

STATE OF MINNESOTA

Office of the State Auditor



Rebecca Otto
State Auditor

**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

YEAR ENDED DECEMBER 31, 2010

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.

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**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

Year Ended December 31, 2010



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

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**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

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**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

ORGANIZATION
DECEMBER 31, 2010

Board

Steve Raukar, Chair
Chris Dahlberg, Alternate
Keith Nelson
Steve O'Neil, Alternate
Peg Sweeney
Paul Bergman, Secretary/Treasurer
Rick Goutermont, Vice Chair
Rich Sve, Alternate

Representing

St. Louis County
Lake County
Lake County
Lake County

Executive Director

Robert Manzoline

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REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA

OFFICE OF THE STATE AUDITOR

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
St. Louis and Lake Counties
Regional Railroad Authority

We have audited the accompanying financial statements of the governmental activities and the General Fund of the St. Louis and Lake Counties Regional Railroad Authority as of and for the year ended December 31, 2010, which collectively comprise the Authority's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Authority's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and the General Fund of the St. Louis and Lake Counties Regional Railroad Authority as of December 31, 2010, and the respective changes in financial position thereof and the budgetary comparison of the General Fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Management has omitted the Management's Discussion and Analysis that accounting principles generally accepted in the United States of America require to be presented to supplement the basic financial statements. Such missing information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who consider it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. Our opinion on the basic financial statements is not affected by this missing information.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 23, 2012, on our consideration of the St. Louis and Lake Counties Regional Railroad Authority'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

March 23, 2012

BASIC FINANCIAL STATEMENTS

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**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

EXHIBIT 1

**GENERAL FUND BALANCE SHEET AND
GOVERNMENTAL ACTIVITIES - STATEMENT OF NET ASSETS
WITH ADJUSTMENTS TO CONVERT MODIFIED TO FULL ACCRUAL
DECEMBER 31, 2010**

	General Fund	Adjustments	Governmental Activities
<u>Assets</u>			
Cash and pooled investments	\$ 1,304,764	\$ -	\$ 1,304,764
Accounts receivable	29,238	-	29,238
Taxes receivable - delinquent	84,479	-	84,479
Due from other governments	544,147	-	544,147
Capital assets			
Non-depreciable	-	3,215,326	3,215,326
Depreciable - net of accumulated depreciation	-	8,100,245	8,100,245
	\$ 1,962,628	\$ 11,315,571	\$ 13,278,199
Total Assets	\$ 1,962,628	\$ 11,315,571	\$ 13,278,199
 <u>Liabilities and Fund Balance/Net Assets</u>			
Liabilities			
Current liabilities			
Accounts payable	\$ 104,492	\$ -	\$ 104,492
Salaries payable	8,135	-	8,135
Due to other governments	5,943	-	5,943
Deferred revenue - unavailable	528,334	(528,334)	-
Deferred revenue - unearned	50,000	-	50,000
Non-current liabilities			
Compensated absences payable - due within one year	-	15,688	15,688
Compensated absences payable - long-term	-	45,222	45,222
	\$ 696,904	\$ (467,424)	\$ 229,480
Total Liabilities	\$ 696,904	\$ (467,424)	\$ 229,480
 Fund Balance			
Unreserved			
Designated for compensated absences	\$ 50,498	\$ (50,498)	
Designated for future trail maintenance	360,180	(360,180)	
Undesignated	855,046	(855,046)	
	\$ 1,265,724	\$ (1,265,724)	
Total Fund Balance	\$ 1,265,724	\$ (1,265,724)	
 Net Assets			
Invested in capital assets		\$ 11,315,571	\$ 11,315,571
Unrestricted		1,733,148	1,733,148
		\$ 13,048,719	\$ 13,048,719
Total Net Assets		\$ 13,048,719	\$ 13,048,719
 Total Liabilities and Fund Balance/Net Assets	\$ 1,962,628	\$ 11,315,571	\$ 13,278,199

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

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**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

***EXHIBIT 1
(Continued)***

**GENERAL FUND BALANCE SHEET AND
GOVERNMENTAL ACTIVITIES - STATEMENT OF NET ASSETS
WITH ADJUSTMENTS TO CONVERT MODIFIED TO FULL ACCRUAL
DECEMBER 31, 2010**

Reconciliation of the General Fund Balance to Net Assets

Fund Balance - General Fund	\$ 1,265,724
Capital assets, net of accumulated depreciation, used in governmental activities are not financial resources and, therefore, are not reported in the governmental funds.	11,315,571
Other long-term assets are not available to pay for the current period expenditures and, therefore, are deferred in the governmental funds.	528,334
Long-term liabilities are not due and payable in the current period and, therefore, are not reported in the governmental funds.	<u>(60,910)</u>
Net Assets - Governmental Activities	<u><u>\$ 13,048,719</u></u>

**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

EXHIBIT 2

**GENERAL FUND STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
AND GOVERNMENTAL ACTIVITIES - STATEMENT OF ACTIVITIES
WITH ADJUSTMENTS TO CONVERT MODIFIED TO FULL ACCRUAL
FOR THE YEAR ENDED DECEMBER 31, 2010**

	General Fund	Adjustments	Governmental Activities
Revenues			
Taxes	\$ 1,124,989	\$ 8,077	\$ 1,133,066
Intergovernmental	787,426	262,243	1,049,669
Charges for services	4,950	-	4,950
Miscellaneous	174,166	-	174,166
Capital contributions	-	1,568,542	1,568,542
	\$ 2,091,531	\$ 1,838,862	\$ 3,930,393
Expenditures/Expenses			
Current			
Economic development			
Administration	\$ 2,833,054	\$ (1,554,644)	\$ 1,278,410
Depreciation	-	186,053	186,053
	\$ 2,833,054	\$ (1,368,591)	\$ 1,464,463
Net Change in Fund Balance/Net Assets	\$ (741,523)	\$ 3,207,453	\$ 2,465,930
Fund Balance/Net Assets - January 1 (Restated, Note 1.E.)	2,007,247	8,575,542	10,582,789
Fund Balance/Net Assets - December 31	\$ 1,265,724	\$ 11,782,995	\$ 13,048,719

**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

***EXHIBIT 2
(Continued)***

**GENERAL FUND STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
AND GOVERNMENTAL ACTIVITIES - STATEMENT OF ACTIVITIES
WITH ADJUSTMENTS TO CONVERT MODIFIED TO FULL ACCRUAL
FOR THE YEAR ENDED DECEMBER 31, 2010**

**Reconciliation of the Statement of General Fund Revenues, Expenditures,
and Changes in Fund Balance to the Statement of Activities of
Governmental Activities
Net Change in Fund Balance**

\$ (741,523)

In the General Fund, under the modified accrual basis, receivables not available for expenditures are deferred. In the Statement of Activities, those revenues are recognized when earned. The adjustment to revenues between the General Fund and the governmental activities is the increase or decrease in revenues deferred as unavailable.

Deferred revenue - December 31	\$ 528,334	
Deferred revenue - January 1	(258,014)	270,320

Governmental funds report capital outlay as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense.

Expenditures for general capital assets and infrastructure	\$ 1,604,513	
Capital contributions	1,568,542	
Current year depreciation	(186,053)	2,987,002

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.

Changes in compensated absences		(49,869)

Change in Net Assets of Governmental Activities

\$ 2,465,930

**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

EXHIBIT 3

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
BUDGETARY COMPARISON
FOR THE YEAR ENDED DECEMBER 31, 2010**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Revenues				
Taxes	<u>\$ 1,345,172</u>	<u>\$ 1,345,172</u>	<u>\$ 1,124,989</u>	<u>\$ (220,183)</u>
Intergovernmental				
State				
Market Value Credit	\$ 92,918	\$ 92,918	\$ 92,918	\$ -
Taconite Credit	-	-	53,489	53,489
State PERA	-	-	1,222	1,222
Mobile Home Taconite Credit	-	-	747	747
IRRRB	-	-	39,813	39,813
Department of Natural Resources	-	-	300,000	300,000
State 30% Rental	-	-	6	6
Disparity Reduction Credit	-	-	26,071	26,071
Local				
Other local grants	188,242	188,242	185,160	(3,082)
Reimbursement for administrative services - Minneapolis-Duluth/Superior Passenger Rail Alliance	-	-	88,000	88,000
Total intergovernmental	<u>\$ 281,160</u>	<u>\$ 281,160</u>	<u>\$ 787,426</u>	<u>\$ 506,266</u>
Charges for services	<u>\$ 37,500</u>	<u>\$ 37,500</u>	<u>\$ 4,950</u>	<u>\$ (32,550)</u>
Miscellaneous	<u>\$ 13,000</u>	<u>\$ 13,000</u>	<u>\$ 174,166</u>	<u>\$ 161,166</u>
Total Revenues	<u>\$ 1,676,832</u>	<u>\$ 1,676,832</u>	<u>\$ 2,091,531</u>	<u>\$ 414,699</u>
Expenditures				
Current				
Economic development	2,936,832	2,936,832	2,833,054	(103,778)
Net Change in Fund Balance	<u>\$ (1,260,000)</u>	<u>\$ (1,260,000)</u>	<u>\$ (741,523)</u>	<u>\$ 518,477</u>
Fund Balance - January 1	<u>2,007,247</u>	<u>2,007,247</u>	<u>2,007,247</u>	<u>-</u>
Fund Balance - December 31	<u>\$ 747,247</u>	<u>\$ 747,247</u>	<u>\$ 1,265,724</u>	<u>\$ 518,477</u>

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**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

NOTES TO THE FINANCIAL STATEMENTS
AS OF AND FOR THE YEAR ENDED DECEMBER 31, 2010

1. Summary of Significant Accounting Policies

The St. Louis and Lake Counties Regional Railroad Authority's financial statements are prepared in accordance with generally accepted accounting principles (GAAP) as of and for the year ended December 31, 2010. The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (statements and interpretations). Governments are also required to follow the pronouncements of the Financial Accounting Standards Board issued through November 30, 1989, (when applicable) that do not conflict with or contradict GASB pronouncements. The more significant accounting policies established in GAAP and used by the St. Louis and Lake Counties Regional Railroad Authority are discussed below.

A. Financial Reporting Entity

The St. Louis and Lake Counties Regional Railroad Authority was established July 14, 1986, under the Regional Railroad Authorities Act, Minn. Stat. §§ 398A.01 to 398A.09. It is governed by a Board composed of three members from the St. Louis County Board of Commissioners and two members from the Lake County Board of Commissioners. Both counties also appoint an alternate member. Its purpose is to operate a scenic tourist excursion railway in Northeastern Minnesota and create a paved multi-purpose trail along abandoned rail lines, where possible, which will enable users to access one community from another. The Board is organized with a chair, vice chair, and secretary-treasurer elected each year.

St. Louis County, as fiscal agent, reports the transactions of the Authority in an agency fund on its annual financial statements.

B. Basic Financial Statements

Basic financial statements include information on the Authority's activities as a whole and information on the individual fund of the Authority. These separate presentations are reported in different columns on Exhibits 1 and 2. Each of the exhibits starts with a column of information based on activities of the General Fund and reconciles it to a column that reports the "governmental activities" of the Authority as a whole.

**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

1. Summary of Significant Accounting Policies

B. Basic Financial Statements (Continued)

The governmental activities columns are reported on the full accrual, economic resources basis, which recognizes all long-term assets and receivables as well as long-term debt and obligations. The Authority's net assets are reported in two parts: invested in capital assets and unrestricted net assets. The Statement of Activities demonstrates the degree to which the expenses of the Authority are offset by revenues.

The Balance Sheet and Statement of Revenues, Expenditures, and Changes in Fund Balance for the General Fund are presented on the modified accrual basis and report current financial resources.

C. Measurement Focus and Basis of Accounting

The governmental activities 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. 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 Authority considers all revenues as available if collected within 60 days after the end of the current period. Charges for services and interest are considered susceptible to accrual. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on long-term debt, compensated absences, and claims and judgments, which are recognized as expenditures to the extent that they have matured. Proceeds of long-term debt and acquisitions under capital leases, if any, 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.

**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

1. Summary of Significant Accounting Policies (Continued)

D. Budgetary Data

The Authority adopts estimated revenue and expenditure budgets for the General Fund on a basis consistent with generally accepted accounting principles. The budget can be amended during the year by the Authority's Board.

E. Restatement

Authority-related construction project costs expensed in prior years were added to construction in progress. Accumulated depreciation was reclassified for depreciation recognized in prior year to reflect a change in the estimated life of Bridge 16. The effect on the beginning balances of governmental activities net assets and capital assets are:

	Net Assets of Governmental Activities	Capital Assets
Balances		
January 1, 2010, as previously reported	\$ 10,424,839	\$ 8,170,619
Addition to construction in progress	78,779	78,779
Reduction to accumulated depreciation	79,171	79,171
January 1, 2010, as restated	\$ 10,582,789	\$ 8,328,569

F. Assets, Liabilities, and Net Assets or Equity

1. Taxes Receivable

Taxes receivable consist of uncollected taxes payable in the years 2002 to 2010. Taxes receivable are offset by deferred revenue for the amount not collected within 60 days of December 31 to indicate they are not available to pay current expenditures. No provision has been made for an estimated uncollectible amount.

**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

1. Summary of Significant Accounting Policies

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

2. Capital Assets

Capital assets, which include property, plant, equipment, and infrastructure assets (for example, paved trails, bridges, sidewalks, and similar items), are reported in the governmental activities column in the government-wide financial statements. Capital assets are defined by the Authority as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair value at the date of donation. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized.

Property, plant, and equipment of the St. Louis and Lake Counties Regional Railroad Authority are depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Infrastructure	20 - 40
Machinery, furniture, and equipment	3 - 20

3. Fund Equity

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

4. Use of Estimates

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

**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

2. Detailed Notes

A. Assets

1. Deposits and Investments

The Authority is authorized by Minn. Stat. §§ 118A.02 and 118A.04 to deposit its cash and to invest in certificates of deposit in financial institutions designated by the St. Louis County Board of Commissioners and the Authority's Board. Minnesota statutes require that all Authority deposits be covered by insurance, surety bond, or collateral. The Authority may invest in the types of securities authorized by Minn. Stat. §§ 118A.04-.05.

The Authority deposits all its cash with its fiscal agent, St. Louis County. Additional disclosures, as required by GASB Statement No. 40, *Deposits and Investment Risk Disclosure*; and Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, are disclosed in the St. Louis County Comprehensive Annual Financial Report.

2. Receivables

Receivables as of December 31, 2010, for the St. Louis and Lake Counties Regional Railroad Authority's governmental activities are as follows:

Due from other governments	\$	544,147
Taxes receivable		84,479
Accounts		<u>29,238</u>
Total Receivables	\$	<u>657,864</u>

**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

2. Detailed Notes

A. Assets (Continued)

3. Capital Assets

Governmental capital asset activity for the year ended December 31, 2010, was as follows:

	Restated (Note 1.E.) Beginning Balance	Increase	Decrease	Ending Balance
Capital assets not depreciated				
Land	\$ 126,211	\$ -	\$ -	\$ 126,211
Construction in progress	1,082,060	2,161,990	154,935	3,089,115
Total capital assets not depreciated	<u>\$ 1,208,271</u>	<u>\$ 2,161,990</u>	<u>\$ 154,935</u>	<u>\$ 3,215,326</u>
Capital assets depreciated				
Infrastructure	\$ 9,150,186	\$ 1,166,000	\$ -	\$ 10,316,186
Machinery, furniture, and equipment	140,959	-	-	140,959
Total capital assets depreciated	<u>\$ 9,291,145</u>	<u>\$ 1,166,000</u>	<u>\$ -</u>	<u>\$ 10,457,145</u>
Less: accumulated depreciation for				
Infrastructure	\$ 2,118,556	\$ 182,458	\$ -	\$ 2,301,014
Machinery, furniture, and equipment	52,291	3,595	-	55,886
Total accumulated depreciation	<u>\$ 2,170,847</u>	<u>\$ 186,053</u>	<u>\$ -</u>	<u>\$ 2,356,900</u>
Total capital assets depreciated, net	<u>\$ 7,120,298</u>	<u>\$ 979,947</u>	<u>\$ -</u>	<u>\$ 8,100,245</u>
Total Capital Assets, Net	<u><u>\$ 8,328,569</u></u>	<u><u>\$ 3,141,937</u></u>	<u><u>\$ 154,935</u></u>	<u><u>\$ 11,315,571</u></u>

Depreciation expense was charged to functions/programs as follows:

Governmental Activities	
Economic development	<u>\$ 186,053</u>

**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

2. Detailed Notes (Continued)

B. Liabilities

1. Payables

Payables at December 31, 2010, for the St. Louis and Lake Counties Regional Railroad Authority's governmental activities are as follows:

Accounts	\$	104,492
Salaries		8,135
Due to other governments		<u>5,943</u>
Total Payables	\$	<u>118,570</u>

2. Deferred Revenue

St. Louis and Lake Counties Regional Railroad Authority's fund and the government-wide financial statements defer revenue for resources that have been received but not yet earned. The governmental fund also reports deferred revenue in connection with receivables for revenues not considered to be available to liquidate liabilities of the current period.

3. Compensated Absences

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

**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

2. Detailed Notes

B. Liabilities

3. Compensated Absences (Continued)

The following is a summary of the changes in long-term compensated absences payable for the year ended December 31, 2010:

Payable - January 1	\$ 11,041
Net increase (decrease)	<u>49,869</u>
Payable - December 31	<u><u>\$ 60,910</u></u>

Under the St. Louis and Lake Counties Regional Railroad Authority's labor agreements, its employees are granted vacation and sick leave in varying amounts based on length of service. Vacation leave accrual is 5 to 20 days per year. Sick leave accrual is 13 to 16.25 days per year.

Unused, accumulated vacation is paid to employees upon termination. The current portion of unused vacation is recognized as a current liability in the government-wide Statement of Net Assets. Vested sick leave is paid to employees at retirement or is used for the payment of employees' health insurance coverage during their retirement. The vested sick leave and unvested sick leave likely to become vested (vesting sick leave) are estimated using the vesting method prescribed by GASB Statement 16. Both vested and vesting amounts are recognized in the government-wide financial statements as liabilities, but not in the governmental funds.

4. Risk Management

The St. Louis and Lake Counties Regional Railroad Authority 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. The Authority maintains commercial insurance policies to address these risks of loss, either by purchasing the policies directly from commercial insurers or by contractual commitments from third parties to name the Authority as an additional insured on policies of commercial liability insurance maintained by the contracting parties.

**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

2. Detailed Notes

B. Liabilities

4. Risk Management (Continued)

There were no significant reductions in insurance coverage from the previous year. There were no settlements in excess of insurance for any of the past three fiscal years.

3. Pension Plans

A. Plan Description

All full-time and certain part-time employees of the St. Louis and Lake Counties Regional Railroad Authority are covered by defined benefit pension plans administered by the Public Employees Retirement Association of Minnesota (PERA). PERA administers the General Employees Retirement Fund, which is a cost-sharing, multiple-employer retirement plan. The plan is established and administered in accordance with Minn. Stat. chs. 353 and 356.

General 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.

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 (five years for those first eligible for membership after June 30, 2010). Defined retirement benefits are based on a member's average yearly salary for the five highest-paid consecutive 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

**ST. LOUIS AND LAKE COUNTIES
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EVELETH, MINNESOTA**

3. Pension Plans

A. Plan Description (Continued)

Plan member, the annuity accrual rate is 1.2 percent of average salary for each of the first ten years and 1.7 percent for each successive year. Using Method 2, the annuity accrual rate is 2.7 percent of average salary for Basic Plan members and 1.7 percent for Coordinated Plan members for each year of service.

For General Employees Retirement Fund members whose annuity is calculated using Method 1, a full annuity is available when age plus years of service equal 90. Normal retirement age is 65 for members hired prior to July 1, 1989, and is the age for unreduced Social Security benefits capped at age 66 for Coordinated Plan members hired on or after July 1, 1989. 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 General Employees Retirement 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.

B. Funding Policy

Pension benefits are funded from member and employer contributions and income from the investment of fund assets. Rates for employer and employee contributions are set by Minn. Stat. ch. 353. These statutes are established and amended by the State Legislature. The Authority makes annual contributions to the pension plans equal to the amount required by state statutes. General Employees Retirement Fund Basic Plan members and Coordinated Plan members are required to contribute 9.1 and 6.0 percent, respectively, of their annual covered salary.

**ST. LOUIS AND LAKE COUNTIES
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EVELETH, MINNESOTA**

3. Pension Plans

B. Funding Policy (Continued)

The Authority is required to contribute the following percentages of annual covered payroll in 2010:

General Employees Retirement Fund	
Basic Plan members	11.78%
Coordinated Plan members	7.00

The Authority's contributions for the years ending December 31, 2010, 2009, and 2008, for the General Employees Retirement Fund were:

<u>2010</u>	<u>2009</u>	<u>2008</u>
\$ 13,027	\$ 10,760	\$ 10,176

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

4. Subsequent Events

A. Lakefront Line Railroad Bridge Replacement and Repair

The St. Louis and Lake Counties Regional Railroad Authority elected to replace and repair three bridges on the Lakefront Line Railroad. A tax levy increase in the amount of \$300,000 per year was approved to pay for construction costs until all bridges have been completed. The first bridge has been replaced. Construction on the second bridge was completed in 2010, and the total cost of \$1,166,000 was added to the infrastructure schedule of capital assets. Construction on the third bridge is scheduled to begin in the fall of 2013, and tentative completion is spring of 2014.

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4. Subsequent Events (Continued)

B. Mesabi Trail

The St. Louis and Lake Counties Regional Railroad Authority is in the process of constructing different sections of the Mesabi Trail. As each section is finished, it will be capitalized as part of the Authority. As of December 31, 2010, the following three sections were in progress: Giants Ridge to Highway 135, Highway 135 to Embarrass, and Eveleth to Fayal. A \$300,000 Minnesota DNR grant agreement was approved in 2011 for future construction of the Murray Road to Highway 1/169 section of the trail.

C. Mesabi Station Facility

Construction for the Mesabi Station Facility in Eveleth, Minnesota, began in November 2009 with an estimated completion date of November 2010. Cost was estimated by DSGW Architects at \$1.7 million, and the bid amount was approved at \$1,129,000. There was construction in progress in relation to this project in the amount of \$1,790,203, as of December 31, 2010, and the project was near completion. The Mesabi Station Facility is to be capitalized in 2011.

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**ST. LOUIS AND LAKE COUNTIES
REGIONAL RAILROAD AUTHORITY
EVELETH, MINNESOTA**

SCHEDULE OF FINDINGS AND RECOMMENDATIONS
FOR THE YEAR ENDED DECEMBER 31, 2010

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

INTERNAL CONTROL

PREVIOUSLY REPORTED ITEMS NOT RESOLVED

03-1 Internal Control/Segregation of Duties

Management is responsible for establishing and maintaining internal control. This responsibility includes the internal control over the various accounting cycles, the fair presentation of the financial statements and related notes, and the accuracy and completeness of all financial records and related information. Adequate segregation of duties is a key internal control in an organization's accounting system. The size of the St. Louis and Lake Counties Regional Railroad Authority and its staffing limits the internal control that management can design and implement into the organization. Management should be aware that segregation of duties is not adequate from an internal control point of view.

Management is responsible for the accuracy and completeness of all financial records and related information. Also, management is responsible for controls over the period-end financial reporting process, including controls over procedures used to enter transaction totals into the general ledger; initiate, authorize, record, and process journal entries into the general ledger; and record recurring and nonrecurring adjustments to the financial statements.

Management has requested that staff from the Office of the State Auditor prepare the annual financial statements and related notes. This arrangement is not unusual for an organization the size of the St. Louis and Lake Counties Regional Railroad Authority. This decision was based on the availability of the Authority's staff and the cost benefit of using this expertise.

During our audit, material adjustments were proposed to convert the Authority's financial records to the financial statements as reported. Adjustments were needed to reclassify a portion of fund balance from undesignated to designated and to adjust capital assets.

We recommend the Board of Directors be mindful that limited staffing causes inherent risks in safeguarding the Authority's assets and the proper reporting of its financial activity. We recommend the Board of Directors continue to implement oversight procedures and monitor those procedures to determine if they are still effective internal controls.

Client's Response:

Management is aware of internal control responsibility and the Board of Directors is aware that staff limitations are not adequate for RRA accounting system. Management has recommended and the Board of Directors has approved continuation of agreements with St. Louis County Auditors Office and State of Minnesota, Office of the Auditor for accounting, financial statements and recording services.

09-1 Capital Asset Records

The Authority maintains capital asset schedules separate from the accounting system maintained by its fiscal agent; however, the Authority does not maintain a construction in progress schedule. Assets were not properly capitalized for jointly-funded projects where expenditures were paid by other entities. Material audit adjustments were needed to reflect this information in the financial statements.

Procedures and records should be sufficient to ensure that the accounting and financial reporting system properly reflect all capital asset activity.

We recommend the Authority develop procedures to ensure that capital assets, including construction in progress and joint projects, are properly accounted for and reflected in its financial statements. The procedures should allow the Authority to identify and monitor capital asset additions, deletions, and changes to construction in progress. This may include having the Authority receive copies of invoices or an accounting from other entities making direct payments for joint construction projects. Capital asset schedules should be verified with the capital asset information reflected in the accounting records maintained by the Authority's fiscal agent, St. Louis County.

Client's Response:

Management will make adjustments to Capital Asset recording particularly with projects under construction. Construction(s) in progress will be capitalized for those projects that carry over from one calendar year into the next calendar year.

Management will make recommendations to RRA Board of Directors that Capital Asset Policy recording be changed to reflect new project construction(s) for Mesabi Trail and Lakefront Line Railroad as independent infrastructure improvements rather than current Group Network or Identification method.

ITEM ARISING THIS YEAR

10-1 Designated Fund Balance Account Records

As of December 31, 2010, the Authority's Board had approved resolutions designating \$475,000 of fund balance for future trail maintenance. The Board also authorized specific project expenditures of \$114,820 to be charged against this fund balance designation. However, expenditures entered into the accounting system were not properly coded, resulting in \$256,674 being charged against the designated fund balance. An audit adjustment was required to correctly report the designated fund balance of \$360,180 in the financial statements.

We recommend the Authority develop procedures to ensure that the financial transactions for the fund balance unreserved, designated for future trail maintenance are properly coded, recorded, and reflected in its financial statements. The procedures should allow the Authority to identify and monitor the capital asset additions, project expenditures, and fund balance accounts for this activity. The Authority's project records should be reconciled on a regular basis with the reports from the accounting system maintained by the fiscal agent.

Client's Response:

Management has worked with St. Louis County Auditor's Office to put into place a coding system that will identify expenditures and financial transactions dedicated for future trail maintenance funds. This procedure was enacted January 2012.

II. OTHER ITEM FOR CONSIDERATION

GASB Statement 54

The Governmental Accounting Standards Board's (GASB) Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, is effective for the Authority for the year ending December 31, 2011. The standard's objectives are to enhance the usefulness of fund balance information included in the financial report through clearer fund balance classifications that can be consistently applied and to clarify existing governmental fund type definitions.

Fund Balance Reporting

Statement 54 establishes new fund balance classifications based on constraints imposed on how resources can be spent. The existing components of fund balance are reserved, unreserved-designated, and unreserved-undesignated. GASB Statement 54 replaces these components with nonspendable, restricted, committed, assigned, and unassigned as defined below:

- *Nonspendable* - amounts that cannot be spent because they are either not in spendable form (for example, inventory or prepaid items) or legally or contractually required to be maintained intact (such as the corpus of a permanent fund).
- *Restricted* - amounts that can be spent only for specific purposes stipulated by constitution, external resource providers, or through enabling legislation.
- *Committed* - amounts that can be used only for specific purposes determined by a formal action of a government's highest level of decision-making authority.
- *Assigned* - amounts a government intends to use for a specific purpose that do not meet the criteria to be classified as restricted or committed.
- *Unassigned* - spendable amounts not contained in the other classifications.

Steps to consider with implementation of the new fund balance classifications:

- review the requirements of GASB Statement 54;
- review current fund balances and compare to the new classifications;
- reclassify January 1, 2011, fund balance using the new classifications;
- review/update/prepare a comprehensive fund balance policy;
- prepare appropriate Board resolutions to commit fund balance; and
- if the Board intends to delegate authority to assign fund balance, prepare the resolutions delegating that authority.

Additional implementation steps could include deciding on how fund balance will be presented in the financials, for example, detailed vs. aggregate methods, and developing the potential note disclosures. Additional guidance on GASB Statement 54 can be found on the Office of the State Auditor's website at:

http://www.auditor.state.mn.us/other/Statements/fundbalances_postGASB54_1012_state_ment.pdf.



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

Board of Directors
St. Louis and Lake Counties
Regional Railroad Authority

We have audited the financial statements of the governmental activities and the General Fund of the St. Louis and Lake Counties Regional Railroad Authority as of and for the year ended December 31, 2010, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated March 23, 2012. 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 the St. Louis and Lake Counties Regional Railroad Authority'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 Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Recommendations, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

A deficiency in internal control over financial reporting 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 and correct, misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the Authority's financial statements will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings and Recommendations as items 03-1, 09-1, and 10-1 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the St. Louis and Lake Counties Regional Railroad Authority'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 Political Subdivisions*, 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 Political Subdivisions* 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, except we did not test for the following: public indebtedness, because the Authority did not issue any debt; deposits and investments and claims and disbursements, because they are tested in conjunction with the audit of St. Louis County.

The results of our tests indicate that for the items tested, the St. Louis and Lake Counties Regional Railroad Authority complied with the material terms and conditions of applicable legal provisions.

Also included in the Schedule of Findings and Recommendations is an other item for consideration. We believe this information to be of benefit to the Authority, and it is reported for that purpose.

The Authority's written responses to the internal control findings identified in our audit have been included in the Schedule of Findings and Recommendations. We did not audit the Authority's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the Board of Directors, management, and others within the St. Louis and Lake Counties Regional Railroad Authority and is not intended to be, and should not be, used by anyone other than those specified parties.

/s/Rebecca Otto

/s/Greg Hierlinger

REBECCA OTTO
STATE AUDITOR

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

March 23, 2012