEMENT'S DISCUSSION AND ANALYSIS

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2008
(Unaudited)**

Lake 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, 2008. 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 County's financial statements.

FINANCIAL HIGHLIGHTS

- Governmental activities' total net assets are \$93,568,267, of which \$82,402,415 is invested in capital assets, net of related debt, and \$1,526,071 is restricted to specific purposes.
- Business-type activities have total net assets of \$2,231,601. Invested in capital assets, net of related debt, represents \$2,030,618 of the total.
- Lake County's net assets increased by \$3,143,559 for the year ended December 31, 2008. Of the increase, \$3,078,781 was an increase in the governmental activities' net assets; and \$64,778 represented an increase in business-type activities' net assets. The Lake County Housing and Redevelopment Authority is shown as a "Discretely Presented Component Unit." The net assets of the County's discretely presented component unit decreased by \$35,428.
- The net cost of governmental activities was \$7,689,785 for the current fiscal year. The net cost was funded by general revenues and other items totaling \$10,768,566.
- Governmental funds' fund balances decreased by \$771,383.

OVERVIEW OF THE FINANCIAL STATEMENTS

This MD&A is intended to serve as an introduction to the basic financial statements. Lake 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), certain budgetary comparison schedules, and the schedule of funding progress are required to accompany the basic financial statements and, therefore, are included as required supplementary information.

There are two government-wide financial statements. The Statement of Net Assets and the Statement of Activities 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 report the County's operations in more detail than the government-wide statements by providing information about the County's most significant funds. For governmental activities, these statements tell how these services were financed in the short-term as well as what remains for future spending. 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

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

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

In the statement of net assets and the statement of activities, we divide the County into three 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 nursing home activities are reported here.
- Component unit--The County includes another separate legal entity in its report. The entity, the Lake County Housing and Redevelopment Authority, is presented in a separate column. Although legally separate, this "component unit" is important because the County is financially accountable for it. Further financial information for this component unit is available in separately issued and audited financial statements.

The government-wide financial statements can be found in Exhibits 1 and 2.

Fund Financial Statements

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

The basic financial statements for governmental funds can be found in Exhibits 3 through 6.

- 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 proprietary funds are substantially the same as the business-type activities we report in the government-wide statements but provide more detail and additional information, such as cash flows, for proprietary funds.

Proprietary fund financial statements may be found in Exhibits 7 through 9.

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 a separate Statement of Fiduciary Net Assets. We exclude these activities from the County's other financial statements because the County cannot use these assets to finance its operations. The County is responsible for ensuring that the assets reported in these funds are used for their intended purposes.

The fiduciary funds financial statement is Exhibit 10.

LAKE COUNTY AS A WHOLE

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
(in Thousands)

	Governmental Activities		Business-Type Activities		Total Primary Government	
	2008	2007	2008	2007	2008	2007
Current and other assets	\$ 15,399	\$ 16,861	\$ 492	\$ 371	\$ 15,891	\$ 17,232
Capital assets	89,393	85,749	2,040	2,117	91,433	87,866
Total Assets	\$ 104,792	\$ 102,610	\$ 2,532	\$ 2,488	\$ 107,324	\$ 105,098
Long-term debt outstanding	\$ 7,408	\$ 9,016	\$ 58	\$ 79	\$ 7,466	\$ 9,095
Other liabilities	3,816	3,105	242	242	4,058	3,347
Total Liabilities	\$ 11,224	\$ 12,121	\$ 300	\$ 321	\$ 11,524	\$ 12,442
net of debt	\$ 82,402	\$ 77,782	\$ 2,031	\$ 2,114	\$ 84,433	\$ 79,896
Restricted	1,526	2,949	-	-	1,526	2,949
Unrestricted	9,640	9,758	201	53	9,841	9,811
Total Net Assets	\$ 93,568	\$ 90,489	\$ 2,232	\$ 2,167	\$ 95,800	\$ 92,656

Table 2
Changes in Net Assets
(in Thousands)

	Governmental Activities		Business-Type Activities		Total Primary Government	
	2008	2007	2008	2007	2008	2007
Fees, fines, charges, and other	\$ 2,538	\$ 2,786	\$ 3,235	\$ 2,564	\$ 5,773	\$ 5,350
Operating grants and contributions	8,098	5,664	-	-	8,098	5,664
Capital grants and contributions	2,296	7,835	-	-	2,296	7,835
Property taxes	6,733	6,136	-	-	6,733	6,136
Other taxes	2,020	1,933	-	-	2,020	1,933
Unrestricted grants and contributions	1,532	1,891	-	-	1,532	1,891
Investment earnings	342	655	6	7	348	662
Gain on sale of capital asset	31	-	-	-	31	-
Miscellaneous	110	171	8	6	118	177
Total Revenues	\$ 23,700	\$ 27,071	\$ 3,249	\$ 2,577	\$ 26,949	\$ 29,648

(Unaudited)

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	<u>Governmental Activities</u>		<u>Business-Type Activities</u>		<u>Total Primary Government</u>	
	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>	<u>2008</u>	<u>2007</u>
Expenses						
General government	\$ 4,064	\$ 3,808	\$ -	\$ -	\$ 4,064	\$ 3,808
Public safety	3,608	3,546	-	-	3,608	3,546
Culture and recreation	878	788	-	-	878	788
Highways and streets	4,320	7,229	-	-	4,320	7,229
Human services	3,448	3,592	3,184	3,081	6,632	6,673
Health	2,711	457	-	-	2,711	457
Sanitation	311	283	-	-	311	283
Conservation of natural resources	861	890	-	-	861	890
Economic development	79	48	-	-	79	48
Interest	341	409	-	-	341	409
Total Expenses	<u>\$ 20,621</u>	<u>\$ 21,050</u>	<u>\$ 3,184</u>	<u>\$ 3,081</u>	<u>\$ 23,805</u>	<u>\$ 24,131</u>
Increase (Decrease) in Net Assets	\$ 3,079	\$ 6,021	\$ 65	\$ (504)	\$ 3,144	\$ 5,517
Net Assets, January 1	<u>90,489</u>	<u>84,468</u>	<u>2,167</u>	<u>2,671</u>	<u>92,656</u>	<u>87,139</u>
Net Assets, December 31	<u>\$ 93,568</u>	<u>\$ 90,489</u>	<u>\$ 2,232</u>	<u>\$ 2,167</u>	<u>\$ 95,800</u>	<u>\$ 92,656</u>

Operating grants increased by \$2,433,535 primarily due to an increase in the Region III adult mental health initiative funding which increased by \$1,877,841 over the previous year. Lake County is the host county for these funds which benefit all of the counties in Region III. Prior to 2008, the state reported these revenues and expenditures at the state level, but is now running the revenues and expenditures through the host county. This change is also reflected in health expenditures which are \$2,253,998 higher than the previous year.

Capital grants decreased by \$5,538,845 due to less construction activity in 2008 compared to 2007. This decrease is also reflected in lower expenditures in highways and streets of \$2,908,981.

Governmental Activities

The cost of all governmental activities this year was \$20,621,605. However, as shown in the Statement of Activities, the amount that our taxpayers ultimately financed for these activities through County taxes and other general revenues was only \$7,689,785, because some of the cost was paid by those who directly benefited from the programs (\$2,537,803) or by other governments and organizations that subsidized certain programs with grants and contributions (\$10,394,017).

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		Net Cost of Services	
	2008	2007	2008	2007
Highways and streets	\$ 4,320	\$ 7,229	\$ 112	\$ (2,705)
General government	4,064	3,808	2,120	1,897
Public safety	3,608	3,546	2,498	2,725
Human services	3,448	3,592	1,749	1,655
Health	2,711	-	327	-
Conservation of natural resources	-	890	-	(125)
All others	2,470	1,985	884	1,317
Total	<u>\$ 20,621</u>	<u>\$ 21,050</u>	<u>\$ 7,690</u>	<u>\$ 4,764</u>

General Fund Budgetary Highlights

Over the course of the year, the County Board reviews the County's General Fund budget and may make budget amendments. These budget amendments fall into three categories: new information changing original budget estimations, greater than anticipated revenues or costs, and final agreement reached on employee contracts. The General Fund budget was not amended significantly in 2008.

In the General Fund, the actual charges to appropriations (expenditures) were \$461,287 greater than the final budget amounts. Unbudgeted expenditures included \$271,352 of unbudgeted homeland security grant expenditures and \$339,307 of unbudgeted trail expenditures.

Resources available for appropriation were also above the final budgeted amount by \$930,869. This was primarily due to greater than expected collections in intergovernmental revenues.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At the end of 2008, the County had \$91,433,076 invested in a broad range of capital assets, including land, buildings, highways and streets, and equipment. (See Table 4.)

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

	Governmental Activities		Business-Type Activities		Totals	
	2008	2007	2008	2007	2008	2007
Land	\$ 3,899	\$ 3,899	\$ 15	\$ 15	\$ 3,914	\$ 3,914
Buildings and improvements	11,801	12,218	1,907	1,984	13,708	14,202
Machinery, vehicles, furniture, and equipment	1,800	1,986	118	118	1,918	2,104
Infrastructure	71,893	67,646	-	-	71,893	67,646
Totals	<u>\$ 89,393</u>	<u>\$ 85,749</u>	<u>\$ 2,040</u>	<u>\$ 2,117</u>	<u>\$ 91,433</u>	<u>\$ 87,866</u>

The County's fiscal year 2009 capital budget calls for it to spend another \$2.7 million for capital projects, \$207 thousand for miscellaneous improvements at various buildings, and \$2.45 million for road construction. The road construction will be funded by state-aid construction funds.

Debt

At year-end, the County had \$5,755,455 in bonds and notes outstanding versus \$7,014,163 last year--a decrease of 18 percent--as shown in Table 5. Capital leases payable decreased by \$146,190.

Table 5
Outstanding Debt at Year-End
(in Thousands)

	Governmental Activities		Business-Type Activities		Totals	
	2008	2007	2008	2007	2008	2007
General obligation bonds	\$ 5,540	\$ 6,620	\$ -	\$ -	\$ 5,540	\$ 6,620
Notes payable	215	394	-	-	215	394
Capital leases	1,956	2,103	9	3	1,965	2,106
Compensated absences	971	1,346	84	112	1,055	1,458
Net other postemployment benefits	68	-	-	-	68	-
Total	<u>\$ 8,750</u>	<u>\$ 10,463</u>	<u>\$ 93</u>	<u>\$ 115</u>	<u>\$ 8,843</u>	<u>\$ 10,578</u>

The state limits the amount of net debt that the County can issue to three percent of the market value of all taxable property in the County. The County's outstanding net debt is below this state-imposed limit.

Other obligations include accrued vacation pay, sick leave payable and net other postemployment benefits. More detailed information about the County's long-term liabilities is presented in the notes to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The County's elected and appointed officials considered many factors when setting the fiscal year 2009 budget, tax rates, and fees that will be charged for the business-type activities.

- County General Fund expenditures for 2009 are budgeted to increase four percent over 2008.
- Property tax levies have increased 9.15 percent for 2009 and include a loss of \$185,000 in state aid for property tax reduction.

CONTACTING LAKE COUNTY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the County's finances and to show the County's accountability for the money it receives. If you have questions about this report, or need additional financial information, contact the County Auditor/Treasurer Steven McMahon, Lake County Courthouse, 601 - 3rd Avenue, Two Harbors, Minnesota 55616.

BASIC FINANCIAL STATEMENTS

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GOVERNMENT-WIDE FINANCIAL STATEMENTS

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

EXHIBIT 1

**STATEMENT OF NET ASSETS
DECEMBER 31, 2008**

	Primary Government			Housing and Redevelopment Authority Component Unit
	Governmental Activities	Business-Type Activities	Total	
<u>Assets</u>				
Cash and pooled investments	\$ 9,319,847	\$ 500	\$ 9,320,347	\$ 329,768
Receivables - net	4,553,370	527,255	5,080,625	163,137
Due from component unit	1,005,331	-	1,005,331	-
Due from primary government	-	-	-	5,912
Inventories	475,094	11,104	486,198	-
Prepaid items	-	49,489	49,489	-
Restricted assets				
Cash and pooled investments	-	5,770	5,770	83,732
Internal balances	-	(102,435)	(102,435)	-
Deferred charges	45,726	-	45,726	-
Capital assets				
Non-depreciable capital assets	3,898,859	15,000	3,913,859	-
Depreciable capital assets - net of accumulated depreciation	85,494,255	2,024,962	87,519,217	1,334,956
Total Assets	\$ 104,792,482	\$ 2,531,645	\$ 107,324,127	\$ 1,917,505
<u>Liabilities</u>				
Accounts payable and other current liabilities	\$ 1,457,232	\$ 201,553	\$ 1,658,785	\$ 11,175
Accrued interest payable	104,660	-	104,660	2,700
Due to component unit	5,912	-	5,912	-
Advance from other governments	905,925	-	905,925	-
Due to primary government	-	-	-	1,005,331
Unearned revenue	-	-	-	51
Payable from restricted assets				
Due to residents	-	5,770	5,770	-
Customer deposits payable	-	-	-	14,534
Long-term liabilities				
Due within one year	1,342,088	34,395	1,376,483	29,000
Due in more than one year	7,408,398	58,326	7,466,724	885,193
Total Liabilities	\$ 11,224,215	\$ 300,044	\$ 11,524,259	\$ 1,947,984

The notes to the financial statements are an integral part of this statement.

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

***EXHIBIT 1
(Continued)***

**STATEMENT OF NET ASSETS
DECEMBER 31, 2008**

	Primary Government			Housing and Redevelopment Authority Component Unit
	Governmental Activities	Business-Type Activities	Total	
<u>Net Assets</u>				
Invested in capital assets - net of related debt	\$ 82,402,415	\$ 2,030,618	\$ 84,433,033	\$ 420,763
Restricted for				
General government	314,230	-	314,230	-
Public safety	238,419	-	238,419	-
Highways and streets	78,164	-	78,164	-
Conservation of natural resources	391,114	-	391,114	-
Debt service	504,144	-	504,144	69,198
Unrestricted	9,639,781	200,983	9,840,764	(520,440)
Total Net Assets	\$ 93,568,267	\$ 2,231,601	\$ 95,799,868	\$ (30,479)

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

**STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2008**

	<u>Expenses</u>	<u>Fees, Charges, Fines, and Other</u>	<u>Program Revenues Operating Grants and Contributions</u>
<u>Functions/Programs</u>			
Primary government			
Governmental activities			
General government	\$ 4,063,900	\$ 464,904	\$ 1,479,412
Public safety	3,608,125	194,252	915,670
Highways and streets	4,320,334	527,619	1,384,848
Sanitation	310,697	192,704	-
Human services	3,448,372	119,416	1,579,987
Health	2,711,206	175,887	2,208,352
Culture and recreation	878,619	843	451,962
Conservation of natural resources	860,905	859,112	77,468
Economic development	78,746	3,066	-
Interest	340,701	-	-
Total governmental activities	\$ 20,621,605	\$ 2,537,803	\$ 8,097,699
Business-type activities			
Nursing Home	3,184,399	3,235,296	-
Total Primary Government	\$ 23,806,004	\$ 5,773,099	\$ 8,097,699
Component unit			
Housing and Redevelopment Authority	\$ 603,285	\$ 161,022	\$ -

General Revenues

Property taxes
Mortgage registry and deed tax
Payments in lieu of tax
Tax increments
Taxes - other
Grants and contributions not restricted to specific programs
Unrestricted investment earnings
Gain on sale of capital assets
Miscellaneous

Total general revenues

Change in net assets

Net Assets - Beginning

Net Assets - Ending

EXHIBIT 2

Capital Grants and Contributions	Net (Expense) Revenue and Changes in Net Assets			Discretely Presented Component Unit
	Primary Government		Total	
	Governmental Activities	Business-Type Activities		
\$ -	\$ (2,119,584)	\$ -	\$ (2,119,584)	
-	(2,498,203)	-	(2,498,203)	
2,296,318	(111,549)	-	(111,549)	
-	(117,993)	-	(117,993)	
-	(1,748,969)	-	(1,748,969)	
-	(326,967)	-	(326,967)	
-	(425,814)	-	(425,814)	
-	75,675	-	75,675	
-	(75,680)	-	(75,680)	
-	(340,701)	-	(340,701)	
\$ 2,296,318	\$ (7,689,785)	\$ -	\$ (7,689,785)	
-	-	50,897	50,897	
\$ 2,296,318	\$ (7,689,785)	\$ 50,897	\$ (7,638,888)	
\$ -				\$ (442,263)
	\$ 6,732,957	\$ -	\$ 6,732,957	\$ 101,249
	14,469	-	14,469	-
	527,478	-	527,478	-
	233,420	-	233,420	205,519
	1,244,817	-	1,244,817	-
	1,532,129	-	1,532,129	85,271
	341,612	6,189	347,801	8,082
	31,162	-	31,162	-
	110,522	7,692	118,214	6,714
	\$ 10,768,566	\$ 13,881	\$ 10,782,447	\$ 406,835
	\$ 3,078,781	\$ 64,778	\$ 3,143,559	\$ (35,428)
	90,489,486	2,166,823	92,656,309	4,949
	\$ 93,568,267	\$ 2,231,601	\$ 95,799,868	\$ (30,479)

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FUND FINANCIAL STATEMENTS

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GOVERNMENTAL FUNDS

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

EXHIBIT 3

**BALANCE SHEET
GOVERNMENTAL FUNDS
DECEMBER 31, 2008**

	<u>General</u>	<u>Road and Bridge</u>	<u>Human Services</u>	<u>Forfeited Tax</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
<u>Assets</u>						
Cash and pooled investments	\$ 4,639,605	\$ 333,061	\$ 3,385,540	\$ 300,073	\$ 341,641	\$ 8,999,920
Escheat cash	36,538	-	-	-	-	36,538
Petty cash and change funds	1,300	1,000	1,000	50	-	3,350
Undistributed cash in agency funds	150,248	45,026	72,404	-	12,361	280,039
Taxes receivable						
Prior	249,062	81,174	126,229	-	17,682	474,147
Accounts receivable	19,152	17,006	41,209	659,989	231	737,587
Accrued interest receivable	61,092	-	-	-	-	61,092
Loans receivable	94,311	-	-	-	50,081	144,392
Due from other funds	197,561	37,193	-	141	58,875	293,770
Due from other governments	1,521,123	814,391	585,638	-	-	2,921,152
Due from component unit	-	-	-	-	1,005,331	1,005,331
Inventories	-	475,094	-	-	-	475,094
Leases receivable	215,000	-	-	-	-	215,000
Total Assets	\$ 7,184,992	\$ 1,803,945	\$ 4,212,020	\$ 960,253	\$ 1,486,202	\$ 15,647,412
<u>Liabilities and Fund Balances</u>						
Liabilities						
Accounts payable	\$ 52,906	\$ 59,579	\$ 133,525	\$ 12,591	\$ -	\$ 258,601
Escheat payable	36,538	-	-	-	-	36,538
Salaries payable	292,891	88,717	111,158	24,622	-	517,388
Contracts payable	-	308,541	-	-	-	308,541
Due to other funds	37,193	141	34,006	58,875	163,555	293,770
Due to other governments	43,332	7,218	181,363	173	104,078	336,164
Due to component unit	5,912	-	-	-	-	5,912
Deferred revenue - unavaiable	390,791	304,261	90,920	612,870	12,719	1,411,561
Advances from other governments	-	905,925	-	-	-	905,925
Total Liabilities	\$ 859,563	\$ 1,674,382	\$ 550,972	\$ 709,131	\$ 280,352	\$ 4,074,400

The notes to the financial statements are an integral part of this statement.

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

**EXHIBIT 3
(Continued)**

**BALANCE SHEET
GOVERNMENTAL FUNDS
DECEMBER 31, 2008**

	<u>General</u>	<u>Road and Bridge</u>	<u>Human Services</u>	<u>Forfeited Tax</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
<u>Liabilities and Fund Balances</u> (Continued)						
Fund Balances						
Reserved for						
Inventories	\$ -	\$ 475,094	\$ -	\$ -	\$ -	\$ 475,094
Capital projects	-	202,038	-	-	-	202,038
Election equipment	33,466	-	-	-	-	33,466
Loans receivable	94,311	-	-	-	50,081	144,392
Law library	34,514	-	-	-	-	34,514
Sheriff's contingency	5,000	-	-	-	-	5,000
Sheriff's forfeited property	72,454	-	-	-	-	72,454
Recorder's technology fund	136,933	-	-	-	-	136,933
Recorder's compliance fund	142,783	-	-	-	-	142,783
Enhanced 911	160,965	-	-	-	-	160,965
Debt service	-	504,144	-	-	-	504,144
Title III forests	391,114	-	-	-	-	391,114
Retired employees	-	36,344	-	-	-	36,344
Unreserved						
Designated for future expenditures	-	-	1,000,000	-	-	1,000,000
Undesignated	5,253,889	(1,088,057)	2,661,048	251,122	-	7,078,002
Unreserved, reported in nonmajor						
Special revenue funds	-	-	-	-	300,707	300,707
Debt service fund	-	-	-	-	855,062	855,062
Total Fund Balances	<u>\$ 6,325,429</u>	<u>\$ 129,563</u>	<u>\$ 3,661,048</u>	<u>\$ 251,122</u>	<u>\$ 1,205,850</u>	<u>\$ 11,573,012</u>
Total Liabilities and Fund Balances	<u>\$ 7,184,992</u>	<u>\$ 1,803,945</u>	<u>\$ 4,212,020</u>	<u>\$ 960,253</u>	<u>\$ 1,486,202</u>	<u>\$ 15,647,412</u>

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

EXHIBIT 4

**RECONCILIATION OF GOVERNMENTAL FUNDS BALANCE SHEET TO
THE GOVERNMENT-WIDE STATEMENT OF NET ASSETS--GOVERNMENTAL ACTIVITIES
DECEMBER 31, 2008**

Fund balances - total governmental funds (Exhibit 3)		\$ 11,573,012
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.		89,393,114
Other long-term assets are not available to pay for current period expenditures and, therefore, are deferred in the governmental funds.		1,411,561
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	\$ (5,540,000)	
Notes payable	(215,455)	
Capital leases payable	(1,956,593)	
Compensated absences	(970,639)	
Net other postemployment benefits payable	(67,799)	
Accrued interest payable	(104,660)	
Deferred debt issuance charges	45,726	(8,809,420)
	<hr/>	<hr/>
Net Assets of Governmental Activities (Exhibit 1)		<u><u>\$ 93,568,267</u></u>

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

EXHIBIT 5

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2008**

	<u>General</u>	<u>Road and Bridge</u>	<u>Human Services</u>	<u>Forfeited Tax</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Revenues						
Taxes	\$ 4,436,497	\$ 1,415,924	\$ 1,752,874	\$ -	\$ 516,956	\$ 8,122,251
Licenses and permits	31,208	-	-	754	75	32,037
Intergovernmental	3,623,295	5,965,723	4,356,763	23,709	181,191	14,150,681
Charges for services	628,054	495,696	254,746	74,842	-	1,453,338
Fines and forfeits	10,437	-	-	-	-	10,437
Gifts and contributions	270	-	-	-	-	270
Investment earnings	329,848	3,627	-	-	8,137	341,612
Miscellaneous	188,348	31,923	40,557	646,677	163,492	1,070,997
Total Revenues	\$ 9,247,957	\$ 7,912,893	\$ 6,404,940	\$ 745,982	\$ 869,851	\$ 25,181,623
Expenditures						
Current						
General government	\$ 3,888,051	\$ -	\$ -	\$ -	\$ 7,596	\$ 3,895,647
Public safety	3,501,483	-	-	-	114,478	3,615,961
Highways and streets	-	8,863,748	-	-	-	8,863,748
Sanitation	305,805	-	-	-	-	305,805
Human services	-	-	3,344,451	-	-	3,344,451
Health	-	-	2,709,087	-	-	2,709,087
Culture and recreation	716,894	-	-	-	-	716,894
Conservation of natural resources	183,853	-	-	659,602	6,284	849,739
Economic development	48,746	-	-	-	30,000	78,746
Capital outlay	-	-	-	15,381	-	15,381
Debt service						
Principal	22,428	501,574	-	-	922,946	1,446,948
Interest	-	86,813	-	-	254,329	341,142
Miscellaneous	-	403	-	-	2,965	3,368
Total Expenditures	\$ 8,667,260	\$ 9,452,538	\$ 6,053,538	\$ 674,983	\$ 1,338,598	\$ 26,186,917
Excess of Revenues Over (Under) Expenditures	\$ 580,697	\$ (1,539,645)	\$ 351,402	\$ 70,999	\$ (468,747)	\$ (1,005,294)

The notes to the financial statements are an integral part of this statement.

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

**EXHIBIT 5
(Continued)**

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2008**

	<u>General</u>	<u>Road and Bridge</u>	<u>Human Services</u>	<u>Forfeited Tax</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Other Financing Sources						
(Uses)						
Transfers in	\$ -	\$ -	\$ -	\$ -	\$ 58,875	\$ 58,875
Capital lease purchase	-	42,050	-	-	-	42,050
Transfers out	-	-	-	(58,875)	-	(58,875)
Total Other Financing Sources (Uses)	\$ -	\$ 42,050	\$ -	\$ (58,875)	\$ 58,875	\$ 42,050
Net Change in Fund Balances	\$ 580,697	\$ (1,497,595)	\$ 351,402	\$ 12,124	\$ (409,872)	\$ (963,244)
Fund Balances - January 1	5,744,732	1,435,297	3,309,646	238,998	1,615,722	12,344,395
Increase (decrease) in reserved for inventories	-	191,861	-	-	-	191,861
Fund Balances - December 31	<u>\$ 6,325,429</u>	<u>\$ 129,563</u>	<u>\$ 3,661,048</u>	<u>\$ 251,122</u>	<u>\$ 1,205,850</u>	<u>\$ 11,573,012</u>

**LAKE COUNTY
TWO HARBORS, 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, 2008**

Net change in fund balances - total governmental funds (Exhibit 5) **\$ (963,244)**

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 revenue between the fund statements and the statement of activities is the increase or decrease in revenue deferred as unavailable.

Deferred revenue - December 31	\$ 1,411,561	
Deferred revenue - January 1	<u>(2,921,040)</u>	(1,509,479)

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, the gain or loss on the disposal of capital assets is reported; in the governmental funds, proceeds from the sale increase financial resources. The difference is the net book value of assets sold.

Expenditures for general capital assets and infrastructure	\$ 6,304,967	
Net book value of assets sold	(1,458)	
Current year depreciation	<u>(2,659,798)</u>	3,643,711

Debt issuances provide current financial resources to governmental funds, but increase long-term liabilities in the statement of net assets. Debt repayment is an expenditure in funds, but a reduction of a liability in the statement of net assets.

Debt issued		
Capital lease		(42,050)

Principal repayments		
General obligation bonds	\$ 1,080,000	
Notes payable	178,708	
Capital lease	<u>188,240</u>	1,446,948

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	\$ 17,345	
Change in deferred bond issuance costs	(13,536)	
Change in compensated absences	375,024	
Change in other postemployment benefits	(67,799)	
Change in inventories	<u>191,861</u>	<u>502,895</u>

Change in Net Assets of Governmental Activities (Exhibit 2) **\$ 3,078,781**

PROPRIETARY FUND

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

EXHIBIT 7

**STATEMENT OF FUND NET ASSETS
PROPRIETARY FUND
NURSING HOME ENTERPRISE FUND
SEPTEMBER 30, 2008**

Assets

Current assets

Petty cash and change funds	\$ 500
Accounts receivable - net	527,255
Inventories	11,104
Prepaid items	49,489
Restricted cash, cash equivalents, and investments	
Resident trust funds	5,770

Total current assets	\$ 594,118
-----------------------------	-------------------

Noncurrent assets

Capital assets	
Nondepreciable	\$ 15,000
Depreciable	4,324,708
Less: accumulated depreciation	(2,299,746)

Capital assets - net of accumulated depreciation	\$ 2,039,962
---	---------------------

Total Assets	\$ 2,634,080
---------------------	---------------------

Liabilities

Current liabilities

Accounts payable	\$ 93,643
Salaries payable	56,431
Accrued vacation payable	51,479
Compensated absences payable - current	32,417
Due to other funds	102,435
Capital leases payable - current	1,978

Total current liabilities	\$ 338,383
----------------------------------	-------------------

Current liabilities payable from restricted assets

Due to residents	\$ 5,770
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Noncurrent liabilities

Compensated absences payable - long-term	\$ 50,960
Capital leases payable - long-term	7,366

Total noncurrent liabilities	\$ 58,326
-------------------------------------	------------------

Total Liabilities	\$ 402,479
--------------------------	-------------------

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

***EXHIBIT 7
(Continued)***

**STATEMENT OF FUND NET ASSETS
PROPRIETARY FUND
NURSING HOME ENTERPRISE FUND
SEPTEMBER 30, 2008**

Net Assets

Invested in capital assets - net of related debt	\$ 2,030,618
Unrestricted	<u>200,983</u>
Total Net Assets	<u><u>\$ 2,231,601</u></u>

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

EXHIBIT 8

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
PROPRIETARY FUND
NURSING HOME ENTERPRISE FUND
FOR THE YEAR ENDED SEPTEMBER 30, 2008**

Operating Revenues	
Patient services revenues	\$ 3,050,571
Ancillary and other services	131,970
Miscellaneous	<u>52,755</u>
Total Operating Revenues	<u>\$ 3,235,296</u>
Operating Expenses	
Nursing services	\$ 1,250,945
Other care-related	94,266
Other services and charges	84,160
Dietary	349,979
Laundry	56,320
Housekeeping	71,338
Plant operations	167,611
Other property and related costs	176,535
Administration	346,175
Employee benefits	461,853
Depreciation	<u>124,647</u>
Total Operating Expenses	<u>\$ 3,183,829</u>
Operating Income (Loss)	<u>\$ 51,467</u>
Nonoperating Revenues (Expenses)	
Operating grants	\$ 7,692
Nursing home payment adjustment	6,189
Interest expense	<u>(570)</u>
Total Nonoperating Revenues (Expenses)	<u>\$ 13,311</u>
Change in Net Assets	\$ 64,778
Net Assets - October 1	<u>2,166,823</u>
Net Assets - September 30	<u><u>\$ 2,231,601</u></u>

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

EXHIBIT 9

**STATEMENT OF CASH FLOWS
PROPRIETARY FUND
NURSING HOME ENTERPRISE FUND
FOR THE YEAR ENDED SEPTEMBER 30, 2008**

Cash Flows from Operating Activities	
Cash received from customers	\$ 2,949,983
Cash paid to suppliers	(784,634)
Cash payments to employees	<u>(2,182,475)</u>
Net cash provided by (used in) operating activities	<u>\$ (17,126)</u>
Cash Flows from Noncapital Financing Activities	
Nursing home payment adjustment received	\$ 6,189
Grant received	<u>7,692</u>
Net cash provided by (used in) noncapital financing activities	<u>\$ 13,881</u>
Cash Flows from Capital and Related Financing Activities	
Principal payments on capital lease	\$ (3,887)
Interest expense	(570)
Acquisition of capital assets	<u>(37,291)</u>
Net cash provided by (used in) capital and related financing activities	<u>\$ (41,748)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	<u>\$ (44,993)</u>
Cash and Cash Equivalents - October 1	<u>45,493</u>
Cash and Cash Equivalents - September 30	<u><u>\$ 500</u></u>
Reconciliation of operating income (loss) to net cash provided by (used in) operating activities	
Operating income (loss)	<u>\$ 51,467</u>
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities	
Depreciation	\$ 124,647
Changes in assets and liabilities	
(Increase) decrease in receivables	(285,313)
(Increase) decrease in inventories	2,136
(Increase) decrease in prepaid items	14,566
Increase (decrease) in accounts payable	(12,602)
Increase (decrease) in salaries payable	15,252
Increase (decrease) in compensated absences	(28,667)
Increase (decrease) in vacations payable	(1,047)
Increase (decrease) in due to other governments	<u>102,435</u>
Total adjustments	<u>\$ (68,593)</u>
Net Cash Provided by (Used in) Operating Activities	<u><u>\$ (17,126)</u></u>

The notes to the financial statements are an integral part of this statement.

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FIDUCIARY FUNDS

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

EXHIBIT 10

**FIDUCIARY FUNDS
STATEMENT OF FIDUCIARY NET ASSETS
DECEMBER 31, 2008**

	<u>Agency</u>
<u>Assets</u>	
Cash and pooled investments	<u><u>\$ 612,634</u></u>
<u>Liabilities</u>	
Accounts payable	\$ 217,836
Taxes collected in advance	12,916
Due to other governments	331,242
Customer deposits - current	<u>50,640</u>
Total Liabilities	<u><u>\$ 612,634</u></u>

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

**NOTES TO THE FINANCIAL STATEMENTS
AS OF AND FOR THE YEAR ENDED DECEMBER 31, 2008**

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, 2008. The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (statements and interpretations). Governments are also required to follow the pronouncements of the Financial Accounting Standards Board (FASB) issued through November 30, 1989, (when applicable) that do not conflict with or contradict GASB pronouncements. Although the County has the option to apply FASB pronouncements issued after that date to its Nursing Home Enterprise Fund, the County has chosen not to do so. The more significant accounting policies established in GAAP and used by the County are discussed below.

A. Financial Reporting Entity

Lake County was established March 1, 1866, and is an organized county having the powers, duties, and privileges granted counties by Minn. Stat. ch. 373. The Lake County Nursing Home was established pursuant to Minn. Stat. §§ 376.55-.60. As required by accounting principles generally accepted in the United States of America, these financial statements present Lake County (primary government) and its component unit for which the County is financially accountable. The County is governed by a five-member Board of Commissioners elected from districts within the County. The Board is organized with a chair and vice chair elected at the annual meeting in January of each year.

Discretely Presented Component Unit

While part of the reporting entity, the discretely presented component unit is presented in a separate column in the government-wide financial statements to emphasize that it is legally separate from the County. The following component unit of Lake County is discretely presented:

<u>Component Unit</u>	<u>Component Unit Included in Reporting Entity Because</u>	<u>Separate Financial Statements</u>
Lake County Housing and Redevelopment Authority	County appoints members, and the Authority is a potential financial burden.	Lake County Housing and Redevelopment Authority P. O. Box 604 Two Harbors, Minnesota 55616

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

1. Summary of Significant Accounting Policies

A. Financial Reporting Entity

Discretely Presented Component Unit (Continued)

The Lake County Housing and Redevelopment Authority is governed by a five-member Board appointed by the Lake County Board of Commissioners. The Lake County HRA has all of the powers and duties of a county housing and redevelopment authority under the provisions of Minn. Stat. §§ 469.001-.047.

Joint Ventures

The County participates in several joint ventures described in Note 6.D. The County also participates in jointly-governed organizations described in Note 6.E.

B. Basic Financial Statements

1. Government-Wide Statements

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

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

1. Summary of Significant Accounting Policies

B. Basic Financial Statements

1. Government-Wide Statements (Continued)

The statement of activities demonstrates the degree to which the direct expenses of each function of the County's governmental activities and different business-type activities are offset by program revenue. 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. Revenue not classified as program revenue, including all taxes, are presented as general revenue.

2. Fund Financial Statements

The fund financial statements provide information about the County's funds, including its fiduciary funds. Separate statements for each fund category--governmental, proprietary, and fiduciary--are presented. The emphasis of governmental and proprietary fund financial statements is on major individual governmental and enterprise funds, with each displayed as separate columns in the fund financial statements. All remaining governmental and enterprise funds are aggregated and reported as nonmajor funds.

The County reports the following major governmental funds:

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

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

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

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

1. Summary of Significant Accounting Policies

B. Basic Financial Statements

2. Fund Financial Statements (Continued)

The Forfeited Tax Special Revenue Fund is used to account for revenues from the sale or lease of lands forfeited to the State of Minnesota and for revenues dedicated for use in memorial forests and various land and timber projects.

The County reports the following major enterprise fund:

The Nursing Home Enterprise Fund is used to account for the operations of the County Nursing Home.

Additionally, the County reports the following fund type:

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

C. Measurement Focus and Basis of Accounting

The government-wide and proprietary 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 revenue in the year for which they are levied. Shared revenues are generally recognized in the period the appropriation goes into effect. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Lake County considers all revenue as available if collected within 90 days after the end of the current period, except for taxes, which have a 60-day accrual 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

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

1. Summary of Significant Accounting Policies

C. Measurement Focus and Basis of Accounting (Continued)

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.

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

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 deposit or effectively withdraw 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 Auditor/Treasurer for the purpose of increasing earnings through investment activities. Pooled and fund investments are reported at their fair value at December 31, 2008, based on market prices. Pursuant to Minn. Stat. § 385.07, investment earnings on cash and pooled investments are credited to the General Fund. Other funds received investment earnings based on other state statutes, grant agreements, contracts, and bond covenants. Pooled investment earnings for 2008 were \$341,612.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Assets or Equity

2. Deposits and Investments (Continued)

Lake County invests in an external investment pool, the Minnesota Association of Governments Investing for Counties (MAGIC) Fund, which is created under a joint powers agreement pursuant to Minn. Stat. § 471.59. The MAGIC Fund is not registered with the Securities and Exchange Commission (SEC), but does operate in a manner consistent with Rule 2a-7 prescribed by the SEC pursuant to the Investment Company Act of 1940 (17 C.F.R. § 270.2a-7). Therefore, the fair value of the County's position in the pool is the same as the value of the pool shares.

3. Receivables and Payables

Activity between funds representative of lending/borrowing arrangements outstanding at the end of the fiscal year is referred to as either "due to/from other funds" (the current portion of interfund loans) or "advances to/from other funds" (the 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." At December 31, 2008, the government-wide financial statements show an internal balance outstanding of \$(102,435). This balance was a payable from the Lake County Nursing Home to the General Fund at September 30, 2008, which is the fiscal year-end of the Nursing Home. As of December 31, 2008, the date at which the General Fund is reported, there were no payables between the Nursing Home and the General Fund.

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.

Loans receivable consist of outstanding loans to individuals for shoreline erosion projects and loans to individuals for economic development.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

1. Summary of Significant Accounting Policies

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

4. Inventories and Prepaid Items

The Road and Bridge Special Revenue Fund inventory is valued at cost using the average cost method and consists of expendable supplies and parts held for consumption and sand and gravel stockpiles. 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.

Inventories in the Nursing Home Enterprise Fund are valued at cost on a first-in, first-out method and consist of nursing home supplies held for consumption. Inventoried items are recorded as an expense when used.

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.

5. Restricted Assets

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

6. Capital Assets

Capital assets, which include property, plant, equipment, and infrastructure assets (for example, roads, bridges, and similar items), are reported in the applicable governmental or business-type activities column in the government-wide financial statements. Capital assets are defined by the government as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Assets or Equity

6. Capital Assets (Continued)

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

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

Property, plant, and equipment of the primary government, as well as the component unit, are depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Buildings	5 - 50
Improvements other than buildings	8 - 20
Public domain infrastructure	50 - 75
Furniture, equipment, and vehicles	5 - 20

7. Compensated Absences

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

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Assets or Equity

7. Compensated Absences (Continued)

Lake County's employees (except for Highway department and supervisory employees) participate in a post-retirement health savings plan administered by the Minnesota State Retirement System. At retirement, depending on the employee's years of service, he or she is issued a lump sum payout of either 10 or 20 percent of the vested sick leave as well as two to three years of insurance coverage. The lump sum payouts are paid directly into the post-retirement health savings plan.

8. Deferred Revenue

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

9. Long-Term Obligations

In the government-wide and 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 straight-line 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.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

1. Summary of Significant Accounting Policies

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

10. Fund Equity

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

11. Use of Estimates

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

2. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

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

Primary government	
Cash and pooled investments	\$ 9,320,347
Restricted cash and pooled investments	5,770
Component unit	
Cash and pooled investments	329,768
Restricted cash and pooled investments	83,732
Fiduciary funds	
Cash and pooled investments	612,634
	<hr/>
Total Cash and Investments	\$ 10,352,251
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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

2. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments (Continued)

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 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 standby letters of credit issued by the Federal Home Loan Bank; and certificates of deposit. Minnesota statutes require that securities pledged as collateral be held in safekeeping in a restricted account at the Federal Reserve Bank or in an account at a trust department of a commercial bank or other financial institution not owned or controlled by the financial institution furnishing the collateral.

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a financial institution failure, the 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, 2008, the primary government's bank balances of \$1,672,420 were not exposed to custodial credit risk.

The Lake County Housing and Redevelopment Authority component unit's book balance of \$413,500 was exposed to custodial credit risk as follows:

Uninsured and uncollateralized Component unit	<u>\$ 61,861</u>
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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

2. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments (Continued)

b. Investments

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

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

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

2. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

b. Investments (Continued)

Interest Rate Risk

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

Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of an 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 in the possession of an outside party. The County does not have an investment policy for custodial credit risk. All of Lake County's investments in negotiable certificates of deposit and government securities are held by the counterparty to the transactions and, therefore, are subject to custodial credit risk. A portion of these investments are insured by Securities Investor Protection Corporation (SIPC) insurance or excess SIPC insurance and are not subject to custodial credit risk.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

2. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

b. Investments

Custodial Credit Risk (Continued)

Negotiable certificates of deposit	
Insured	\$ 1,782,115
Uninsured, held by counterparty	49,907
Government securities	
Insured	1,756,742
Uninsured, held by counterparty	491,481

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 policy of the County to diversify investments to avoid risk and, also, for cash-flow purposes.

The following table presents the County's deposit and investment balances at December 31, 2008, 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% of Portfolio	Maturity Date	
U.S. government agency securities					
Federal National Mortgage Association	AAA	Moody's		12/24/2010	\$ 202,200
Federal National Mortgage Association	AAA	Moody's		05/05/2011	250,440
Federal National Mortgage Association	AAA	Moody's		01/16/2014	300,828
Federal National Mortgage Association	AAA	Moody's		08/06/2015	250,665
Federal National Mortgage Association	N/R	N/A		02/01/2019	223,910
Total Federal National Mortgage Association			13.2%		\$ 1,228,043
Federal Home Loan Bank Bonds	AAA	Moody's	<5%	06/10/2015	\$ 254,545
Government National Mortgage Association Note	N/R	N/A	<5%	02/15/2019	\$ 14,293
Federal Home Loan Mortgage Corporation	AAA	Moody's		05/20/2011	\$ 200,664
Federal Home Loan Mortgage Corporation	AAA	Moody's		02/12/2016	250,333
Federal Home Loan Mortgage Corporation	AAA	Moody's		01/15/2018	300,345
Total Federal Home Loan Mortgage Corporation			8.1%		\$ 751,342

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

2. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments (Continued)

Investment Type	Credit Risk		Concentration Risk	Interest Rate Risk	Carrying (Fair) Value
	Credit Rating	Rating Agency	Over 5% of Portfolio	Maturity Date	
Investment pools/mutual funds					
MAGIC Fund	N/R	N/A	54.0%	N/A	\$ 5,035,934
Wells Fargo Government Money Market	N/R	N/A	<5%	N/A	215,439
Total investment pools/mutual funds					\$ 5,251,373
Negotiable certificates of deposit					
Bank North	N/A	N/A	<5%	02/20/2009	\$ 96,268
Nicolet National Bank	N/A	N/A	<5%	03/05/2009	96,335
Hanmi Bank	N/A	N/A	<5%	03/10/2010	96,448
Wright Express Finl	N/A	N/A	<5%	03/18/2009	96,416
GMAC Bank	N/A	N/A	<5%	03/19/2010	96,925
Capital One Natl Assn	N/A	N/A	<5%	03/19/2009	96,441
National Bank Comm	N/A	N/A	<5%	03/31/2009	96,425
National City Bank	N/A	N/A	<5%	04/23/2009	96,485
Columbus Bk & Tr Co	N/A	N/A	<5%	05/07/2009	96,499
Infibank NA	N/A	N/A	<5%	05/14/2009	96,522
Merrick Bank Corp	N/A	N/A	<5%	06/12/2009	96,000
Wachovia Bank FSB	N/A	N/A	<5%	07/02/2009	96,000
Capmark Bank	N/A	N/A	<5%	07/09/2009	96,749
Washington Mutual	N/A	N/A	<5%	07/10/2009	96,000
Marshall & Ilsley Bk	N/A	N/A	<5%	07/16/2010	96,686
Southwest Bank	N/A	N/A	<5%	07/16/2010	96,686
GE Capital Finl Inc	N/A	N/A	<5%	08/20/2010	95,905
BMW Bank NA	N/A	N/A	<5%	12/01/2010	96,680
American Express Bank	N/A	N/A	<5%	12/03/2010	96,552
Total negotiable certificates of deposit					\$ 1,832,022
Total investments					\$ 9,331,618
Deposits - primary government					560,975
Deposits - component unit					413,500
Petty cash					3,850
Resident trust funds					5,770
Escheat cash					36,538
Total Cash and Investments					\$ 10,352,251

N/A - Not Applicable

N/R - Not Rated

<5% - Concentration is less than 5% of investments

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

2. Detailed Notes on All Funds

A. Assets (Continued)

2. Receivables

Receivables as of December 31, 2008, for the County's governmental activities and business-type activities are as follows:

	Total Receivables	Amounts Not Scheduled for Collection During the Subsequent Year
Governmental Activities		
Taxes	\$ 474,147	\$ -
Due from other governments	2,921,152	-
Accounts	737,587	-
Interest	61,092	-
Loans receivable	144,392	109,803
Leases receivable	215,000	-
	<u>\$ 4,553,370</u>	<u>\$ 109,803</u>
Total Governmental Activities		
	<u>\$ 4,553,370</u>	<u>\$ 109,803</u>
Business-Type Activities		
Accounts	\$ 527,255	\$ -
	<u>\$ 527,255</u>	<u>\$ -</u>

3. Capital Assets

Capital asset activity for the year ended December 31, 2008, was as follows:

Governmental Activities

	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets not depreciated				
Land	\$ 3,898,859	\$ -	\$ -	\$ 3,898,859
Capital assets depreciated				
Buildings	\$ 16,097,783	\$ 27,796	\$ -	\$ 16,125,579
Improvements other than buildings	461,478	-	-	461,478
Machinery, furniture, and equipment	7,909,414	326,352	232,560	8,003,206
Infrastructure	82,669,706	5,950,819	-	88,620,525
	<u>\$ 107,138,381</u>	<u>\$ 6,304,967</u>	<u>\$ 232,560</u>	<u>\$ 113,210,788</u>
Total capital assets depreciated				
	<u>\$ 107,138,381</u>	<u>\$ 6,304,967</u>	<u>\$ 232,560</u>	<u>\$ 113,210,788</u>

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

2. Detailed Notes on All Funds

A. Assets

3. Capital Assets

Governmental Activities (Continued)

	Beginning Balance	Increase	Decrease	Ending Balance
Less: accumulated depreciation for				
Buildings	\$ 4,070,929	\$ 426,466	\$ -	\$ 4,497,395
Improvements other than buildings	269,814	18,632	-	288,446
Machinery, furniture, and equipment	5,923,208	511,373	231,102	6,203,479
Infrastructure	15,023,886	1,703,327	-	16,727,213
Total accumulated depreciation	\$ 25,287,837	\$ 2,659,798	\$ 231,102	\$ 27,716,533
Total capital assets depreciated, net	\$ 81,850,544	\$ 3,645,169	\$ 1,458	\$ 85,494,255
Governmental Activities Capital Assets, Net	<u>\$ 85,749,403</u>	<u>\$ 3,645,169</u>	<u>\$ 1,458</u>	<u>\$ 89,393,114</u>

Business-Type Activities

	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets not depreciated				
Land	\$ 15,000	\$ -	\$ -	\$ 15,000
Capital assets depreciated				
Land improvements	\$ 91,983	\$ -	\$ -	\$ 91,983
Buildings	3,531,543	19,410	-	3,550,953
Machinery, furniture, and equipment	653,144	28,628	-	681,772
Total capital assets depreciated	\$ 4,276,670	\$ 48,038	\$ -	\$ 4,324,708
Less: accumulated depreciation for				
Land improvements	\$ 80,017	\$ 2,851	\$ -	\$ 82,868
Buildings	1,560,104	92,893	-	1,652,997
Machinery, furniture, and equipment	534,978	28,903	-	563,881
Total accumulated depreciation	\$ 2,175,099	\$ 124,647	\$ -	\$ 2,299,746
Total capital assets depreciated, net	\$ 2,101,571	\$ (76,609)	\$ -	\$ 2,024,962
Business-Type Activities Capital Assets, Net	<u>\$ 2,116,571</u>	<u>\$ (76,609)</u>	<u>\$ -</u>	<u>\$ 2,039,962</u>

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

2. 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	\$ 248,521
Public safety	134,958
Highways and streets, including depreciation of infrastructure assets	1,964,490
Human services	96,266
Sanitation	3,614
Culture and recreation	184,949
Conservation of natural resources	<u>27,000</u>
Total Depreciation Expense - Governmental Activities	<u>\$ 2,659,798</u>
Business-Type Activities	
Nursing home	<u>\$ 124,647</u>

B. Interfund Receivables, Payables, and Transfers

1. Due To/From Other Funds

The composition of interfund balances as of December 31, 2008, is as follows:

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>	<u>Purpose</u>
General	Debt Service	\$ 163,555	Temporary loan, deficit cash balance
	Human Services	<u>34,006</u>	Reimbursement for services, correction of receipting error
Total due to General Fund		\$ 197,561	
Road and Bridge	General	37,193	Reimbursement for services
Forfeited Tax	Road and Bridge	141	Pit reforestation
Resource Development	Forfeited Tax	<u>58,875</u>	Forfeited tax apportionment
Total Due To/From Other Funds		<u>\$ 293,770</u>	

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

2. Detailed Notes on All Funds

B. Interfund Receivables, Payables, and Transfers

1. Due To/From Other Funds (Continued)

The Nursing Home Enterprise Fund reports \$102,435 due to the General Fund. That balance was payable at the Nursing Home Enterprise Fund's year-end of September 30, 2008, but paid at December 31, 2008.

2. Due To/From Primary Government and Component Units

<u>Receivable Entity</u>	<u>Payable Entity</u>	<u>Amount</u>	<u>Purpose</u>
Component Unit - Lake County Housing and Redevelopment Authority	Primary Government - Debt Service Fund	<u>\$ 5,912</u>	Bond administration fees
Primary Government - Debt Service	Component Unit - Lake County Housing and Redevelopment Authority	<u>\$ 1,005,331</u>	Shortfalls in tax increment collections funded by primary government

3. Interfund Transfers

Interfund transfers for the year ended December 31, 2008, consisted of the following:

Transfers to Resource Development Special Revenue Fund from Forfeited Tax Special Revenue Fund	<u>\$ 58,875</u>	Distribute net proceeds
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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

2. Detailed Notes on All Funds (Continued)

C. Liabilities

1. Payables

Payables at December 31, 2008, were as follows:

	<u>Governmental Activities</u>	<u>Business-Type Activities</u>
Accounts payable	\$ 258,601	\$ 93,643
Escheat property payable	36,538	-
Salaries payable	517,388	56,431
Accrued vacation payable	-	51,479
Contracts payable	308,541	-
Due to other governments	<u>336,164</u>	<u>-</u>
Total Payables	<u>\$ 1,457,232</u>	<u>\$ 201,553</u>

2. Leases

Business-Type Activities

Capital Leases

In January 2008, the Lake County Nursing Home entered into a lease agreement to finance a copier. The lease runs for five years with interest at 6.35 percent and monthly payments of \$210. At lease expiration, the copier will become the Nursing Home's property and, as such, it has been recorded as a capital asset. The copier is carried at a cost of \$10,748.

See Notes 2.C.3. and 2.C.4. for information on the lease payable and debt service requirements.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

2. Detailed Notes on All Funds

C. Liabilities (Continued)

3. Long-Term Debt

Governmental Activities

Type of Indebtedness	Final Maturity	Installment Amounts	Interest Rate (%)	Original Issue Amount	Outstanding Balance December 31, 2008
General obligation bonds					
G.O. Refunding Bonds, Series 2003B	2009	\$130,000 - \$150,000	2.50 - 3.00	\$ 700,000	\$ 150,000
G.O. Tax Increment Refunding Bonds, Series 2003C	2009	\$250,000 - \$275,000	2.75 - 4.00	1,045,000	275,000
G.O. Capital Improvement Bonds, Series 2005A	2019	\$155,000 - \$310,000	3.375 - 3.80	3,200,000	2,835,000
G.O. State-Aid Highway Bonds, Series 2005B	2013	\$455,000 - \$460,000	3.25 - 3.50	3,200,000	2,280,000
Total General Obligation Bonds				<u>\$ 8,145,000</u>	<u>\$ 5,540,000</u>
Other long-term debt					
General obligation revenue note	2012	\$20,304 - \$24,286	2.00	\$ 222,422	\$ 94,311
Promissory note (Allete)	2010	\$58,915	5.00	282,072	121,144
Capital lease	2021	\$146,667	5.375	2,200,000	1,906,667
Capital lease	2009	\$27,686 \$7,500 - \$19,579	6.25	49,024	7,876
Capital lease	2011		4.90	42,050	42,050
Total Other Long-Term Debt				<u>\$ 2,795,568</u>	<u>\$ 2,172,048</u>

Business-Type Activities - Lake County Nursing Home

Type of Indebtedness	Final Maturity	Installment Amounts	Interest Rate (%)	Original Issue Amount	Outstanding Balance September 30, 2008
Capital lease	2013	\$2,520	6.35	<u>\$ 10,748</u>	<u>\$ 9,344</u>

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

2. Detailed Notes on All Funds

C. Liabilities (Continued)

4. Debt Service Requirements

Debt service requirements at December 31, 2008, were as follows:

Governmental Activities

Year Ending December 31	General Obligation Bonds		Other Long-Term Debt	
	Principal	Interest	Principal	Interest
2009	\$ 1,100,000	\$ 177,247	\$ 242,089	\$ 113,757
2010	675,000	146,458	249,463	102,500
2011	685,000	122,888	189,544	89,274
2012	690,000	99,048	170,952	79,198
2013	700,000	74,710	146,667	70,950
2014 - 2018	1,380,000	190,581	733,335	236,500
2019 - 2021	310,000	5,890	439,998	47,300
Total	<u>\$ 5,540,000</u>	<u>\$ 816,822</u>	<u>\$ 2,172,048</u>	<u>\$ 739,479</u>

Business-Type Activities - Lake County Nursing Home

Year Ending September 30	Capital Leases	
	Principal	Interest
2009	\$ 1,978	\$ 536
2010	2,107	407
2011	2,245	269
2012	2,392	123
2013	622	7
Total	<u>\$ 9,344</u>	<u>\$ 1,342</u>

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

2. Detailed Notes on All Funds

C. Liabilities (Continued)

5. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2008, was as follows:

Governmental Activities

	Beginning Balance	Additions	Deductions	Ending Balance	Due Within One Year
General obligation bonds	\$ 6,620,000	\$ -	\$ 1,080,000	\$ 5,540,000	\$ 1,100,000
Notes payable	394,163	-	178,708	215,455	81,973
Total bonds and notes payable	\$ 7,014,163	\$ -	\$ 1,258,708	\$ 5,755,455	\$ 1,181,973
Capital lease payable	2,102,783	42,050	188,240	1,956,593	160,115
Compensated absences	1,345,663	395,100	770,124	970,639	-
Net other postemployment benefits	-	67,799	-	67,799	-
Governmental Activities Long-Term Liabilities	<u>\$ 10,462,609</u>	<u>\$ 504,949</u>	<u>\$ 2,217,072</u>	<u>\$ 8,750,486</u>	<u>\$ 1,342,088</u>

Business-Type Activities - Lake County Nursing Home

	Beginning Balance	Additions	Deductions	Ending Balance	Due Within One Year
Capital lease payable	\$ 2,484	\$ 10,748	\$ 3,888	\$ 9,344	\$ 1,978
Compensated absences	112,044	-	28,667	83,377	32,417
Business-Type Activities Long-Term Liabilities	<u>\$ 114,528</u>	<u>\$ 10,748</u>	<u>\$ 32,555</u>	<u>\$ 92,721</u>	<u>\$ 34,395</u>

The County has covenanted to provide ongoing disclosure of certain annual financial information and operating data with respect to the County, including audited financial statements of the County.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

3. Employee Retirement Systems and Pension Plans

A. Defined Benefit Plan

Plan Description

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

Public Employees Retirement Fund members belong to either the Coordinated Plan or the Basic Plan. Coordinated Plan members are covered by Social Security, and Basic Plan members are not. All new members must participate in the Coordinated Plan. All police officers, firefighters, and peace officers who qualify for membership by statute are covered by the Public Employees Police and Fire Fund. Members who are employed in a county correctional institution as a correctional guard or officer, a joint jailer/dispatcher, or as a supervisor of correctional guards or officers or of joint jailer/dispatchers and are directly responsible for the direct security, custody, and control of the county correctional institution and its inmates, are covered by the Public Employees Correctional Fund.

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 defined 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

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

3. Employee Retirement Systems and Pension Plans

A. Defined Benefit Plan

Plan Description (Continued)

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 hired prior to July 1, 1989, 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. Normal retirement age is 55 for Public Employees Police and Fire Fund members and Public Employees Correctional Fund members and either 65 or 66 (depending on date hired) for Public Employees Retirement Fund members. A reduced retirement annuity is also available to eligible members seeking early retirement.

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

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. 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 9.1 and 6.0 percent, respectively, of their annual covered salary. Public Employees Police and Fire Fund members were required to contribute 8.6 percent of their annual

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

3. Employee Retirement Systems and Pension Plans

A. Defined Benefit Plan

Funding Policy (Continued)

covered salary in 2008. That rate increased to 9.4 percent in 2009. 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 2008 and 2009:

	<u>2008</u>	<u>2009</u>
Public Employees Retirement Fund		
Basic Plan members	11.78%	11.78%
Coordinated Plan members	6.50	6.75
Public Employees Police and Fire Fund	12.90	14.10
Public Employees Correctional Fund	8.75	8.75

The County's contributions for the years ending December 31, 2008, 2007, and 2006, for the Public Employees Retirement Fund, the Public Employees Police and Fire Fund, and the Public Employees Correctional Fund were:

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Public Employees Retirement Fund	\$ 414,745	\$ 396,937	\$ 370,507
Public Employees Police and Fire Fund	120,403	115,311	94,744
Public Employees Correctional Fund	41,819	44,581	36,401

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

B. Defined Contribution Plan

Three County Commissioners are covered by the Public Employees Defined Contribution Plan, a multiple-employer, deferred compensation plan administered by PERA in accordance with Minn. Stat. ch. 353D. The plan is established and administered in accordance with Minn. Stat. ch. 353D, which may be amended by the State Legislature. 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.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

3. Employee Retirement Systems and Pension Plans

B. Defined Contribution Plan (Continued)

Plan benefits depend solely on amounts contributed to the plan plus investment earnings, less administrative expenses. Minn. Stat. § 353D.03 specifies plan provisions, including the employee and employer contribution rates for those qualified personnel who elect to participate. An eligible elected official who decides to participate contributes 5.0 percent of salary, which is matched by the employer. Employees may elect to make member contributions in an amount not to exceed the employer share. Employee and employer contributions are combined and used to purchase shares in one or more of the seven accounts of the Minnesota Supplemental Investment Fund. For administering the plan, PERA receives 2.0 percent of employer contributions and 0.25 percent of the assets in each member account annually.

Total contributions by dollar amount and percentage of covered payroll made by the County during the year ended December 31, 2008, were:

	<u>Employee</u>	<u>Employer</u>
Contribution amount	\$ 9,399	\$ 9,399
Percentage of covered payroll	5%	5%

Required contribution rates were 5.0 percent.

4. Postemployment Benefits

In 2008, Lake County prospectively implemented the requirements of a new accounting statement, Government Accounting Standards Board (GASB) Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*.

A. Plan Description and Funding Policy

Lake County explicitly subsidizes the cost of retiree health insurance coverage for certain retired employees through a sick leave reserve program under a single-employer self-insured plan. Highway Department employees with at least 10 years of service who are eligible to receive a retirement benefit from PERA are eligible for up to two years of health insurance premiums paid by the County at the single rate. Supervisory employees with at least 15 years of service and Highway Department employees with 20 or more years of service are eligible for up to three years of health insurance premiums. At retirement, each eligible employee's sick leave hours are converted to a

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

4. Postemployment Benefits

A. Plan Description and Funding Policy (Continued)

dollar amount using the employee's hourly pay rate at retirement. The period of time for which the employee may receive the paid health insurance benefit is limited to the dollar value of the employee's accumulated sick leave at retirement. As of December 31, 2008, there were four retirees using their sick leave balances for insurance premiums.

Active employees who retire from the County when eligible to receive a retirement benefit from PERA, who do not qualify for the aforementioned benefits and do not participate in any other health benefits program providing similar coverage, will be eligible to continue coverage with respect to both themselves and their eligible dependents under the County's health benefits program. These retirees are required to pay 100 percent of the total premium cost. Since the premium is a blended rate determined on the entire active and retiree population, the retirees are receiving an implicit rate subsidy. As of December 31, 2008, 13 retirees were receiving health benefits from the County's health plan. The authority to provide these benefits is established in Minn. Stat. § 471.61, subd. 2a.

The cost of other postemployment benefits is funded on a "pay-as-you-go" method.

B. Annual OPEB Cost and Net OPEB Obligation

The County's annual other postemployment benefit (OPEB) cost is calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years. The following table shows the components of the County's annual OPEB cost for 2008, the amount actually contributed to the plan, and changes in the County's net OPEB obligation:

ARC	\$	86,583
Interest on net OPEB obligation		-
Adjustment to ARC		-
		<hr/>
Annual OPEB cost	\$	86,583
Contributions during the year		(18,784)
		<hr/>
Increase in net OPEB obligation	\$	67,799
Net OPEB, beginning of year		-
		<hr/>
Net OPEB, end of year	\$	67,799
		<hr/>

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

4. Postemployment Benefits

B. Annual OPEB Cost and Net OPEB Obligation (Continued)

The County's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for 2008 were as follows:

	Year Ended December 31, 2008
Percentage of annual OPEB cost contributed	21.7%
Annual OPEB cost	\$ 86,583
Employer contributions	(18,784)
Net Increase in Net OPEB Obligation	<u>\$ 67,799</u>

C. Funding Status and Funding Progress

The actuarial accrued liability for benefits at December 31, 2008, is \$618,083. The County currently has no assets that have been irrevocably deposited in a trust for future health benefits, thus the entire amount is unfunded. The covered payroll (annual payroll of active employees covered by the plan) is \$5,722,969. The ratio of the unfunded actuarially accrued liabilities (UAAL) to covered payroll is 10.8 percent.

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and healthcare cost trends. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The Schedule of Funding Progress, presented as required supplementary information following the notes to the financial statements, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Projections of benefits for financial reporting purposes are based on the substantive plan (as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation. The actuarial methods and assumptions used include techniques that are designed to reduce the effect of short-term volatility in actuarial accrued liabilities, consistent with the long-term perspective of the calculations.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

4. Postemployment Benefits

C. Funding Status and Funding Progress (Continued)

In the January 1, 2008, actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions included a 4.5 percent discount rate, which is based on the estimated long-term investment yield on the general assets of the County. The annual healthcare cost trend rate is 9.0 percent initially, reduced incrementally to an ultimate rate of 5.0 percent after eight years. The unfunded actuarial accrued liability is being amortized as a level dollar amount over 30 years.

5. Postemployment Health Care Plans

A. MSRS Health Care Savings Plan

All Lake County employees (except for Highway Department employees and supervisory employees) are eligible to participate in a Health Care Savings Plan (HCSP) administered by the Minnesota State Retirement System (MSRS). The plan is authorized under Minn. Stat. § 352.98, and through an Internal Revenue Service (IRS) private letter ruling establishing the HCSP as a tax-exempt benefit as of July 29, 2002. The plan is open to any active public employee in Minnesota if they are covered under certain public service retirement plans.

Under the terms of the HCSP, employees are allowed to save money, tax-free, to use upon termination of employment to pay for eligible health care expenses. The IRS private letter ruling requires mandatory participation of all employees in each bargaining unit in order to gain tax-free benefits. Allowable amounts deposited into individual accounts must be negotiated by each individual bargaining unit and the employer. The plan must be written into the collective bargaining agreement or a Memo of Understanding. For those employees not covered by a bargaining unit, amounts to be deposited into individual accounts must be agreed to by the employer and included in a written personnel policy.

Under Lake County's plan, both unionized and non-represented employees are required to contribute, at retirement, a lump sum of 10 or 20 percent of their eligible unused sick time plus the value of 24 or 36 months of health insurance premiums into their HCSP account, depending on the years of service.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

5. Postemployment Health Care Plans (Continued)

B. VEBA Plan

Effective 2008, the Lake County Board of Commissioners approved a Voluntary Employees' Beneficiary Association (VEBA) plan for funding employee health benefits as authorized under Sections 501(c)(9) and 213(d) of the IRS code for members of the Sheriff's Deputy Union and for non-represented employees. The VEBA plan is a health reimbursement plan providing for individual employer funded accounts that can be used to help pay eligible medical expenses incurred by participating employees. The plan is used in combination with a high deductible health plan. Funding is provided through pre-tax contributions from Lake County on employee health care elections.

In 2008, the maximum County contribution for active employees is \$1,950 for employees with single coverage and \$3,770 for employees with family coverage. Any balance remaining in an employee's account at year-end rolls over into the subsequent year. Upon retirement, any balance remaining in the VEBA account may be used to pay medical expenses.

Eligibility requirements include:

- be an active employee or retiree of a public entity,
- active employees must have a high deductible health plan, and
- be a member of a bargaining unit that has approved the VEBA plan.

6. Summary of Significant Contingencies and Other Items

A. Risk Management

The County is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; injuries to employees; or natural disasters. To manage its workers' compensation and property and casualty risks, 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 dental coverage and participates in a health insurance pool for employee health coverage. For other risks, the County carries commercial insurance. The County retains risk for the deductible portions of the insurance policies. The

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

6. Summary of Significant Contingencies and Other Items

A. Risk Management (Continued)

amounts of these deductibles are considered immaterial to the financial statements. 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 \$410,000 per claim in 2008 and \$430,000 in 2009. Should the MCIT Workers' Compensation Division liabilities exceed assets, MCIT may assess the County in a method and amount to be determined by MCIT.

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

The North East Service Cooperative (NESC) is a joint powers entity which sponsors a plan to provide group employee health benefits to its participating members. All members pool premiums and losses; however, a particular member may receive increases or decreases depending on a good or bad year of claims experience. Premiums are determined annually by the NESC and are based partially on the experience of the County and partially on the experience of the group. The NESC solicits proposals from carriers and negotiates the contracts.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

6. Summary of Significant Contingencies and Other Items

A. Risk Management (Continued)

The County retains the risk of loss from claims related to employee dental. The County has contracted with Delta Dental to administer the County's dental claims. The County provides dental coverage to permanent full-time employees based on negotiated union contracts to cover a portion of the dental claims. Claims are recognized as they are paid. The amount of claims incurred at the balance sheet date which have not been accrued in the financial statements is immaterial.

	Year Ended December 31	
	2008	2007
Unpaid claims, beginning of fiscal year	\$ -	\$ -
Incurred claims (including Incurred But Not Reported)	113,865	109,648
Claims payments	(113,865)	(109,648)
Unpaid Claims, End of Fiscal Year	\$ -	\$ -

B. 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.

C. Other Commitments

Lake County has entered into a joint powers agreement with the Town of Silver Creek to assist the Town in financing a wastewater collection, treatment, and disposal system in the Castle Danger area. The County has agreed to contribute \$65,586 per year through the year 2017 to help finance this project. The total amount to be contributed is \$1,035,000, of which \$484,688 has been paid through December 31, 2008. The

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

6. Summary of Significant Contingencies and Other Items

C. Other Commitments (Continued)

outstanding commitment at December 31, 2008, is \$550,312. The agreement may be terminated by the mutual agreement of the two parties. This amount has not been recorded as a liability in Lake County's financial statements.

D. Joint Ventures

Arrowhead Regional Corrections

The County, in a joint powers agreement pursuant to Minn. Stat. § 471.59, participates with Carlton, Cook, Koochiching, and St. Louis Counties in the Arrowhead Regional Corrections Board, which was established pursuant to the Community Corrections Act, Minn. Stat. §§ 401.01-.16.

The Arrowhead Regional Corrections Board comprises three major divisions: juvenile institutional services, adult institutional services, and court and field services. These divisions are composed of the five participating counties' probation departments, the Arrowhead Juvenile Detention Center, and the Northeast Regional Corrections Center.

Arrowhead Regional Corrections is governed by an eight-member Board, composed of one member appointed from each of the participating counties' Boards of Commissioners, except for St. Louis County, which has three members from its Board. In addition, the right to have an additional member is annually rotated among Carlton, Cook, Koochiching, and Lake Counties.

Arrowhead Regional Corrections is financed through state grants and contributions from the participating counties. During 2007 (the most recent information available), County contributions were in the following proportion:

Carlton County	9.53%
Cook County	1.52
Koochiching County	2.75
Lake County	2.28
St. Louis County	<u>83.92</u>
Total	<u>100.00%</u>

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

6. Summary of Significant Contingencies and Other Items

D. Joint Ventures

Arrowhead Regional Corrections (Continued)

Below is a summary of the financial information from Arrowhead Regional Corrections' government-wide statements for December 31, 2007 (the most recent information available):

Total Assets	\$ 12,819,588
Total Liabilities	5,417,642
Total Net Assets	7,401,946
Total Revenues	21,415,725
Total Expenses	20,476,511
Change in Net Assets	939,214

Lake County provided \$269,200 in funding during 2008. Separate financial information can be obtained from:

Arrowhead Regional Corrections
St. Louis County Courthouse
100 North 5th Avenue West
Room 319
Duluth, Minnesota 55802

Community Health Board

Carlton, Cook, Lake, and St. Louis Counties entered into a joint powers agreement creating and operating the Carlton, Cook, Lake, and St. Louis County Community Health Board. This agreement was entered into January 1, 1977, and is established pursuant to Minn. Stat. § 471.59.

The Community Health Board is composed of nine members. The Carlton, Cook, and Lake County Boards of Commissioners each appoint two members; the St. Louis County Board of Commissioners appoints three members. Financing is obtained through federal and state grants. Lake County provided no funding to this organization in 2008.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

6. Summary of Significant Contingencies and Other Items

D. Joint Ventures

Community Health Board (Continued)

At December 31, 2007 (the most recent information available), the Community Health Board's summary of financial information was:

Total Assets	\$ 1,311,645
Total Liabilities	1,154,632
Total Net Assets	157,013
Total Revenues	3,742,318
Total Expenses	3,716,572
Change in Net Assets	25,746

Separate financial information can be obtained from:

Carlton, Cook, Lake, and St. Louis Counties
Community Health Board
404 West Superior Street, Suite 220
Duluth, Minnesota 55802

Northeast Minnesota Office of Job Training

Aitkin, Carlton, Cook, Itasca, Koochiching, Lake, and St. Louis Counties (excluding the City of Duluth) entered into a joint powers agreement pursuant to Minn. Stat. § 471.59 for the purpose of developing and implementing a private and public job training program. The United States Congress, through the Job Training Partnership Act of 1982, authorized states to establish "service delivery areas" to provide programs to achieve full employment through the use of grants. The counties identified above are defined as such a service delivery area, and the Northeast Minnesota Office of Job Training is designated as the grant recipient and administrator for such service delivery area. Lake County is not a funding mechanism for this organization.

The governing body is composed of seven members, one from the Board of Commissioners of each of the participating counties.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

6. Summary of Significant Contingencies and Other Items

D. Joint Ventures

Northeast Minnesota Office of Job Training (Continued)

A summary of the financial information of the Northeast Minnesota Office of Job Training's government-wide statements for June 30, 2008, was:

Total Assets	\$ 2,697,187
Total Liabilities	1,317,583
Total Net Assets	1,379,604
Total Revenues	5,034,686
Total Expenses	5,160,410
Change in Net Assets	(125,724)

Separate financial information can be obtained from:

Northeast Minnesota Office of Job Training
820 North Ninth Street
Suite 210
Virginia, Minnesota 55792

Minnesota Counties Information Systems

The Counties of Aitkin, Carlton, Cass, Chippewa, Cook, Crow Wing, Dodge, Itasca, Koochiching, Lac qui Parle, Lake, Sherburne, and St. Louis entered into a joint powers agreement, pursuant to Minn. Stat. § 471.59, creating and operating Minnesota Counties Information Systems (MCIS). MCIS operates and maintains data processing facilities and management information systems for the benefit of members of this agreement.

MCIS is governed by a 13-member board. Each participating county appoints a member. Financing is obtained through user charges to the members. Cass County is the fiscal agent for MCIS.

Each county's share of the assets and liabilities cannot be accurately determined since it will depend on the number of counties that are members when the agreement is dissolved.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

6. Summary of Significant Contingencies and Other Items

D. Joint Ventures

Minnesota Counties Information Systems (Continued)

A summary of the financial information of MCIS at December 31, 2006 (the most recent information available), was:

Total Assets	\$ 785,330
Total Liabilities	202,814
Total Net Assets	582,516
Total Revenues	2,387,269
Total Expenses	2,195,143
Change in Net Assets	192,126

Separate financial information can be obtained from:

Minnesota Counties Information Systems
413 Southeast 7th Avenue
Grand Rapids, Minnesota 55744

Northern Counties Land Use Board

The Northern Counties Land Use Board was established through a joint powers agreement, pursuant to Minn. Stat. § 471.59, for the purpose of helping to formulate land use plans for the protection, sustainable use, and development of lands and natural resources.

The joint powers are the Counties of Aitkin, Cook, Koochiching, Lake, Lake of the Woods, Marshall, Pennington, Roseau, and St. Louis. Three elected County Commissioners from St. Louis County and two from each of the other counties make up the membership of the Board. St. Louis County handles all of the financial transactions for this organization through its Northern Counties Land Use Board Agency Fund.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

6. Summary of Significant Contingencies and Other Items

D. Joint Ventures

Northern Counties Land Use Board (Continued)

A summary of the financial statements at December 31, 2006 (the most recent information available), is shown below:

Total Assets	\$ 75,537
Total Liabilities	20,061
Total Net Assets	55,476
Total Revenues	23,750
Total Expenses	7,780
Change in Net Assets	15,970

Lake County made contributions of \$5,000 in 2008 to the Northern Counties Land Use Board.

Separate financial information can be obtained from:

Northern Counties Land Use Board
St. Louis County Courthouse
100 N. 5th Avenue West, #214
Duluth, Minnesota 55802

North Shore Collaborative

The North Shore Collaborative was established in 1995 pursuant to Minn. Stat. § 124D.23. The Collaborative includes Lake County, Cook County, Independent School District 381, Independent School District 166, and the Grand Portage Reservation. The purpose of the Collaborative is to form a coalition of agencies, schools, and communities along the North Shore that will systematically address the mental health and other needs of the whole person for all children and youth; ensure their graduation from high school; and assist them in becoming healthy, happy, productive citizens.

Control of the North Shore Collaborative is vested in a Board of Directors. Lake County has three members on the Board. Financing is provided by state and federal grants, appropriations from Collaborative members, and miscellaneous revenues. Lake

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

6. Summary of Significant Contingencies and Other Items

D. Joint Ventures

North Shore Collaborative (Continued)

County is the fiscal agent for the Collaborative and handles all of the financial transactions for the organization. Financial information for the Collaborative for the fiscal year ended December 31, 2008, is as follows:

Assets	\$ 217,836
Liabilities	\$ 217,836

Arrowhead Health Alliance

Carlton, Cook, Koochiching, and Lake Counties entered into a joint powers agreement, pursuant to Minn. Stat. §§ 471.59 and 256B.692, for the purpose of organizing, governing, planning, and administering a county-based purchasing entity to participate in prepaid healthcare programs through the Minnesota Department of Human Services and the federal Centers for Medicare and Medicaid Services.

Control of the Arrowhead Health Alliance is vested in a Board of Directors composed of one representative from each of the member counties. Carlton County is the fiscal agent for the Arrowhead Health Alliance.

Lake County contributed \$78,697 in start-up funds to the Arrowhead Health Alliance in 2007. The County provided no further funding in 2008.

E. Jointly-Governed Organizations

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

The North Shore Management Board provides Lake Superior Shoreline planning for Cook, Lake, and St. Louis Counties; the Cities of Beaver Bay, Grand Marais, Silver Bay, and Two Harbors; and the Towns of Duluth and Lakewood. The County provided \$2,500 in funding to the North Shore Management Board for 2007.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

6. Summary of Significant Contingencies and Other Items

E. Jointly-Governed Organizations (Continued)

The St. Louis and Lake Counties Regional Railroad Authority operates a tourism train within the counties. Lake County did not provide any funding to the Regional Railroad Authority in 2008.

F. Related-Party Transactions - Lake County Housing and Redevelopment Authority

The Lake County Housing and Redevelopment Authority is a discretely presented component unit of Lake County. The following are related-party transactions:

SEGOG Property

In June 2005, the County entered into an agreement with the Authority to sell 70 acres of land to the Authority for \$250,000. The property will be used for housing development to meet the County's housing needs and to assist in fostering economic development in the County. The purchase price of \$250,000 will be paid to the County as individual lots are sold in the development. This agreement has not been finalized as of December 31, 2008, and no cash payments have been made.

Tax Increment Shortfalls

The Authority's tax increment revenues have not been sufficient to cover bond payments on the Cove Point and Superior Shores tax increment bonds. Lake County has made the bond payments on these bond issues; however, the Lake County Housing and Redevelopment Authority remains obligated to Lake County for these shortfalls. A receivable has been set up on the County's financial statements in the amount of \$1,005,331.

G. Tax-Forfeited Land

The County manages approximately 150,000 acres of state-owned, tax-forfeited land. This land generates revenues primarily from recreational land leases and land and timber sales. Land management costs, including forestry costs such as site preparation, seedlings, tree planting, and logging roads, are accounted for as current operating expenditures.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

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

H. Excess of Expenditures Over Appropriations

For the year ended December 31, 2008, expenditures exceeded appropriations in the following funds:

General Fund	\$ 461,287
Economic Development Special Revenue Fund	30,000
Unorganized Townships Special Revenue Fund	41,274

I. Subsequent Events

In 2009, the Lake County Board approved the issuance of a \$400,000 General Obligation Capital Note, Series 2009A, to be used for the purchase of a Road and Bridge plow truck, an ambulance, squad cars, and other vehicles.

7. Component Unit Disclosures

A. Summary of Significant Accounting Policies

In addition to those identified in Note 1, the County's discretely presented component unit, the Lake County Housing and Redevelopment Authority, has the following significant accounting policies.

Reporting Entity

The Lake County Housing and Redevelopment Authority was established June 13, 1984, and became active in 1986, having all the powers and duties of a county housing and redevelopment authority under the provisions of Minn. Stat. §§ 469.001 to 469.047. The Authority is governed by a five-member Board, appointed by the Lake County Board of Commissioners. The Board is organized with a chair, vice chair, secretary, and treasurer, elected annually.

Basis of Presentation

The Lake County Housing and Redevelopment Authority prepares separate financial statements.

The Authority reports a major governmental fund, the General Fund, and a major enterprise fund -- the Silverpointe Enterprise Fund.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

7. Component Unit Disclosures

A. Summary of Significant Accounting Policies (Continued)

Measurement Focus and Basis of Accounting

The government-wide and proprietary 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. The Lake County Housing and Redevelopment Authority considers all revenues as available if collected within 90 days after the end of the current period, except for taxes, which have a 60-day accrual period. Property and other taxes, licenses, and interest are all considered to be susceptible to accrual.

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

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

Cash and Cash Equivalents

The Authority's cash and cash equivalents consist of savings and checking accounts, cash on hand, and certificates of deposit, and do not include restricted accounts.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

7. Component Unit Disclosures

A. Summary of Significant Accounting Policies (Continued)

Receivables and Payables

All 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.”

Property taxes, including property taxes captured as tax increment, 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. The Authority approved an annual levy for operating purposes. Property taxes, including tax increment, are collected by Lake County. Unpaid taxes at December 31 become liens on the respective property and are classified in the financial statements as taxes receivable.

Restricted Assets

Certain funds of the Authority 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.

Capital Assets

Capital assets, which include land, buildings and structures, and equipment, are reported in the government-wide financial statements. Capital assets are defined by the government as assets with an initial, individual cost of more than \$1,000 and have an expected life of at least five years. Such assets are recorded at historical cost.

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.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

7. Component Unit Disclosures

A. Summary of Significant Accounting Policies

Capital Assets Continued)

Buildings and structures and equipment of the Authority are depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Buildings and structures	25 - 40
Equipment	7

Long-Term Obligations

In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the statement of net assets.

B. Detailed Notes on All Funds

1. Assets

Deposits and Investments

a. Deposits

The Authority's total cash and cash equivalents are reported as follows:

Government-wide statement of net assets	
Cash	\$ 329,768
Restricted cash and pooled investments	<u>83,732</u>
Total Cash	<u>\$ 413,500</u>

Minn. Stat. §§ 118A.02 and 118A.04 authorize the Authority to designate a depository for public funds and to invest in certificates of deposit. Minn. Stat. § 118A.03 requires that all Authority 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 at the close of the financial institution's banking day, not covered by insurance or bonds.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

7. Component Unit Disclosures

B. Detailed Notes on All Funds

1. Assets

Deposits and Investments

a. Deposits (Continued)

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

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a financial institution failure, the Authority’s deposits may not be returned to it. The Authority does not have a deposit policy for custodial credit risk. As of December 31, 2008, \$61,861 of the Authority’s book balance of \$413,500 was exposed to custodial credit risk. These deposits are held in a trust account by the property manager of the Authority’s rental units. The trust accounts are in the property manager’s name and hold funds for multiple properties managed by the company. The account balances of each property are tracked internally by the property manager. Although the accounts are covered by FDIC insurance, it is not possible to determine the amount of FDIC coverage that is available to cover each property’s individual balances.

Uninsured and uncollateralized	<u>\$ 61,861</u>
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b. Investments

Minn. Stat. §§ 118A.04 and 118A.05 generally authorize the same types of investments as available to the Authority as are available to the County and are detailed in Note 2.A.1.b.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

7. Component Unit Disclosures

B. Detailed Notes on All Funds

1. Assets

Deposits and Investments

b. Investments (Continued)

As of, and during the year ended December 31, 2008, the Authority did not own any investments that required disclosure regarding interest rate risk, credit risk, custodial credit risk, or concentration of credit risk.

Receivables

Receivables as of December 31, 2008, for the Authority's activities are as follows:

	Total Receivables	Amounts Not Scheduled for Collection During the Subsequent Year
Taxes	\$ 13,077	\$ -
Accounts receivable	119,594	-
Accrued interest	1,504	-
Due from other governments	10,000	-
Loans receivable	18,962	-
	<hr/>	<hr/>
Total Governmental Activities	\$ 163,137	\$ -

Loan Receivable

The Authority has a \$18,962 loan receivable from North Shore Business Enterprise Center, Inc., an unrelated non-profit organization.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

7. Component Unit Disclosures

B. Detailed Notes on All Funds

1. Assets (Continued)

Capital Assets

Capital asset activity for the year ended December 31, 2008, was as follows:

Business-Type Activities

	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets depreciated				
Buildings and structures	\$ 1,879,117	\$ -	\$ -	\$ 1,879,117
Equipment	3,911	-	-	3,911
Total capital assets depreciated	\$ 1,883,028	\$ -	\$ -	\$ 1,883,028
Less: accumulated depreciation for				
Buildings and structures	\$ 497,183	\$ 46,978	\$ -	\$ 544,161
Equipment	3,911	-	-	3,911
Total accumulated depreciation	\$ 501,094	\$ 46,978	\$ -	\$ 548,072
Business-Type Activities				
Capital Assets, Net	\$ 1,381,934	\$ (46,978)	\$ -	\$ 1,334,956

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

Business-Type Activities	
Senior housing	\$ 46,978

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

7. Component Unit Disclosures

B. Detailed Notes on All Funds (Continued)

2. Liabilities

Long-Term Debt

Business-Type Activities

<u>Type of Indebtedness</u>	<u>Final Maturity</u>	<u>Installment Amounts</u>	<u>Interest Rate (%)</u>	<u>Original Issue Amount</u>	<u>Outstanding Balance December 31, 2008</u>
1996 General Obligation Senior Housing Bonds	2028	Varies	3.92	\$ 1,160,642	\$ 914,193

Debt Service Requirements

Debt service requirements at December 31, 2008, were as follows:

Business-Type Activities

<u>Year Ending December 31</u>	<u>Revenue Bonds</u>	
	<u>Principal</u>	<u>Interest</u>
2009	\$ 29,000	\$ 45,045
2010	30,741	43,549
2011	32,313	41,977
2012	33,966	40,323
2013	35,704	38,586
2014 - 2018	207,864	163,585
2019 - 2023	266,764	104,685
2024 - 2028	277,841	30,337
Totals	\$ 914,193	\$ 508,087

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

7. Component Unit Disclosures

B. Detailed Notes on All Funds

2. Liabilities (Continued)

Changes in Long-Term Liabilities

Business-Type Activities

	Beginning Balance	Additions	Deductions	Ending Balance	Due Within One Year
Bonds payable					
General Obligation					
Senior Housing Bonds	\$ 941,508	\$ -	\$ 27,315	\$ 914,193	\$ 29,000

C. Summary of Significant Contingencies and Other Items

Tax Increment Financing Districts

The Authority administers the following tax increment financing district established pursuant to Minn. Stat. §§ 469.174 to 469.1791.

District Number 2

Blue Water/Superior Shores Project

The bonds for District No. 2 are general obligation bonds issued by Lake County and are included in the Lake County financial statements. The bonds do not constitute debt of the Authority. The County collects and pays the debt service payments pursuant to the amended Tax Increment Pledge Agreement, and the Authority recognizes the tax increment revenues and tax increment distributions to Lake County in its financial statements.

Risk Management

The Authority is exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; or natural disasters. To manage these risks, the Authority has joined the Minnesota Counties Insurance Trust (MCIT). The Authority retains risk for the deductible portions of the insurance policies. The amounts of these deductibles are considered immaterial to the financial statements. 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.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

7. Component Unit Disclosures

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

Tax Increment Assistance

The Lake County Housing and Redevelopment Authority is committed to provide tax increment assistance pursuant to the Northshore Business Enterprise Center development agreement. The assistance is provided in the form of an annual tax rebate to the developer. The annual tax rebate is contingent upon payment of annual property taxes by the developer. The assistance for the project is limited in amount based on both the scope of the project and the life of the tax increment district. The tax increment assistance does not result in debt proceeds and does not meet the definition of debt.

Conduit Debt Obligation

The Lake County Housing and Redevelopment Authority has issued the Health Care Facilities Revenue Bonds, Series 2000, originally issued for \$5,000,000 in May 2000, and refinanced in October 2003, for \$4,108,000, to provide financial assistance to First Plan of Minnesota to construct two medical clinics. The bonds are secured by the property financed through a loan agreement and are payable solely from the revenues of First Plan of Minnesota. Neither the Authority nor the state is obligated in any manner for repayment of the bonds. Accordingly, the bonds are not reported as a liability in the Authority's financial statements.

Financial Condition

The Authority's expenses, including required payments to Lake County pursuant to bond obligations, exceed current tax increment financing and other revenues. This continuing condition has resulted in a deficit balance of unrestricted net assets. Under current agreements and regulations, it appears the financial condition of the Authority will continue to deteriorate. The Authority's Board is looking into ways to improve its financial condition, including working with other similarly situated parties and the Minnesota Legislature to amend tax increment laws. The Authority is also in discussion with Lake County regarding its current obligations and the availability of alternative revenue sources.

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

7. Component Unit Disclosures

C. Summary of Significant Contingencies and Other Items

Financial Condition (Continued)

The ability of the Authority to continue as a going concern is dependent on its ability to generate additional revenues and/or limit its current debt obligations to provide sufficient net cash flow to fund its daily and long-term obligations. The financial statements do not include any adjustments that might be necessary if the Authority is unable to continue as a going concern.

Related-Party Transactions

The Lake County Housing and Redevelopment Authority related-party transactions are described in detail in Note 6.F.

D. Joint Ventures

In 2008, the Lake County Housing and Development Authority entered into a joint powers agreement with Cook County/Grand Marais Joint Economic Development Authority pursuant to Minn. Stat. § 471.59 for the purpose of preserving the existing housing market, encouraging new housing construction, and providing housing opportunities to the residents of Lake and Cook Counties. The power of each party will be exercised jointly under this agreement with the assistance of a housing coordinator to be retained by both parties. The Lake County Housing and Redevelopment Authority is the fiscal agent and all the financial information is included as part of the Lake County Housing and Redevelopment Authority's financial statements.

REQUIRED SUPPLEMENTARY INFORMATION

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Schedule 1

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2008**

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Revenues				
Taxes	\$ 5,142,670	\$ 5,142,670	\$ 4,436,497	\$ (706,173)
Licenses and permits	25,220	25,220	31,208	5,988
Intergovernmental	2,186,898	2,186,898	3,623,295	1,436,397
Charges for services	521,572	521,572	628,054	106,482
Fines and forfeits	1,500	1,500	10,437	8,937
Gifts and contributions	-	-	270	270
Investment earnings	353,000	353,000	329,848	(23,152)
Miscellaneous	86,228	86,228	188,348	102,120
Total Revenues	\$ 8,317,088	\$ 8,317,088	\$ 9,247,957	\$ 930,869
Expenditures				
Current				
General government				
Commissioners	\$ 401,521	\$ 401,521	\$ 423,799	\$ (22,278)
Courts	20,500	20,500	44,171	(23,671)
Law library	23,000	23,000	26,108	(3,108)
County administration	68,408	68,408	80,132	(11,724)
County auditor	522,692	522,692	497,224	25,468
County assessor	396,186	396,186	398,041	(1,855)
Elections	27,071	27,071	26,089	982
Accounting and auditing	54,000	54,000	72,545	(18,545)
Data processing	555,632	555,632	528,367	27,265
Personnel	163,151	163,151	245,648	(82,497)
Attorney	387,795	387,795	376,675	11,120
Recorder	244,021	244,021	219,531	24,490
Planning and zoning	229,559	229,559	238,600	(9,041)
Buildings and plant	733,351	733,351	613,385	119,966
Veterans service officer	58,999	58,999	59,146	(147)
Training	5,000	5,000	912	4,088
Motor pool	82,420	82,420	37,678	44,742
Total general government	\$ 3,973,306	\$ 3,973,306	\$ 3,888,051	\$ 85,255

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

**Schedule 1
(Continued)**

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2008**

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Expenditures				
Current (Continued)				
Public safety				
Sheriff	\$ 1,660,052	\$ 1,660,052	\$ 1,766,623	\$ (106,571)
Ambulance	43,533	43,533	47,308	(3,775)
Emergency services	132,931	132,931	110,655	22,276
Coroner	20,000	20,000	12,960	7,040
County jail	876,334	876,334	849,041	27,293
Community corrections	293,961	293,961	270,382	23,579
Sentence to serve	71,341	71,341	66,862	4,479
Emergency management	127,229	127,229	79,243	47,986
Civil defense	-	-	2,457	(2,457)
Other public safety	45,290	45,290	295,952	(250,662)
Total public safety	\$ 3,270,671	\$ 3,270,671	\$ 3,501,483	\$ (230,812)
Sanitation				
Solid waste	\$ 167,866	\$ 167,866	\$ 165,089	\$ 2,777
Recycling	133,994	133,994	118,279	15,715
Hazardous waste	27,400	27,400	22,437	4,963
Total sanitation	\$ 329,260	\$ 329,260	\$ 305,805	\$ 23,455
Culture and recreation				
Historical society	\$ 28,000	\$ 28,000	\$ 28,000	\$ -
Arenas	162,885	162,885	133,516	29,369
Humane society	3,500	3,500	3,500	-
Memorial Day observance	750	750	900	(150)
Recreation board	130,105	130,105	131,903	(1,798)
Trails	-	-	339,307	(339,307)
County/regional library	79,768	79,768	79,768	-
Total culture and recreation	\$ 405,008	\$ 405,008	\$ 716,894	\$ (311,886)
Conservation of natural resources				
County extension	\$ 99,539	\$ 99,539	\$ 99,395	\$ 144
Soil and water conservation	39,755	39,755	39,813	(58)
Agricultural society/County fair	16,807	16,807	16,017	790
Water planning	23,628	23,628	23,628	-
Wetland challenge	5,000	5,000	5,000	-
Total conservation of natural resources	\$ 184,729	\$ 184,729	\$ 183,853	\$ 876

The notes to the required supplementary information are an integral part of this schedule.

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

**Schedule 1
(Continued)**

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2008**

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Expenditures				
Current (Continued)				
Economic development				
Information centers	\$ 14,999	\$ 14,999	\$ 20,746	\$ (5,747)
Airports	28,000	28,000	28,000	-
Total economic development	\$ 42,999	\$ 42,999	\$ 48,746	\$ (5,747)
Debt service				
Principal	\$ -	\$ -	\$ 22,428	\$ (22,428)
Total Expenditures	\$ 8,205,973	\$ 8,205,973	\$ 8,667,260	\$ (461,287)
Excess of Revenues Over (Under)				
Expenditures	\$ 111,115	\$ 111,115	\$ 580,697	\$ 469,582
Other Financing Sources (Uses)				
Transfers out	68,409	68,409	-	(68,409)
Net Change in Fund Balance	\$ 179,524	\$ 179,524	\$ 580,697	\$ 401,173
Fund Balance - January 1	5,744,732	5,744,732	5,744,732	-
Fund Balance - December 31	\$ 5,924,256	\$ 5,924,256	\$ 6,325,429	\$ 401,173

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Schedule 2

**BUDGETARY COMPARISON SCHEDULE
ROAD AND BRIDGE SPECIAL REVENUE FUND
FOR THE YEAR ENDED DECEMBER 31, 2008**

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Revenues				
Taxes	\$ 1,554,627	\$ 1,554,627	\$ 1,415,924	\$ (138,703)
Intergovernmental	8,712,611	8,712,611	5,965,723	(2,746,888)
Charges for services	143,000	143,000	495,696	352,696
Investment earnings	-	-	3,627	3,627
Miscellaneous	37,500	37,500	31,923	(5,577)
Total Revenues	\$ 10,447,738	\$ 10,447,738	\$ 7,912,893	\$ (2,534,845)
Expenditures				
Current				
Highways and streets				
Administration	\$ 349,323	\$ 349,323	\$ 419,269	\$ (69,946)
Maintenance	1,653,422	1,653,422	1,740,361	(86,939)
Construction	6,972,010	6,972,010	5,790,172	1,181,838
Equipment maintenance and shop	841,864	841,864	913,946	(72,082)
Total highways and streets	\$ 9,816,619	\$ 9,816,619	\$ 8,863,748	\$ 952,871
Debt service				
Principal	\$ 460,000	\$ 460,000	\$ 501,574	\$ (41,574)
Interest	85,260	85,260	86,813	(1,553)
Administrative (fiscal) charges	-	-	403	(403)
Total debt service	\$ 545,260	\$ 545,260	\$ 588,790	\$ (43,530)
Total Expenditures	\$ 10,361,879	\$ 10,361,879	\$ 9,452,538	\$ 909,341
Excess of Revenues Over (Under)				
Expenditures	\$ 85,859	\$ 85,859	\$ (1,539,645)	\$ (1,625,504)
Other Financing Sources (Uses)				
Transfers in	\$ 5,000	\$ 5,000	\$ -	\$ (5,000)
Capital lease purchase	-	-	42,050	42,050
Total Other Financing Sources (Uses)	\$ 5,000	\$ 5,000	\$ 42,050	\$ 37,050
Net Change in Fund Balance	\$ 90,859	\$ 90,859	\$ (1,497,595)	\$ (1,588,454)
Fund Balance - January 1	1,435,297	1,435,297	1,435,297	-
Increase (decrease) in reserved for inventories	-	-	191,861	191,861
Fund Balance - December 31	\$ 1,526,156	\$ 1,526,156	\$ 129,563	\$ (1,396,593)

The notes to the required supplementary information are an integral part of this schedule.

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Schedule 3

**BUDGETARY COMPARISON SCHEDULE
HUMAN SERVICES SPECIAL REVENUE FUND
FOR THE YEAR ENDED DECEMBER 31, 2008**

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Revenues				
Taxes	\$ 2,080,644	\$ 2,080,644	\$ 1,752,874	\$ (327,770)
Intergovernmental	3,913,567	3,913,567	4,356,763	443,196
Charges for services	91,600	91,600	254,746	163,146
Miscellaneous	16,250	16,250	40,557	24,307
Total Revenues	\$ 6,102,061	\$ 6,102,061	\$ 6,404,940	\$ 302,879
Expenditures				
Current				
Human services				
Income maintenance	\$ 854,448	\$ 854,448	\$ 829,848	\$ 24,600
Social services	4,828,450	4,828,450	2,514,603	2,313,847
Total human services	\$ 5,682,898	\$ 5,682,898	\$ 3,344,451	\$ 2,338,447
Health				
Nursing service	\$ 53,440	\$ 53,440	\$ 45,691	\$ 7,749
Transportation	7,379	7,379	9,506	(2,127)
Environmental health	80,987	80,987	93,966	(12,979)
Mental health	-	-	2,282,588	(2,282,588)
Health education	277,357	277,357	277,336	21
Total health	\$ 419,163	\$ 419,163	\$ 2,709,087	\$ (2,289,924)
Total Expenditures	\$ 6,102,061	\$ 6,102,061	\$ 6,053,538	\$ 48,523
Net Change in Fund Balance	\$ -	\$ -	\$ 351,402	\$ 351,402
Fund Balance - January 1	3,309,646	3,309,646	3,309,646	-
Fund Balance - December 31	\$ 3,309,646	\$ 3,309,646	\$ 3,661,048	\$ 351,402

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Schedule 4

**BUDGETARY COMPARISON SCHEDULE
FORFEITED TAX SPECIAL REVENUE FUND
FOR THE YEAR ENDED DECEMBER 31, 2008**

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Revenues				
Licenses and permits	\$ 575	\$ 575	\$ 754	\$ 179
Intergovernmental	22,241	22,241	23,709	1,468
Charges for services	70,000	70,000	74,842	4,842
Miscellaneous	946,900	946,900	646,677	(300,223)
Total Revenues	\$ 1,039,716	\$ 1,039,716	\$ 745,982	\$ (293,734)
Expenditures				
Conservation of natural resources				
Current				
Land use	\$ 743,361	\$ 743,361	\$ 659,602	\$ 83,759
Capital outlay				
Conservation of natural resources	15,000	15,000	15,381	(381)
Total Expenditures	\$ 758,361	\$ 758,361	\$ 674,983	\$ 83,378
Excess of Revenues Over (Under)				
Expenditures	\$ 281,355	\$ 281,355	\$ 70,999	\$ (210,356)
Other Financing Sources (Uses)				
Transfers out	-	-	(58,875)	(58,875)
Net Change in Fund Balance	\$ 281,355	\$ 281,355	\$ 12,124	\$ (269,231)
Fund Balance - January 1	238,998	238,998	238,998	-
Fund Balance - December 31	\$ 520,353	\$ 520,353	\$ 251,122	\$ (269,231)

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Schedule 5

**SCHEDULE OF FUNDING PROGRESS
OTHER POSTEMPLOYMENT BENEFIT PLAN
DECEMBER 31, 2008**

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded Actuarial Accrued Liability (UAAL) (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as Percentage of Covered Payroll ((b - a)/c)
January 1, 2008	\$ -	\$ 618,083	\$ 618,083	0.00%	\$ 5,722,969	10.8%

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

**NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION
FOR THE YEAR ENDED DECEMBER 31, 2008**

1. Budgetary Information

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

In July of each year, all departments and agencies submit requests for appropriations to the County Auditor/Treasurer so that a budget can be prepared. Before September 15, the proposed budget is presented to the County Board for review. A final budget is adopted by the Board and certified to the Auditor/Treasurer by December 30.

The appropriated budget is prepared by fund, function, and department. The County's department heads may make transfers of appropriations within a department with County Board approval. Transfers of appropriations between departments also require approval of the County Board. The legal level of budgetary control (the level at which expenditures may not legally exceed appropriations) is the fund level.

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

2. Excess of Expenditures Over Appropriations

For the year ended December 31, 2008, expenditures exceeded appropriations in the following fund:

General Fund	\$ 461,287
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3. Schedule of Funding Progress - Other Postemployment Benefit Plan

Lake County currently has no assets that have been irrevocably deposited in a trust for future health benefits. Therefore, the actuarial value of assets is zero.

Lake County implemented Governmental Accounting Standards Board Statement 45 in the fiscal year ended December 31, 2008. Information for prior years is not available.

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SUPPLEMENTARY INFORMATION

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

NONMAJOR GOVERNMENTAL FUNDS

The Resource Development Special Revenue Fund is used to account for intergovernmental revenue used for resource development, forest management, game and fish habitat improvement, and recreational development and maintenance of County-administered natural resources land.

The Economic Development Special Revenue Fund is used to account for intergovernmental revenue used to finance various economic development projects.

The Unorganized Townships Special Revenue Fund is used to account for the activities of Unorganized Townships 1 and 2 related to fire protection and election services. Activities related to road maintenance in the unorganized townships are accounted for in the County's Road and Bridge Special Revenue Fund.

The Debt Service Fund is used to account for the accumulation of resources for and the payment of principal, interest, and related costs of general long-term debt.

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Statement 1

**COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS
DECEMBER 31, 2008**

	Special Revenue (Statement 3)	Debt Service	Total
<u>Assets</u>			
Cash and pooled investments	\$ 341,641	\$ -	\$ 341,641
Undistributed cash in agency funds	3,430	8,931	12,361
Taxes receivable			
Prior	3,214	14,468	17,682
Accounts receivable	231	-	231
Due from other funds	58,875	-	58,875
Due from component unit	-	1,005,331	1,005,331
Loans receivable	50,081	-	50,081
	<hr/>	<hr/>	<hr/>
Total Assets	\$ 457,472	\$ 1,028,730	\$ 1,486,202
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>
<u>Liabilities and Fund Balances</u>			
Liabilities			
Due to other funds	\$ -	\$ 163,555	\$ 163,555
Due to other governments	104,078	-	104,078
Deferred revenue - unavailable	2,606	10,113	12,719
	<hr/>	<hr/>	<hr/>
Total Liabilities	\$ 106,684	\$ 173,668	\$ 280,352
	<hr/>	<hr/>	<hr/>
Fund Balances			
Reserved for loans receivable	\$ 50,081	\$ -	\$ 50,081
Unreserved			
Designated for debt service	-	855,062	855,062
Undesignated	300,707	-	300,707
	<hr/>	<hr/>	<hr/>
Total Fund Balances	\$ 350,788	\$ 855,062	\$ 1,205,850
	<hr/>	<hr/>	<hr/>
Total Liabilities and Fund Balances	\$ 457,472	\$ 1,028,730	\$ 1,486,202
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Statement 2

**COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
NONMAJOR GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2008**

	Special Revenue (Statement 4)	Debt Service	Total
Revenues			
Taxes	\$ 58,307	\$ 458,649	\$ 516,956
Licenses and permits	75	-	75
Intergovernmental	97,760	83,431	181,191
Investment earnings	-	8,137	8,137
Miscellaneous	3,066	160,426	163,492
Total Revenues	\$ 159,208	\$ 710,643	\$ 869,851
Expenditures			
Current			
General government	\$ 7,596	\$ -	\$ 7,596
Public safety	114,478	-	114,478
Conservation of natural resources	6,284	-	6,284
Economic development	30,000	-	30,000
Debt service			
Principal	302,946	620,000	922,946
Interest	124,783	129,546	254,329
Administrative (fiscal) charges	-	2,965	2,965
Total Expenditures	\$ 586,087	\$ 752,511	\$ 1,338,598
Excess of Revenues Over (Under) Expenditures	\$ (426,879)	\$ (41,868)	\$ (468,747)
Other Financing Sources (Uses)			
Transfers in	58,875	-	58,875
Net Change in Fund Balance	\$ (368,004)	\$ (41,868)	\$ (409,872)
Fund Balance - January 1	718,792	896,930	1,615,722
Fund Balance - December 31	\$ 350,788	\$ 855,062	\$ 1,205,850

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Statement 3

**COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS
SPECIAL REVENUE FUNDS
DECEMBER 31, 2008**

	<u>Resource Development</u>	<u>Economic Development</u>	<u>Unorganized Townships</u>	<u>Total</u>
<u>Assets</u>				
Cash and pooled investments	\$ 177,123	\$ 42,201	\$ 122,317	\$ 341,641
Undistributed cash in agency funds	-	-	3,430	3,430
Taxes receivable				
Prior	-	-	3,214	3,214
Accounts receivable	-	231	-	231
Due from other funds	58,875	-	-	58,875
Loans receivable	-	50,081	-	50,081
	<hr/>	<hr/>	<hr/>	<hr/>
Total Assets	<u>\$ 235,998</u>	<u>\$ 92,513</u>	<u>\$ 128,961</u>	<u>\$ 457,472</u>
 <u>Liabilities and Fund Balances</u>				
Liabilities				
Due to other governments	\$ -	\$ -	\$ 104,078	\$ 104,078
Deferred revenue - unavailable	-	-	2,606	2,606
	<hr/>	<hr/>	<hr/>	<hr/>
Total Liabilities	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 106,684</u>	<u>\$ 106,684</u>
 Fund Balances				
Reserved for loans receivable	\$ -	\$ 50,081	\$ -	\$ 50,081
Unreserved				
Undesignated	235,998	42,432	22,277	300,707
	<hr/>	<hr/>	<hr/>	<hr/>
Total Fund Balances	<u>\$ 235,998</u>	<u>\$ 92,513</u>	<u>\$ 22,277</u>	<u>\$ 350,788</u>
 Total Liabilities and Fund Balances				
	<u>\$ 235,998</u>	<u>\$ 92,513</u>	<u>\$ 128,961</u>	<u>\$ 457,472</u>

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Statement 4

**COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
NONMAJOR GOVERNMENTAL FUNDS
SPECIAL REVENUE FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2008**

	<u>Resource Development</u>	<u>Economic Development</u>	<u>Unorganized Townships</u>	<u>Total</u>
Revenues				
Taxes	\$ -	\$ -	\$ 58,307	\$ 58,307
Licenses and permits	-	-	75	75
Intergovernmental	90,422	-	7,338	97,760
Miscellaneous	-	3,066	-	3,066
	<u>-</u>	<u>3,066</u>	<u>-</u>	<u>3,066</u>
Total Revenues	<u>\$ 90,422</u>	<u>\$ 3,066</u>	<u>\$ 65,720</u>	<u>\$ 159,208</u>
Expenditures				
Current				
General government	\$ -	\$ -	\$ 7,596	\$ 7,596
Public safety	-	-	114,478	114,478
Conservation of natural resources	6,284	-	-	6,284
Economic development	-	30,000	-	30,000
Debt service				
Principal	302,946	-	-	302,946
Interest	124,783	-	-	124,783
	<u>124,783</u>	<u>-</u>	<u>-</u>	<u>124,783</u>
Total Expenditures	<u>\$ 434,013</u>	<u>\$ 30,000</u>	<u>\$ 122,074</u>	<u>\$ 586,087</u>
Excess of Revenues Over (Under)				
Expenditures	\$ (343,591)	\$ (26,934)	\$ (56,354)	\$ (426,879)
Other Financing Sources (Uses)				
Transfers in	58,875	-	-	58,875
	<u>58,875</u>	<u>-</u>	<u>-</u>	<u>58,875</u>
Net Change in Fund Balance	\$ (284,716)	\$ (26,934)	\$ (56,354)	\$ (368,004)
Fund Balance - January 1	<u>520,714</u>	<u>119,447</u>	<u>78,631</u>	<u>718,792</u>
Fund Balance - December 31	<u><u>\$ 235,998</u></u>	<u><u>\$ 92,513</u></u>	<u><u>\$ 22,277</u></u>	<u><u>\$ 350,788</u></u>

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Schedule 6

**BUDGETARY COMPARISON SCHEDULE
RESOURCE DEVELOPMENT SPECIAL REVENUE FUND
FOR THE YEAR ENDED DECEMBER 31, 2008**

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Revenues				
Intergovernmental	\$ 85,000	\$ 85,000	\$ 90,422	\$ 5,422
Expenditures				
Current				
Conservation of natural resources				
Forestry	\$ 203,000	\$ 203,000	\$ 6,284	\$ 196,716
Debt service				
Principal	305,582	305,582	302,946	2,636
Interest	125,467	125,467	124,783	684
Total Expenditures	\$ 634,049	\$ 634,049	\$ 434,013	\$ 200,036
Excess of Revenues Over (Under)				
Expenditures	\$ (549,049)	\$ (549,049)	\$ (343,591)	\$ 205,458
Other Financing Sources (Uses)				
Transfers in	-	-	58,875	58,875
Net Change in Fund Balance	\$ (549,049)	\$ (549,049)	\$ (284,716)	\$ 264,333
Fund Balance - January 1	520,714	520,714	520,714	-
Fund Balance - December 31	\$ (28,335)	\$ (28,335)	\$ 235,998	\$ 264,333

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Schedule 7

**BUDGETARY COMPARISON SCHEDULE
ECONOMIC DEVELOPMENT SPECIAL REVENUE FUND
FOR THE YEAR ENDED DECEMBER 31, 2008**

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Revenues				
Miscellaneous	\$ 13,392	\$ 13,392	\$ 3,066	\$ (10,326)
Expenditures				
Current				
Economic development				
Other economic development	-	-	30,000	(30,000)
Net Change in Fund Balance	\$ 13,392	\$ 13,392	\$ (26,934)	\$ (40,326)
Fund Balance - January 1	<u>119,447</u>	<u>119,447</u>	<u>119,447</u>	<u>-</u>
Fund Balance - December 31	<u><u>\$ 132,839</u></u>	<u><u>\$ 132,839</u></u>	<u><u>\$ 92,513</u></u>	<u><u>\$ (40,326)</u></u>

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Schedule 8

**BUDGETARY COMPARISON SCHEDULE
UNORGANIZED TOWNSHIPS SPECIAL REVENUE FUND
FOR THE YEAR ENDED DECEMBER 31, 2008**

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Revenues				
Taxes	\$ 65,440	\$ 65,440	\$ 58,307	\$ (7,133)
Licenses and permits	50	50	75	25
Intergovernmental	-	-	7,338	7,338
Total Revenues	\$ 65,490	\$ 65,490	\$ 65,720	\$ 230
Expenditures				
Current				
General government				
Elections	\$ 6,800	\$ 6,800	\$ 7,596	\$ (796)
Public safety				
Emergency services	74,000	74,000	114,478	(40,478)
Total Expenditures	\$ 80,800	\$ 80,800	\$ 122,074	\$ (41,274)
Net Change in Fund Balance	\$ (15,310)	\$ (15,310)	\$ (56,354)	\$ (41,044)
Fund Balance - January 1	78,631	78,631	78,631	-
Fund Balance - December 31	\$ 63,321	\$ 63,321	\$ 22,277	\$ (41,044)

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Schedule 9

**BUDGETARY COMPARISON SCHEDULE
DEBT SERVICE FUND
FOR THE YEAR ENDED DECEMBER 31, 2008**

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Revenues				
Taxes	\$ 469,300	\$ 469,300	\$ 458,649	\$ (10,651)
Intergovernmental	-	-	83,431	83,431
Investment earnings	13,000	13,000	8,137	(4,863)
Miscellaneous	224,868	224,868	160,426	(64,442)
Total Revenues	\$ 707,168	\$ 707,168	\$ 710,643	\$ 3,475
Expenditures				
Debt service				
Principal	\$ 620,000	\$ 620,000	\$ 620,000	\$ -
Interest	129,647	129,647	129,546	101
Administrative (fiscal) charges	4,325	4,325	2,965	1,360
Total Expenditures	\$ 753,972	\$ 753,972	\$ 752,511	\$ 1,461
Excess of Revenues Over (Under) Expenditures	\$ (46,804)	\$ (46,804)	\$ (41,868)	\$ 4,936
Other Financing Sources (Uses)				
Transfers in	69,495	69,495	-	(69,495)
Net Change in Fund Balance	\$ 22,691	\$ 22,691	\$ (41,868)	\$ (64,559)
Fund Balance - January 1	896,930	896,930	896,930	-
Fund Balance - December 31	\$ 919,621	\$ 919,621	\$ 855,062	\$ (64,559)

FIDUCIARY FUNDS

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Statement 5

**COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES
ALL AGENCY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2008**

	<u>Balance January 1</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance December 31</u>
<u>CITIES, TOWNS, AND OTHER GOVERNMENTS</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 118	\$ 10,409,422	\$ 10,409,316	\$ 224
<u>Liabilities</u>				
Due to other governments	\$ 118	\$ 10,409,422	\$ 10,409,316	\$ 224
<u>TAXES AND PENALTIES</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 377,311	\$ 15,776,505	\$ 15,830,003	\$ 323,813
<u>Liabilities</u>				
Taxes collected in advance	\$ 15,123	\$ 12,916	\$ 15,123	\$ 12,916
Due to other governments	362,188	15,763,589	15,814,880	310,897
Total Liabilities	\$ 377,311	\$ 15,776,505	\$ 15,830,003	\$ 323,813
<u>STATE</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 25,953	\$ 267,547	\$ 273,379	\$ 20,121
<u>Liabilities</u>				
Due to other governments	\$ 25,953	\$ 267,547	\$ 273,379	\$ 20,121

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

**Statement 5
(Continued)**

**COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES
ALL AGENCY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2008**

	<u>Balance January 1</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance December 31</u>
<u>SEWER SYSTEM DEPOSITS</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 51,740	\$ 15,675	\$ 16,775	\$ 50,640
<u>Liabilities</u>				
Customer deposits - current	\$ 51,740	\$ 15,675	\$ 16,775	\$ 50,640
 <u>NORTH SHORE COLLABORATIVE</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 253,554	\$ 213,451	\$ 249,169	\$ 217,836
<u>Liabilities</u>				
Accounts payable	\$ 253,554	\$ 213,451	\$ 249,169	\$ 217,836
 <u>TOTAL ALL AGENCY FUNDS</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 708,676	\$ 26,682,600	\$ 26,778,642	\$ 612,634
<u>Liabilities</u>				
Accounts payable	\$ 253,554	\$ 213,451	\$ 249,169	\$ 217,836
Taxes collected in advance	15,123	12,916	15,123	12,916
Due to other governments	388,259	26,440,558	26,497,575	331,242
Customer deposits - current	51,740	15,675	16,775	50,640
Total Liabilities	\$ 708,676	\$ 26,682,600	\$ 26,778,642	\$ 612,634

OTHER SCHEDULE

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Schedule 10

**SCHEDULE OF INTERGOVERNMENTAL REVENUE
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2008**

Shared Revenue

State

Highway users tax	\$ 4,986,490
County program aid	272,311
PERA rate reimbursement	24,475
Disparity reduction aid	155,178
Police aid	113,052
Taconite credit	583,492
Enhanced 911	78,397
Market value credit	436,688
	<hr/>

Total Shared Revenue	<u>\$ 6,650,083</u>
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Reimbursement for Services

State

Minnesota Department of Human Services	<u>\$ 180,488</u>
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Payments

State

Payments in lieu of taxes	\$ 527,478
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Local

Region III funding from other counties	65,000
Other	59,985
	<hr/>

Total Payments	<u>\$ 652,463</u>
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Grants

State

Minnesota Department of	
Public Safety	\$ 24,844
Transportation	68,159
Health	72,016
Natural Resources	298,991
Human Services	2,883,593
Board of Water and Soil Resources	106,790
Office of Environmental Assistance	55,000
Miscellaneous boards	6,008
	<hr/>

Total State	<u>\$ 3,515,401</u>
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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Schedule 10
(Continued)

**SCHEDULE OF INTERGOVERNMENTAL REVENUE
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2008**

Grants (Continued)

Federal

Department of	
Agriculture	\$ 1,444,823
Interior	232,749
Transportation	409,505
Health and Human Services	744,435
Homeland Security	315,054
Environmental Protection Agency	<u>5,680</u>

Total Federal	<u>\$ 3,152,246</u>
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Total State and Federal Grants	<u>\$ 6,667,647</u>
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Total Intergovernmental Revenue	<u><u>\$ 14,150,681</u></u>
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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Schedule 11

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED DECEMBER 31, 2008**

I. SUMMARY OF AUDITOR'S RESULTS

- A. Our report expresses unqualified opinions on the basic financial statements of Lake County.
- B. Significant deficiencies in internal control were disclosed by the audit of financial statements of Lake County and are reported in the "Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*." One of the significant deficiencies is a material weakness.
- C. No instances of noncompliance material to the financial statements of Lake County were disclosed during the audit.
- D. A significant deficiency relating to the audit of the major federal award programs is reported in the "Report on Compliance with Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance with OMB Circular A-133." The significant deficiency is a material weakness.
- E. The Auditor's Report on Compliance for the major federal award programs for Lake County expresses an unqualified opinion.
- F. A finding relative to a major federal award program for Lake County was reported as required by Section 510(a) of OMB Circular A-133.
- G. The major programs are:
- | | |
|--|--------------|
| National Forest Lands - 25% Payments to States | CFDA #10.665 |
| National Forest Lands - 3/4 of 1% | CFDA #10.668 |
| Medical Assistance | CFDA #93.778 |
| Homeland Security Grant Program | CFDA #97.067 |
- H. The threshold for distinguishing between Types A and B programs was \$300,000.
- I. Lake County was not determined to be a low-risk auditee.

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

INTERNAL CONTROL

PREVIOUSLY REPORTED ITEMS NOT RESOLVED

96-11 Segregation of Duties

One basic objective of internal control is to provide for segregation of incompatible duties. In other words, responsibilities should be separated among employees so that a single employee is not able to authorize a transaction, record the transaction in accounts, and be responsible for custody of the asset resulting from the transaction. The following duties should be segregated if possible:

- Someone independent of the cash collection and receipting function and the cash disbursement function should prepare bank reconciliations. If this is not possible, someone independent of these functions should review the bank reconciliations.
- Individuals who collect and receipt cash should not also:
 - post cash receipts to the general ledger system,
 - process cash disbursements,
 - maintain the general ledger,
 - make bank deposits,
 - make wire transfers,
 - make general journal entries, or
 - prepare billings.
- Individuals who process vouchers for payments should not also:
 - print or sign checks or
 - make journal entries.

Lake County does not segregate the duties of cash collection and receipting from posting receipts to the general ledger system, maintaining the general ledger, making journal entries, processing cash disbursements, or making bank deposits. Also, the same person who processes cash disbursements has the ability to print and sign checks. In addition, bank reconciliations are prepared by the same person who does some cash receipting. At the department level, many of these functions are also not segregated.

We recommend the County Board segregate these functions as much as possible. If it is not possible to segregate these duties, Lake County management should be aware of the lack of segregation of the accounting functions and implement oversight procedures to ensure that the internal control policies and procedures are being performed by staff. One possible oversight procedure is to distribute detailed monthly revenue and expenditure reports to department heads and require them to affirm they have reviewed the reports and concur with the revenues and expenditures reported for their department.

Client's Response:

The Auditor/Treasurer will review these functions with staff and reassign when possible. The Auditor/Treasurer will also look at other possible oversight procedures to ensure internal control policies and procedures are being performed.

03-2 Capital Assets

The County maintains its capital asset records on a capital asset software system called Assetkeeper. Capital asset additions and deletions are entered into this system, and depreciation is calculated by the system. Capital asset policies utilized by the County in maintaining the capital asset system have not been formally approved by the County Board. A capital assets policy should be adopted which defines the County's accounting policies over capital assets, such as capitalization thresholds, useful lives, and depreciation methods. The policy should also include the procedures to be used to identify capital asset additions and deletions.

A physical inventory of capital assets has not been done since the capital asset records were initially established in 2003.

We recommend the County Board establish a capital assets policy to define the accounting policies for capital assets. The policy should also establish procedures to identify capital asset additions and deletions. Department heads should report capital asset additions and deletions to the person maintaining Assetkeeper at least annually. Also, we recommend a physical inventory of capital assets be performed periodically. This physical inventory can be rotated so that a portion of the capital assets is inventoried each year. Each asset should be inventoried at least once every five years. Some critical capital assets may need to be inventoried more frequently.

Client's Response:

The Board will attempt to develop policies and procedures for capital assets and discuss the process of doing a physical inventory.

03-4 Preparation of Financial Statements

The County is required to prepare financial statements in accordance with generally accepted accounting principles (GAAP). The preparation of the financial statements is the responsibility of the County's management. Financial statement preparation in accordance with GAAP requires internal controls over both: (1) recording, processing, and summarizing accounting data (maintaining internal books and records); and (2) preparing and reporting appropriate government-wide and fund financial statements, including the related notes to the financial statements.

As is the case with many small and medium-sized entities, the County has relied on its independent external auditors to assist in the preparation of the basic financial statements, including notes to the financial statements, as part of its external financial reporting process. Accordingly, the County's ability to prepare financial statements in accordance with GAAP is based, at least in part, on its reliance on its external auditors, who cannot by definition be considered part of the government's internal control. This condition was caused by the County's decision that it is more cost effective to have its auditors prepare its annual basic financial statements than to incur the time and expense of obtaining the necessary training and expertise required to prepare the financial statements internally. As a result of this condition, the government lacks internal control over the preparation of financial statements in accordance with GAAP.

We recommend the County obtain the training and expertise to internally prepare its annual financial statements in accordance with GAAP. If County management intends to have staff from the Office of the State Auditor assist in preparation then, at a minimum, they must identify and train individuals to obtain the expertise that can sufficiently review, understand, and approve the County's financial statements, including notes.

Client's Response:

The County will continue to have the financial coordinator work with the State Auditor's Office on preparing financial statements.

06-1 Journal Entries

Lake County limits access to the journal entry function on the Integrated Financial System (IFS) to select County employees. At the time of our review, eleven County employees had access to this function. Most journal entries are made by the Financial Coordinator, the County Auditor/Treasurer, and the Human Services Accountant. The journal entries made by these employees are not reviewed or approved by anyone else.

The ability to make journal entries on the IFS general ledger system is a powerful function. It allows those employees with access to the journal entry function to make changes to the general ledger system. To prevent abuse of this function, it should be limited to those employees who have a logical need for this access. Also needed is a procedure for review and approval of the journal entries made.

We recommend the County Auditor/Treasurer review the access to the journal entry function to determine if there is a logical need for that access for all employees who have access. We also recommend a procedure be established to require review and approval of journal entries by someone other than the person making the journal entries. This person should obtain an understanding of the journal entry and its purpose before approval. The approval could be documented by signature on a journal entry form or a printed copy of the journal entry made. Supporting documentation or sufficient explanation should be attached to or included on the journal entry to explain why the journal entry is being made and who is making the journal entry. Journal entries should be filed in a manner that allows for their review should questions arise. A report should be generated from the IFS system that lists all journal entries made. The person charged with review and approval of journal entries should periodically review this report. Review of this report would be to ensure that no journal entries have been made which have not been submitted for review and approval.

Client's Response:

The County has determined who has the authority to make journal entries in the IFS. The County Auditor/Treasurer will now determine if it is necessary for all of these individuals to have this authority. Also, an attempt will be made to develop procedures to review journal entries.

06-2 Budgeting

The Lake County Board has adopted a formal written budget policy which includes policies on when budget amendments must go before the County Board for approval and when they may be submitted to the County Auditor/Treasurer only. However, there have been no procedures or forms developed to implement the budget policy and to communicate the budget amendment requests to either the County Board or the County Auditor/Treasurer. Also, the budget policy does not address how the budget will be monitored and who will monitor it.

We noted one instance in the current audit where the County Board approved a budget amendment in the Board minutes but it was not entered into the IFS system.

We recommend that procedures and forms be developed to implement the budget policy. Budget amendments should be tracked on budget amendment forms which should be approved by either the County Board or the County Auditor/Treasurer in accordance with the policy. Approved budget amendments should be entered into the IFS system by a person independent of the budgeting process.

The budget policy should be revised to include budget monitoring procedures. These procedures could include department head review of monthly budget to actual reports, County Board review of periodic budget to actual reports, or County Budget Officer review of budget to actual reports. Reviewers should indicate their review of budget to actual reports by signing off on them.

Client's Response:

A budget policy has been developed. Procedures and forms have been developed, and the County is implementing the policy for fiscal year 2009. The Board is also working on revising the budget policy to include monitoring procedures.

06-3 Audit Adjustments

A control deficiency exists when the design or operation of a control does not allow management or employees in the normal course of performing their assigned functions to prevent or detect misstatements of the financial statements on a timely basis. One control deficiency that typically is considered significant is identification by the auditor of a material misstatement in the financial statements that was not initially identified by the entity's internal controls, even if management subsequently corrects the misstatement. The inability to detect a material misstatement in the financial statements increases the likelihood that the financial statements would not be fairly presented.

During our audit, we proposed numerous adjustments that resulted in significant changes to the County's financial statements. The County provides cash basis financial statements and prepares some of the modified accrual information necessary to adjust the cash basis financial statements to the modified accrual basis. However, County staff do not have the time nor the governmental accounting expertise to prepare all of the information necessary to provide accurate financial statements. Therefore, audit adjustments were necessary to record additional receivables and payables found during the audit, adjust fund balance reserves, adjust state-aid highway allotments, allocate unallocated revenues and expenditures, adjust deferred revenues, adjust receivables for uncollectible amounts, record prior year book entries not made, and to make

reclassification entries as necessary. Audit adjustments were also necessary to adjust modified accrual financial statements to the accrual basis for the government-wide financial statements.

We recommend that County staff review the trial balances and journal entries in detail to ensure they have an understanding of all audit adjustments made so that, in future audits, this information can be prepared by the County.

Client's Response:

It is still the County's expectation that the financial coordinator will be able to fulfill these recommendations in time.

06-4 Accounting Policies and Procedures Manual

The County does not have a current and comprehensive accounting policies and procedures manual. All governments should document their accounting policies and procedures. Although other methods might suffice, this documentation is traditionally in the form of an accounting policies and procedures manual. This manual should document the accounting policies and procedures which make up the County's internal control system.

An accounting policies and procedures manual will enhance employees' understanding of their role and function in the internal control system, establish responsibilities, provide guidance for employees, improve efficiency and consistency of transaction processing, and improve compliance with established policies. It can also help to prevent deterioration of key elements in the County's internal control system and can help to avoid circumvention of County policies.

We recommend the County establish an accounting policies and procedures manual. The accounting policies and procedures manual should be prepared by appropriate levels of management and be approved by the County Board to emphasize its importance and authority. The documentation should describe procedures as they are intended to be performed, indicate which employees are to perform which procedures, and explain the design and purpose of control-related procedures to increase employee understanding and support for controls.

Client's Response:

The Auditor/Treasurer will attempt to assemble information for the County Board to review.

06-5 Computer Risk Management

Lake County has internal controls in place for its computer system. As part of these internal controls, the County has developed policies on emergency recovery procedures, data backup procedures, password controls, and acceptable uses of technology resources. However, the policies have not been updated on an ongoing basis, and the County has no formal procedures to identify and manage risks associated with its computer system.

Risk management begins with a risk assessment of a county's computer system to identify those risks that could negatively influence computer operations. Internal controls should be implemented to reduce the identified risks. Internal controls implemented should be documented in a well-maintained policies and procedures manual, which should be communicated to the County's staff. Staff adherence to these policies and procedures should be monitored. Because computer systems are ever changing, the County should include in its plan periodic reassessment of risk to ensure existing internal controls are still effective.

We recommend the County Board develop a plan to ensure that internal controls are in place to reduce the risk associated with the County's computer systems.

Client's Response:

The Information Systems Department has begun to identify risks that could negatively influence computer operations. A plan, along with appropriate policies, will be put together after the risk assessment is complete.

06-6 New Vendors

Lake County does not have any procedures for determining if new vendors have been added to the accounts payable system or if the new vendors added are legitimate vendors.

The ability to set up new vendors on the accounts payable system should be limited to those individuals with a logical need for this function. In addition, periodically, a report listing active vendors should be printed and reviewed by someone independent of the accounts payable system. That person should document the review by signing off on the report.

Also, when invoices are submitted for vendors that have not previously done business with the County, some procedures should be required to verify whether the vendor is legitimate. Procedures could include looking up the vendor in the phone book or on the

internet or requiring the company to send information about their business. Periodically, the vendor listing should be reviewed for old, unused vendors, and those vendors should be removed from the system.

Client's Response:

The Auditor/Treasurer will consult with the Human Services Director and attempt to review current procedures and develop new procedures if necessary.

06-7 Payroll

In Lake County, authorization for payroll changes such as new hires, promotions, and step increases, is initiated in the personnel office. Notification of the changes to be made is sent to the payroll department. In the payroll department, the payroll clerk inputs the changes into the master file of the payroll system and subsequently checks payroll edit reports to make sure the changes went into the system properly.

After the payroll clerk clears the payroll edit reports, she runs the final payroll reports and payroll checks. No one independent of the payroll function reviews the checks or payroll reports to determine that all payments were made to actual employees and the hours worked appear to be correct.

We recommend that someone independent of the payroll processing function review the payroll edit reports to make sure all changes made to the payroll system master file were authorized. This independent person should also review the final payroll reports and check to verify all employees paid are actual employees and the hours worked appear to be correct. The functions of generating and signing payroll checks should be segregated from the payroll processing function, if possible.

Client's Response:

The Auditor/Treasurer will continue to work at using current staff to have someone independent to review the payroll edits before final payroll processing.

07-1 Approval of Time Sheets

During our current audit, we noted that supervisors and certain employees who do not have immediate supervisors are approving their own time sheets. Approval of time sheets is an important internal control which helps to ensure that the time worked is reported accurately and reliably.

We recommend that each time sheet contain two attestations of the hours worked. One attestation should be by the employee, and the other should be by the employee's supervisor or other appropriate person.

Client's Response:

The County will look at implementing a policy that requires two attestations for each timesheet.

III. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARD PROGRAMS

INTERNAL CONTROL

ITEM ARISING THIS YEAR

08-1 Equipment and Real Property Management - Homeland Security Program CFDA#97.067)

Lake County purchased \$299,873 of radio equipment with federal homeland security funds. The purchases were coded to a homeland security expense account and were not identified as capital outlays. Therefore, the assets did not get included in the capital assets system. Also, the capital assets management system does not track whether a capital asset was purchased with federal funds.

Section 32 of the Common Rule requires that property records must be maintained that include a description of the property, a serial number or other identification number, the source of property, who holds title, the acquisition date and cost of the property, percentage of federal participation in the property, location use and condition of the property, and ultimate disposition data.

Lake County's capital assets records do not contain information which tracks the source of the funding for equipment acquired with federal funds. Also, equipment must be coded to a capital outlay account in order to be included by the capital assets system.

We recommend the Financial Coordinator maintain capital assets records which identify the source of funds for assets acquired with federal funds. We also recommend that capital outlay expenditures be properly coded to capital outlay accounts, regardless of the source of funding. This will ensure that all capital outlay has been properly capitalized in the capital assets system and properly reported on the government-wide financial statements.

Corrective Action Plan:

Contact Person:

Lola Haus

Corrective Action Planned:

The county department applying for and receiving the grant must be made aware of the reporting requirements of the grant. If the proper information is furnished to the auditor's office, then the grant can be properly tracked on the county's accounting system.

The financial coordinator will be instructed to maintain capital asset records which identify the source of funds for acquired assets.

Anticipated Completion Date:

December 31, 2009

IV. OTHER FINDINGS AND RECOMMENDATIONS

MINNESOTA LEGAL COMPLIANCE

PREVIOUSLY REPORTED ITEM NOT RESOLVED

07-2 Safekeeping of Investments

Minn. Stat. § 118A.06 requires that all investments be held in safekeeping with:

- a federal reserve bank;
- any bank authorized under the laws of the United States or any state to exercise corporate trust powers including, but not limited to, the bank from which the investment is purchased;
- a primary reporting dealer in United States government securities to the Federal Reserve Bank of New York; or

- a securities broker-dealer having its principal executive office in Minnesota licensed under chapter 80A, or an affiliate of it, and regulated by the Securities and Exchange Commission.

Lake County had on hand at December 31, 2008, government securities and negotiable certificates of deposit totaling \$1,041,388, which were purchased through Morgan Keegan. Morgan Keegan is not a primary reporting dealer nor does it have its principal executive offices in Minnesota. The government investments were purchased in book entry form and are maintained in an account at the Bank of New York. The certificate of deposit is tracked by the Depository Trust Corporation. However, for purposes of custody, the securities are “held” by the party who controls their movement, which in this case is the brokerage firm. Therefore, we do not believe that these investments are being safekept in accordance with Minn. Stat. § 118A.06.

We recommend the County Auditor/Treasurer comply with the requirements of Minn. Stat. § 118A.06. Investments may be held only by brokerage firms that are primary reporting dealers or have their principal offices in Minnesota. If investments are purchased through these dealers, they must be held at a bank rather than at the brokerage firm.

Client’s Response:

The Auditor/Treasurer will take the steps necessary to comply with Minnesota statutes.

PREVIOUSLY REPORTED ITEM RESOLVED

Bidding (07-3)

Lake County entered into a contract for the purchase of four Ford Expeditions. The contract was not awarded to the lowest bidder as required by Minn. Stat. § 375.21, subd. 1.

Resolution

In the current audit, we did not note any bids where the contract was not awarded to the lowest bidder.



REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA

OFFICE OF THE STATE AUDITOR

SUITE 500
525 PARK STREET
SAINT PAUL, MN 55103-2139

(651) 296-2551 (Voice)
(651) 296-4755 (Fax)
state.auditor@state.mn.us (E-mail)
1-800-627-3529 (Relay Service)

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
Lake County

We have audited the financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of Lake County as of and for the year ended December 31, 2008, which collectively comprise the County's basic financial statements, and have issued our report thereon dated September 30, 2009. The financial statements include the Nursing Home Enterprise Fund as of and for the year ended September 30, 2008. 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 Lake County's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the County's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph of this section and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the County's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the County's financial statements that is more than inconsequential will not be prevented or detected by the County's internal control. We considered the deficiencies described in the accompanying Schedule of Findings and Questioned Costs as items 96-11, 03-2, 03-4, 06-1 through 06-7, and 07-1 to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the County's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider item 06-3 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Lake 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, Lake County complied with the material terms and conditions of applicable legal provisions, except as described in the Schedule of Findings and Questioned Costs as item 07-2.

Lake County's written responses to the significant deficiencies, material weakness, and legal compliance findings identified in our audit have been included in the Schedule of Findings and Questioned Costs. We did not audit the County's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Board of County Commissioners, management, others within Lake County, 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

September 30, 2009

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REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA

OFFICE OF THE STATE AUDITOR

SUITE 500
525 PARK STREET
SAINT PAUL, MN 55103-2139

(651) 296-2551 (Voice)
(651) 296-4755 (Fax)
state.auditor@state.mn.us (E-mail)
1-800-627-3529 (Relay Service)

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

Board of County Commissioners
Lake County

Compliance

We have audited the compliance of Lake County with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended December 31, 2008. Lake County's major federal programs are identified in the Summary of Auditor's Results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the County's management. Our responsibility is to express an opinion on the County's compliance based on our audit.

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

In our opinion, Lake County complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended December 31, 2008.

Internal Control Over Compliance

The management of Lake County is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the County's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the County's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in Lake County's internal control that might be significant deficiencies or material weaknesses as defined below. However, as discussed below, we identified a deficiency in internal control over compliance that we consider to be a significant deficiency.

A control deficiency in internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the County's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the County's internal control. We consider the deficiency in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as item 08-1 to be a significant deficiency.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by Lake County's internal control. We consider the deficiency in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as item 08-1 to be a material weakness.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of Lake County as of and for the year ended December 31, 2008, which collectively comprise the County's basic financial statements, and have issued our report thereon

dated September 30, 2009. Our audit was performed for the purpose of forming opinions on the County's basic financial statements. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Lake County's corrective action plan to the federal award finding identified in our audit is included in the accompanying Schedule of Findings and Questioned Costs. We did not audit the County's corrective action plan and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Board of County Commissioners, management and others within the County, 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

September 30, 2009

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**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Schedule 12

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2008**

Federal Grantor Pass-Through Agency Grant Program Title	Pass-Through Grant Numbers	Federal CFDA Number	Expenditures
U.S. Department of Agriculture			
Direct			
U.S. Forest Service Cooperative Agreement		10.R9-9-95-35B	\$ 27,000
Passed Through Carlton, Cook, Lake, and St. Louis Community Health Board			
Special Supplemental Nutrition Program for Women, Infants, and Children (WIC)		10.557	35,608
Passed Through Minnesota Department of Human Services			
Matching Grant for Food Stamp Program		10.561	101,532
Passed Through Minnesota Department of Finance			
National Forest Lands - 25% Payments to States		10.665	393,411
National Forest Lands - 3/4 of 1%		10.668	887,272
Total U.S. Department of Agriculture			\$ 1,444,823
U.S. Department of the Interior			
Direct			
Payments in Lieu of Taxes		15.226	\$ 232,749
U.S. Department of Transportation			
Passed Through Minnesota Department of Transportation			
Highway Planning and Construction	SP-38-604-13 SP-38-605-09	20.205	\$ 209,264
Passed Through Minnesota Department of Natural Resources			
Recreational Trails Program	013-06-2c 0040-08-2c	20.219	87,930
Total U.S. Department of Transportation			\$ 297,194
U.S. Environmental Protection Agency			
Passed Through Carlton, Cook, Lake, and St. Louis Community Health Board			
State Indoor Radon Grants		66.032	\$ 680
Passed Through Minnesota Pollution Control Agency			
Beach Monitoring and Program Implementation Grants		66.472	5,000
Total U.S. Environmental Protection Agency			\$ 5,680

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

**Schedule 12
(Continued)**

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2008**

Federal Grantor Pass-Through Agency Grant Program Title	Pass-Through Grant Numbers	Federal CFDA Number	Expenditures
U.S. Department of Health and Human Services			
Passed Through Carlton, Cook, Lake, and St. Louis Community Health Board			
Alzheimer's Disease Demonstration Grants to the States		93.051	\$ 934
Center for Disease Control and Prevention		93.283	31,634
Temporary Assistance for Needy Families		93.558	5,841
Maternal and Child Health Services Block Grant		93.994	10,162
Passed Through Minnesota Department of Health			
Center for Disease Control and Prevention		93.283	1,000
Passed Through Minnesota Department of Human Services			
Promoting Safe and Stable Families		93.556	4,358
Temporary Assistance for Needy Families		93.558	66,088
IV-D Child Support		93.563	171,820
Refugee and Entrant Assistance		93.566	263
Child Care Cluster			
Child Care and Development Block Grant		93.575	4,514
Child Care Mandatory and Matching Funds		93.596	1,201
Foster Care - Title IV-E		93.658	45,645
Social Services Block Grant Title XX		93.667	101,202
Support for Emancipation and Living Functionally		93.674	925
State Children's Insurance Program		93.767	257
Medical Assistance		93.778	297,487
Community Mental Health Services Block Grant		93.958	1,104
Total U.S. Department of Health and Human Services			\$ 744,435
U.S. Department of Homeland Security			
Passed Through Minnesota Department of Public Safety			
Boating Safety Financial Assistance		97.012	\$ 4,070
Emergency Management Performance Grant	2007-EMPG-00532		
	2008-EMPG-00687	97.042	16,230
Homeland Security Grant Program	2005-SHSP-00465		
	2005-SHSP-00540		
	2007-HSGP-00500		
	2009-OSGP-00283	97.067	294,754
Total U.S. Department of Homeland Security			\$ 315,054
Total Federal Awards			\$ 3,039,935

**LAKE COUNTY
TWO HARBORS, MINNESOTA**

Schedule 12
(Continued)

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2008**

Notes to Schedule of Expenditures of Federal Awards

1. The Schedule of Expenditures of Federal Awards presents the activity of federal award programs expended by Lake County.
The County's reporting entity is defined in Note 1 to the financial statements.
2. The expenditures on this schedule are on the modified accrual basis of accounting. Due to timing differences in revenue recognition under the modified accrual basis, expenditures on this schedule may not equal federal revenues reported in the financial statements.
In 2008, \$279,192 of prior year federal expenditures were recognized as revenue in the financial statements, and \$166,881 of current year federal expenditures were not recognized as revenues because they were not received within the period of availability.
3. Pass-through grant numbers are presented for grants for which they have been assigned.