STATE OF MINNESOTA

Office of the State Auditor

Rebecca Otto
State Auditor

MINNESOTA VALLEY REGIONAL RAIL AUTHORITY
REDWOOD FALLS, MINNESOTA

FOR THE YEAR ENDED DECEMBER 31, 2012

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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MINNESOTA VALLEY REGIONAL RAIL AUTHORITY REDWOOD FALLS, MINNESOTA

For the Year Ended December 31, 2012

Audit Practice Division
Office of the State Auditor
State of Minnesota

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MINNESOTA VALLEY REGIONAL RAIL AUTHORITY
REDWOOD FALLS, MINNESOTA

TABLE OF CONTENTS

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Introductory Section

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MINNESOTA VALLEY REGIONAL RAIL AUTHORITY
REDWOOD FALLS, MINNESOTA

ORGANIZATION
2012

Name	Office	Term Expires
Bob Fox*	Chair	Appointed Yearly
Tom Workman	Vice Chair	Appointed Yearly
Sharon Hollatz	Secretary/Treasurer	Appointed Yearly
Ron Antony	Member	Appointed Yearly
Harold Pettis	Member	Appointed Yearly
Scott Blumhoefer	Member	Appointed Yearly
Julie Rath	Administrator	Appointed Yearly
David Schauer	Legal Counsel	Appointed Yearly

*Chair 2012 and 2013

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Financial Section

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STATE OF MINNESOTA
OFFICE OF THE STATE AUDITOR

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INDEPENDENT AUDITOR'S REPORT

Board Members
Minnesota Valley Regional Rail Authority

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities and the General Fund of the Minnesota Valley Regional Rail Authority as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements
Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility
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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Authority's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

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 Minnesota Valley Regional Rail Authority as of December 31, 2012, and the respective changes in financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Required Supplementary Information as listed in the table of contents be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Supplementary Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Minnesota Valley Regional Rail Authority's basic financial statements. The supplementary information as listed in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements. The supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 31, 2013, on our consideration of the Minnesota Valley Regional Rail 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* in considering the Minnesota Valley Regional Rail Authority's internal control over financial reporting and compliance.

Report on Schedule of Expenditures of Federal Awards Required by OMB Circular A-133

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the basic financial statements. The accompanying Schedule of Expenditures of Federal Awards (SEFA) 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 is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the SEFA is fairly stated in all material respects in relation to the basic financial statements as a whole.

/s/Rebecca Otto	*/s/Greg Hierlinger*
REBECCA OTTO STATE AUDITOR	GREG HIERLINGER, CPA DEPUTY STATE AUDITOR

October 31, 2013

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MANAGEMENT’S DISCUSSION AND ANALYSIS

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MINNESOTA VALLEY REGIONAL RAIL AUTHORITY
REDWOOD FALLS, MINNESOTA

MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2012
(Unaudited)

As management of the Minnesota Valley Regional Rail Authority, we offer the readers of the Authority's financial statements this narrative overview and analysis of its financial activities for the fiscal year ended December 31, 2012. Since this information is designed to focus on the current year's activities, resulting changes, and currently known facts, it should be read in conjunction with the financial statements. All amounts, unless otherwise indicated, are expressed in whole dollars.

FINANCIAL REPORTING ENTITY

The Minnesota Valley Regional Rail Authority was established June 21, 1982, under the Regional Railroad Authorities Act, Minn. Stat. § 398A.03. The Authority is governed by a Board composed of one member from the Board of County Commissioners of Carver County, Redwood County, Renville County, Sibley County, and Yellow Medicine County, and a representative from the Shipper's Association. The Authority is organized with a chair, a vice chair, and a secretary/treasurer.

FINANCIAL HIGHLIGHTS

The assets of the Minnesota Valley Regional Rail Authority exceeded its liabilities by $20,616,030 (net position), of which $20,373,383 is net investment in capital assets (Exhibit 1), leaving unrestricted net position of $242,647.

The Authority's total net position increased $4,291,137 in 2012. This is attributable to an increase in intergovernmental revenues for the investment in capital assets.

OVERVIEW OF THE FINANCIAL STATEMENTS

This Management's Discussion and Analysis (MD&A) is intended to serve as an introduction to the basic financial statements. The Minnesota Valley Regional Rail Authority's basic financial statements consist of two statements that combine government-wide financial statements and fund financial statements and notes to the financial statements. The MD&A (this section) is required to accompany the basic financial statements and, therefore, is included as required supplementary information.

The first column of each of the first two statements presents governmental fund data. These columns focus on how money flows in and out and the balances left at year-end that are available for spending. They 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. These columns provide a detailed short-term view of the Authority's operations and the basic services it provides. Governmental fund information helps determine whether there are more or fewer financial resources that can be spent in the near future to finance the Authority's programs. We reconcile the relationship (or differences) between governmental funds and governmental activities (reported in the third column) in the center column of each statement.

The third column in each statement presents the governmental activities Statement of Net Position and the Statement of Activities, which provide information about the activities of the Authority as a whole and present a longer-term view of the Authority's finances. These columns 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. Over time, increases or decreases in the Authority's net position are one indicator of whether its financial health is improving or deteriorating.

Governmental Fund

As compared to 2011, 2012 revenues for the Authority's General Fund increased by $1,057,211 and expenditures increased $66,833.

The General Fund balance increased by $543,818 for a total unassigned fund balance of $213,280.

The Minnesota Valley Regional Rail Authority adopts an annually appropriated budget for its General Fund. A budgetary comparison schedule has also been provided as required supplementary information for this fund to demonstrate compliance with the budget.

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

Government-Wide Financial Analysis

Over time, net position serves as a useful indicator of the Authority's financial position. The Minnesota Valley Regional Rail Authority's assets exceeded liabilities by $20,616,030 at the close of 2012. The largest portion of the Authority's net position reflects the Authority's investment in capital assets (for example, land, buildings, equipment and infrastructure, such as the rail bed), less any related debt (still outstanding) used to acquire those assets. However, it should be noted that these assets are not available for future spending or for liquidating any remaining debt.

Governmental Activities
Net Position

	2012	2011
Assets		
Current and other assets	$ 490,044	$ 979,429
Capital assets	25,122,592	21,056,347
Total Assets	$ 25,612,636	$ 22,035,776
Liabilities		
Long-term liabilities	$ 4,749,209	$ 4,893,429
Other liabilities	247,397	817,454
Total Liabilities	$ 4,996,606	$ 5,710,883
Net Position		
Net investment in capital assets	$ 20,373,383	$ 16,162,918
Unrestricted	242,647	161,975
Total Net Position	$ 20,616,030	$ 16,324,893

Governmental Activities

The Minnesota Valley Regional Rail Authority's activities increased the Authority's net position during 2012 by $4,291,137, representing a 26.3 percent increase, primarily because of the Authority's increase in intergovernmental revenues for the investment in capital assets. Key elements in this increase in net position are as follows:

Governmental Activities
Changes in Net Position

	2012	2011
Revenues		
Program revenues		
Charges for services	$ 107,220	$ 93,225
Licenses and permits	142,856	131,943
Intergovernmental	4,766,704	4,729,718
Capital contributions	-	30,000
General revenues		
Interest earnings	11,833	3,207
Miscellaneous	69,300	38,268
Total Revenues	$ 5,097,913	$ 5,026,361
Expenses		
Program expenses		
Economic development	806,776	789,409
Increase in Net Position	$ 4,291,137	$ 4,236,952
Net Position - January 1	16,324,893	12,087,941
Net Position - December 31	$ 20,616,030	$ 16,324,893

General Fund Budgetary Highlights

There were no differences between the original General Fund expenditure budget and the final budget in 2012.

Actual General Fund revenues exceeded budgeted revenues by $5,321,559, primarily due to more pass-through intergovernmental revenues recognized than anticipated.

Actual expenditures exceeded budgeted expenditures by $4,775,741. The more-than-expected expenditures reflect more-than-anticipated rehabilitation costs.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The Minnesota Valley Regional Rail Authority's depreciable capital assets at December 31, 2012, totaled $19,876,477 (net of accumulated depreciation). This investment in capital assets includes land improvements, buildings, and equipment. The Authority's investment in construction in progress increased $4,655,115 from the previous year due to construction on a rail project.

Capital Assets at Year-End
(Net of Depreciation)

	2012	2011
Capital assets not depreciated		
Land	$ 591,000	$ 591,000
Construction in progress	4,655,115	-
Total capital assets not depreciated	$ 5,246,115	$ 591,000
Capital assets depreciated		
Land improvements	$ 23,428,779	$ 23,428,779
Buildings	63,000	63,000
Machinery and equipment	4,000	4,000
Total capital assets depreciated	$ 23,495,779	$ 23,495,779
Less: accumulated depreciation for		
Land improvements	$ 3,577,502	$ 2,991,782
Buildings	37,800	34,650
Machinery and equipment	4,000	4,000
Total accumulated depreciation	$ 3,619,302	$ 3,030,432
Total capital assets depreciated, net	$ 19,876,477	$ 20,465,347
Total Capital Assets, Net	$ 25,122,592	$ 21,056,347

Additional information on the Authority's capital assets can be found in the notes to the financial statements.

Long-Term Debt

At the end of the current fiscal year, the Authority had total outstanding debt of $4,749,209. Other liabilities and contingencies are described in the notes to the financial statements.

Outstanding Debt

	2012	2011
State loan	$ 4,589,209	$ 4,693,429
Operator loan	160,000	200,000
Total	$ 4,749,209	$ 4,893,429

The Authority received these interest-free rehabilitation loans under Minn. Stat. § 222.50 to provide assistance for improvement of rail service in the state. The state will provide 80 percent of the rehabilitation costs, up to $4,800,000; the shippers will provide ten percent, up to $600,000; and the Authority will provide ten percent, up to $600,000, which the operator will provide in the form of in-kind work. Repayment to the operator will be 15 annual payments of $40,000 each to be funded from the Authority's annual MIC payment. The loans will be paid from the Authority's rents as received from the operator.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS

For 2013-14, we are nearing the end of the authorized funding appropriations from the federal government and state bonding dollars for our project. There is approximately $1.7 million in authorized bonding funds available, and we plan to use this balance to complete bridge upgrades to 286,000 lbs. standards. There needs to be amended language to the bond authorization before we can move ahead with the use of the funds.

New sources of funding will continue to be pursued for the remaining 60 miles of track and multiple bridges that need to be repaired or replaced to reach the 286,000 lbs. standard for rail cars of this size.

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the Minnesota Valley Regional Rail Authority's finances. Questions concerning any of the information provided in this report, or requests for additional financial information, should be addressed to Julie Rath, Administrator; Minnesota Valley Regional Rail Authority; 200 South Mill Street; Redwood Falls, Minnesota 56283.

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BASIC FINANCIAL STATEMENTS

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MINNESOTA VALLEY REGIONAL RAIL AUTHORITY
REDWOOD FALLS, MINNESOTA

EXHIBIT 1

STATEMENT OF NET POSITION OF GOVERNMENTAL ACTIVITIES AND GOVERNMENTAL FUND BALANCE SHEET DECEMBER 31, 2012

	General Fund	Adjustments	Governmental Activities
Assets			
Cash and pooled investments	$ 164,981	$ -	$ 164,981
Accounts receivable	101,690	-	101,690
Due from other governments	223,373	-	223,373
Capital assets			
Non-depreciable	-	5,246,115	5,246,115
Depreciable - net	-	19,876,477	19,876,477
Total Assets	**$ 490,044**	**$ 25,122,592**	**$ 25,612,636**
Liabilities and Fund Balance/Net Position			
Liabilities			
Current liabilities			
Accounts payable	$ 37,815	$ -	$ 37,815
Contracts payable	209,582	-	209,582
Deferred revenue - unavailable	29,367	(29,367)	-
Long-term liabilities			
Due within one year	-	142,165	142,165
Due in more than one year	-	4,607,044	4,607,044
Total Liabilities	**$ 276,764**	**$ 4,719,842**	**$ 4,996,606**
Fund Balance			
Unassigned	213,280	**$ (213,280)**	
Net Position			
Net investment in capital assets		$ 20,373,383	$ 20,373,383
Unrestricted		242,647	242,647
Total Net Position		**$ 20,616,030**	**$ 20,616,030**
Total Liabilities and Fund Balance/Net Position	**$ 490,044**	**$ 25,122,592**	**$ 25,612,636**

Reconciliation of the General Fund Balance to Net Position	
Fund Balance - General Fund	$ 213,280
Long-term assets deferred in the governmental fund	29,367
Capital assets are reported in the Statement of Net Position but not in the Fund Balance Sheet.	25,122,592
Long-term liabilities are reported in the Statement of Net Position but not in the Fund Balance Sheet.	(4,749,209)
Net Position - Governmental Activities	**$ 20,616,030**

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

MINNESOTA VALLEY REGIONAL RAIL AUTHORITY
REDWOOD FALLS, MINNESOTA

EXHIBIT 2

STATEMENT OF ACTIVITIES OF GOVERNMENTAL ACTIVITIES AND GOVERNMENTAL FUND REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE FOR THE YEAR ENDED DECEMBER 31, 2012

	General Fund	Adjustments	Governmental Activities
Revenues			
Licenses and permits	$ 142,856	$ -	$ 142,856
Intergovernmental	5,245,426	(478,722)	4,766,704
Charges for services	107,220	-	107,220
Investment earnings	11,833	-	11,833
Miscellaneous	53,724	15,576	69,300
Total Revenues	**$ 5,561,059**	**$ (463,146)**	**$ 5,097,913**
Expenditures/Expenses			
Current			
Economic development			
Administration	$ 65,022	$ -	$ 65,022
Rehabilitation	4,738,003	(4,066,245)	671,758
Transportation	5,002	-	5,002
Repairs and maintenance	64,994	-	64,994
Debt service			
Principal	144,220	(144,220)	-
Total Expenditures/Expenses	**$ 5,017,241**	**$ (4,210,465)**	**$ 806,776**
Net Change in Fund Balance/Net Position	**$ 543,818**	**$ 3,747,319**	**$ 4,291,137**
Fund Balance/Net Position - January 1	**(330,538)**	**16,655,431**	**16,324,893**
Fund Balance/Net Position - December 31	**$ 213,280**	**$ 20,402,750**	**$ 20,616,030**

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

EXHIBIT 2
(Continued)

STATEMENT OF ACTIVITIES OF GOVERNMENTAL ACTIVITIES AND GOVERNMENTAL FUND REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE FOR THE YEAR ENDED DECEMBER 31, 2012

Reconciliation of the Statement of General Fund Revenues, Expenditures, and Changes in Fund Balance to the Statement of Activities				
Net change in fund balance			**$**	**543,818**
In the funds, under the modified accrual basis, receivables not available for expenditure are deferred. In the statement of activities, those revenues are recognized when earned. The adjustment to revenues between the fund statements and the statement of activities is the increase or decrease in revenues deferred as unavailable.				
Deferred revenue - December 31	**$**	29,367		
Deferred revenue - January 1		(492,513)		(463,146)
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. The adjustment is the amount by which capital outlay exceeded depreciation expense in the current period.				
Expenditures for general capital assets and infrastructure	**$**	4,655,115		
Current year depreciation		(588,870)		4,066,245
Incurring long-term debt provides current financial resources to governmental funds, while the repayment of long-term debt consumes the current financial resources of the funds. Neither transaction, however, has any effect on net position. The adjustment is the payments on debt.				144,220
Change in Net Position of Governmental Activities			**$**	**4,291,137**

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1. Summary of Significant Accounting Policies

The Minnesota Valley Regional Rail Authority's financial statements are prepared in accordance with generally accepted accounting principles (GAAP) for the year ended December 31, 2012. The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (statements and interpretations). The more significant accounting policies established in GAAP and used by the Minnesota Valley Regional Rail Authority are discussed below.

A. Financial Reporting Entity

The Minnesota Valley Regional Rail Authority was established June 21, 1982, under the Regional Railroad Authorities Act, Minn. Stat. § 398A.03. It is governed by a Board composed of one member from the Boards of Commissioners of Carver County, Redwood County, Renville County, Sibley County, and Yellow Medicine County, and a representative from the Shipper's Association. The Authority is organized with a chair, a vice chair, and a secretary/treasurer.

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.

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 position is reported in two parts: net investment in capital assets and unrestricted net position. The statement of activities demonstrates the degree to which the expenses of the Authority are offset by revenues.

1. Summary of Significant Accounting Policies

B. Basic Financial Statements (Continued)

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 columns 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.

The governmental fund column (General Fund) is 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 Minnesota Valley Regional Rail Authority considers all revenues as available if collected within 60 days after the end of the current period. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met and are available. Charges for services and interest are considered to be susceptible to accrual. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on long-term debt 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 are reported as other financing sources.

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

D. Assets, Liabilities, and Net Position or Equity

1. Deposits and Investments

Deposits and investments are reported at their fair value at December 31, 2012, based on market price.

1. Summary of Significant Accounting Policies

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

2. Receivables

The financial statements of the Authority contain no allowance for uncollectible accounts. Uncollectible amounts due for receivables are recognized as bad debts at the time information becomes available that would indicate the uncollectibility of the particular receivable. These amounts are not considered to be material in relation to the financial position or operations of the fund.

3. Capital Assets

Capital assets are defined by the Authority as assets with an initial cost of more than $4,000 and an estimated useful life in excess of two years. Capital assets are reported at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are to be 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 the assets' lives are not capitalized.

Capital assets are depreciated using the straight-line method over the following estimated useful lives:

Assets	Years
Land improvements	40
Buildings	20
Machinery and equipment	5

4. Deferred Revenue

Governmental funds and governmental activities defer revenue for resources that have been received, but not yet earned. Governmental funds also report deferred revenue in connection with receivables for revenues not considered to be available to liquidate liabilities of the current period.

1. Summary of Significant Accounting Policies

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

5. Long-Term Liabilities

Long-term liabilities are not reported in the fund. The General Fund reports only liabilities expected to be financed with available, spendable financial resources. The statement of net position reports long-term liabilities of the governmental activities.

6. Classification of Net Position

Net position in the government-wide financial statements is classified in the following categories:

Net investment in capital assets - the amount of net position representing capital assets, net of accumulated depreciation, and reduced by outstanding debt attributed to the acquisition, construction, or improvement of the assets.

Restricted net position - the amount of net position for which external restrictions have been imposed by creditors, grantors, contributors, or laws or regulations of other governments and restrictions imposed by law through constitutional provisions or enabling legislation.

Unrestricted net position - the amount of net position that does not meet the definition of restricted or net investment in capital assets.

7. Classification of Fund Balances

Fund balance is divided into five classifications based primarily on the extent to which the Authority is bound to observe constraints imposed upon the use of the resources in the governmental funds. The classifications are as follows:

Nonspendable - amounts that cannot be spent because they are not in spendable form, or are legally or contractually required to be maintained intact. The “not in spendable form” criterion includes items that are not expected to be converted to cash.

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Position or Equity

7. Classification of Fund Balances (Continued)

Restricted - amounts in which constraints have been placed on the use of resources either externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or by law through constitutional provisions or enabling legislation.

Committed - amounts that can be used only for the specific purposes imposed by formal action (resolution) of the Authority's Board. Those committed amounts cannot be used for any other purpose unless the Board removes or changes the specified use by taking the same type of action (resolution) it employed to previously commit those amounts.

Assigned - amounts the Authority intends to use for specific purposes that do not meet the criteria to be classified as restricted or committed. In the General Fund, assigned amounts represent intended uses established by the Authority's Board.

Unassigned - the residual classification for the General Fund and includes all spendable amounts not contained in the other fund balance classifications.

The Authority applies restricted resources first when expenditures are incurred for purposes for which either restricted or unrestricted (committed, assigned, and unassigned) amounts are available. Similarly, within unrestricted fund balance, committed amounts are reduced first, followed by assigned, and then unassigned amounts when expenditures are incurred for purposes for which amounts in any of the unrestricted fund balance classifications could be used.

8. 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

A. Assets

1. Deposits and Investments

The following table presents the Authority's cash and deposit balances at December 31, 2012:

Checking	$	98,530
Certificates of deposit		66,451
Total Cash and Investments	$	164,981

During the year ended December 31, 2012, the Authority had no investments other than certificates of deposit.

a. Deposits

The Authority is authorized by Minn. Stat. §§ 118A.02 and 118A.04 to designate a depository for public funds and to invest in certificates of deposit. The Authority is required by Minn. Stat. § 118A.03 to protect deposits with 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 and 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, 2012, the Authority's deposits were not exposed to custodial credit risk.

2. Detailed Notes

A. Assets

1. Deposits and Investments (Continued)

b. Investments

The Authority may invest in the following types of investments as authorized by Minn. Stat. §§ 118A.04 and 118A.05:

(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.

2. Detailed Notes

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 Authority does not have a policy to address this risk.

Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. The Authority does not have a policy to address this risk.

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 Authority does not have a policy to address this risk. On December 31, 2012, the Authority's investments were not exposed to custodial credit risk.

Concentration of Credit Risk

The concentration of credit risk is the risk of loss that may be caused by the Authority's investment in a single issuer. The Authority does not have a policy to address this risk.

2. Detailed Notes

A. Assets (Continued)

2. Receivables

Receivables as of December 31, 2012, for the Authority follow:

	Receivables	Amounts Not Scheduled for Collection During the Subsequent Year
Accounts receivable	$ 101,690	$ -
Due from other governments	223,373	-
Total	$ 325,063	$ -

3. Capital Assets

Capital asset activity for the year ended December 31, 2012, was as follows:

	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets not depreciated				
Land	$ 591,000	$ -	$ -	$ 591,000
Construction in progress	-	4,655,115	-	4,655,115
Total capital assets not depreciated	$ 591,000	$ 4,655,115	$ -	$ 5,246,115
Capital assets depreciated				
Land improvements	$ 23,428,779	$ -	$ -	$ 23,428,779
Buildings	63,000	-	-	63,000
Machinery and equipment	4,000	-	-	4,000
Total capital assets depreciated	$ 23,495,779	$ -	$ -	$ 23,495,779
Less: accumulated depreciation for				
Land improvements	$ 2,991,782	$ 585,720	$ -	$ 3,577,502
Buildings	34,650	3,150	-	37,800
Machinery and equipment	4,000	-	-	4,000
Total accumulated depreciation	$ 3,030,432	$ 588,870	$ -	$ 3,619,302
Total capital assets depreciated, net	$ 20,465,347	$ (588,870)	$ -	$ 19,876,477
Governmental Activities Capital Assets, Net	$ 21,056,347	$ 4,066,245	$ -	$ 25,122,592

2. Detailed Notes

A. Assets

3. Capital Assets (Continued)

Depreciation expense of $588,870 was charged to the Authority's economic development function for the year ended December 31, 2012.

B. Liabilities

1. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2012, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
State loan	$ 4,693,429	$ -	$ 104,220	$ 4,589,209	$ 102,165
Operator loan	200,000	-	40,000	160,000	40,000
Total	$ 4,893,429	$ -	$ 144,220	$ 4,749,209	$ 142,165

The Authority received these interest-free rehabilitation loans under Minn. Stat. § 222.50 to provide assistance for improvement of rail service in the state. The state will provide 80 percent of the rehabilitation costs, up to $4,800,000; the shippers will provide 10 percent, up to $600,000; and the Authority will provide 10 percent, up to $600,000, which the operator will provide in the form of in-kind work. Repayment to the operator will be 15 annual payments of $40,000 each, to be funded from the Authority's annual Worldcom payment. The loans will be paid from the Authority's rents as received from the operator. Therefore, the amount due within one year is an estimate as the exact amount cannot be determined. The state's portion is secured by a mortgage on the Authority's property.

2. Detailed Notes

B. Liabilities

1. Changes in Long-Term Liabilities (Continued)

Annual debt service requirements to maturity for the operator loan as of December 31, 2012, are:

Year Ended	Operator
2013	$ 40,000
2014	40,000
2015	40,000
2016	40,000
Total	$ 160,000

2. Construction Commitments

The government has active construction projects and other commitments as of December 31, 2012. The projects and commitments include the following:

	Spent-to-Date	Remaining Commitment
Rail line rehabilitation project	$ 4,325,000	$ 316,650

3. 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; and natural disasters. To manage these risks, the Authority has joined the Minnesota Counties Intergovernmental Trust (MCIT). MCIT is a public entity risk pool currently operated as a common risk management and insurance program for its members. 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 previous year or settlements in excess of insurance coverage for any of the past three fiscal years.

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REQUIRED SUPPLEMENTARY INFORMATION

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MINNESOTA VALLEY REGIONAL RAIL AUTHORITY
REDWOOD FALLS, MINNESOTA

EXHIBIT A-1

BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2012

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Revenues				
Licenses and permits	$ 123,100	$ 123,100	$ 142,856	$ 19,756
Intergovernmental	-	-	5,245,426	5,245,426
Charges for services	100,000	100,000	107,220	7,220
Investment earnings	100	100	11,833	11,733
Miscellaneous	16,300	16,300	53,724	37,424
Total Revenues	**$ 239,500**	**$ 239,500**	**$ 5,561,059**	**$ 5,321,559**
Expenditures				
Current				
Economic development				
Administration	$ 60,350	$ 60,350	$ 65,022	$ (4,672)
Rehabilitation	40,550	40,550	4,738,003	(4,697,453)
Transportation	600	600	5,002	(4,402)
Repairs and maintenance	-	-	64,994	(64,994)
Debt service				
Principal	140,000	140,000	144,220	(4,220)
Total Expenditures	**$ 241,500**	**$ 241,500**	**$ 5,017,241**	**$ (4,775,741)**
Change in Fund Balance	**$ (2,000)**	**$ (2,000)**	**$ 543,818**	**$ 545,818**
Fund Balance - January 1	**(330,538)**	**(330,538)**	**(330,538)**	**-**
Fund Balance - December 31	**$ (332,538)**	**$ (332,538)**	**$ 213,280**	**$ 545,818**

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

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NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION
FOR THE YEAR ENDED DECEMBER 31, 2012

1. General Budget Policies

   The Minnesota Valley Regional Rail Authority's Board adopts an estimated revenue and expenditure budget for the General Fund. The budget is prepared on the modified accrual basis of accounting.

   The budgets may be amended or modified at any time by the Authority's Board. Expenditures may not legally exceed budgeted appropriations. Comparisons of final budgeted revenues and expenditures to actual are presented as required supplementary information.

2. Budget Basis of Accounting

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

3. Budget Amendments

   The Authority did not amend its expenditure budget during 2012.

4. Excess of Expenditures Over Budget

   For the year ended December 31, 2012, expenditures exceeded the budgeted appropriations by $4,775,741 in the General Fund.

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SUPPLEMENTARY INFORMATION

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MINNESOTA VALLEY REGIONAL RAIL AUTHORITY
REDWOOD FALLS, MINNESOTA

EXHIBIT B-1

SCHEDULE OF INTERGOVERNMENTAL REVENUE
FOR THE YEAR ENDED DECEMBER 31, 2012

Reimbursement for Services		
Sibley County	**$**	**54,172**
Grants		
State		
Minnesota Department of		
Natural Resources	$	13,350
Public Safety		8,717
Transportation		3,190,130
Total state	**$**	**3,212,197**
Federal		
Department of		
Homeland Security	$	29,057
Transportation Federal Railroad Administration (FRA)		1,950,000
Total federal	**$**	**1,979,057**
Total state and federal grants	**$**	**5,191,254**
Total Intergovernmental Revenue	**$**	**5,245,426**

MINNESOTA VALLEY REGIONAL RAIL AUTHORITY
REDWOOD FALLS, MINNESOTA

EXHIBIT B-2

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2012

Federal Grantor Pass-Through Agency Grant Program Title	Federal CFDA Number	Expenditures
U.S. Department of Transportation Federal Railroad Administration (FRA)		
Passed Through Minnesota Department of Transportation		
Rail Line Relocation and Improvement	20.320	$ 1,950,000
U.S. Department of Homeland Security		
Passed Through Minnesota Department of Public Safety		
Disaster Grants - Public Assistance (Presidentially Declared Disasters)	97.036	29,057
Total Federal Awards		**$ 1,979,057**

The notes to the Schedule of Expenditures of Federal Awards are an integral part of this schedule.

MINNESOTA VALLEY REGIONAL RAIL AUTHORITY
REDWOOD FALLS, MINNESOTA

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2012

1. Reporting Entity

The Schedule of Expenditures of Federal Awards presents the activities of federal award programs expended by the Minnesota Valley Regional Rail Authority. The Authority's reporting entity is defined in Note 1 to the basic financial statements.

2. Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Minnesota Valley Regional Rail Authority under programs of the federal government for the year ended December 31, 2012. The information in this schedule is presented in accordance with the requirements of Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Because the schedule presents only a selected portion of the operations of the Minnesota Valley Regional Rail Authority, it is not intended to and does not present the financial position, or changes in net position of the Authority.

3. Summary of Significant Accounting Policies

Expenditures reported on the schedule are reported on the modified accrual basis of accounting. Such expenditures are recognized following the cost principles contained in OMB Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments*, wherein certain types of expenditures are not allowable or are limited as to reimbursement. Pass-through grant numbers were not assigned by the pass-through agencies.

4. Subrecipients

The Minnesota Valley Regional Rail Authority did not pass any federal awards through to subrecipients during the year ended December 31, 2012.

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Management and Compliance Section

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MINNESOTA VALLEY REGIONAL RAIL AUTHORITY
REDWOOD FALLS, MINNESOTA

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED DECEMBER 31, 2012

I. SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued: **Unmodified**

Internal control over financial reporting:

- Material weaknesses identified? **Yes**
- Significant deficiencies identified? **Yes**

Noncompliance material to the financial statements noted? **No**

Federal Awards

Internal control over major programs:

- Material weaknesses identified? **Yes**
- Significant deficiencies identified? **No**

Type of auditor's report issued on compliance for major programs: **Unmodified**

Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133? **Yes**

The major program is:

Rail Line Relocation and Improvement	CFDA #20.320

The threshold for distinguishing between Types A and B programs was $300,000.

Authority qualified as a low-risk auditee? **No**

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

INTERNAL CONTROL

PREVIOUSLY REPORTED ITEMS NOT RESOLVED

00-1 Segregation of Duties

Criteria: A good system of internal control provides for an adequate segregation of duties so that no one individual handles a transaction from its inception to completion.

Condition: The Minnesota Valley Regional Rail Authority lacks proper segregation of duties. The Authority contracts with the Redwood Area Development Corporation for administrative services where only one staff person performs the tasks related to administrative and accounting functions. As a result, the Authority has one staff person who is responsible for billing, collecting, recording, and depositing receipts as well as reconciling bank accounts.

Context: Due to the limited number of office personnel within the Authority, segregation of the accounting functions necessary to ensure adequate internal accounting control is not possible. This is not unusual in operations the size of the Minnesota Valley Regional Rail Authority; however, the Authority's Board and management should constantly be aware of this condition and realize that the concentration of duties and responsibilities in a limited number of individuals is not desirable from an accounting point of view.

Effect: Inadequate segregation of duties could adversely affect the Authority's ability to detect misstatements in amounts that would be material in relation to the financial statements in a timely period by staff in the normal course of performing their assigned functions.

Cause: The Authority has indicated it does not have the economic resources to hire additional qualified accounting staff to adequately segregate the accounting functions.

Recommendation: We recommend that the Authority's Board and management be aware of the lack of segregation of duties of the accounting functions and, where possible, implement oversight procedures to ensure the internal control policies and procedures are implemented to the extent possible.

Client's Response:

The Minnesota Valley Regional Rail Authority (MVRRA) is well aware of the fact that the Redwood Area Development Corporation (RADC) has a limited staff that is working under contract with MVRRA to provide administrative services including their bookkeeping needs on a monthly basis. It has been this way since 2003 when the arrangements were made to provide these services to MVRRA. On a monthly basis the Treasurer signs checks and approves the bank reconciliation, and the bills are approved at the monthly meetings. Staff does not have the ability to sign any of the checks written on behalf of the Rail Authority. In 2014, we are looking to go to a rail property management agreement, and then all of the licenses, annual fees, and billings will be done by an outside third party which will be cloud-based and the money will be direct deposited into our accounts. RADC will only provide the regular bookkeeping services for monthly expenditures.

07-1 Audit Adjustment

Criteria: A deficiency in internal control over financial reporting exists when the design or operation of a control does not allow management or staff, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements of the financial statements on a timely basis. Clarified Auditing Standards AU-C Section 265 defines a material weakness as a deficiency, or combination of deficiencies, in internal control 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.

Condition: During our audit, we identified a material adjustment that resulted in a significant change to the Authority's financial statements. The Authority 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.

Context: The inability to make accrual adjustments or to detect significant misstatements in the financial statements increases the likelihood that the financial statements would not be fairly presented. Some of the adjustments required additional time by the auditors to determine the correct balances.

Effect: During our audit, we proposed an adjustment to convert the Authority's financial records to the financial statements as reported. A material audit adjustment was necessary in the General Fund to increase expenditures and contracts payable liability by $209,582 for work completed on the rail line rehabilitation project in 2012 but not paid until 2013.

Cause: Authority staff did not detect the error in the normal course of performing their assigned functions.

Recommendation: We recommend that Authority 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 Authority. We also recommend the Authority establish internal controls necessary to determine that all adjusting entries are made to ensure the Authority's annual financial statements are reported in accordance with generally accepted accounting principles. The controls should include review of the balances and supporting documentation by a qualified individual to identify potential misstatements.

Client's Response:

The MVRRA has made the necessary adjustments during this 2012 audit to correct the two balances in question.

07-2 Capital Assets Policies and Procedures

Criteria: A capital assets policy should be adopted which defines the Authority's accounting policies over capital assets, such as capitalization thresholds, useful lives, and depreciation methods. A physical inventory should be taken of capital assets at least every five years.

Condition: The Authority has not adopted a capital assets policy. No physical inventory of capital assets has been conducted since the records were first established.

Context: The Authority maintains its capital assets records on a spreadsheet. Additions and deletions are entered into this spreadsheet and depreciation is calculated. However, the capital assets policy utilized by the Authority in maintaining the spreadsheet has not been formally approved by the Board.

Effect: Without a written capitalization policy, the Authority may capitalize or depreciate assets inconsistently from year to year. Without a physical inventory of capital assets, it is possible that items that were disposed of will not be properly taken off inventory.

Cause: The Authority has not established or approved a capital assets policy, and no one has been assigned the responsibility of setting up a system to do a physical inventory of capital assets.

Recommendation: We recommend the Authority establish a capital assets policy to define the Authority's accounting policies over capital assets. The policy should also establish procedures to identify capital additions and deletions. Also, we recommend a physical inventory of capital assets be performed at least once every five years. This physical inventory can be rotated so that a portion of the capital assets is inventoried each year.

Client's Response:

The MVRRA is in the process of adopting an accounting and internal controls policy procedural manual which will address this. We will include the threshold, physical inventory every 5 years, and depreciation.

10-2 Documenting and Monitoring Internal Controls

Criteria: The Authority's management is responsible for developing and monitoring its internal controls. This responsibility requires performing an assessment of existing controls over significant functions used to produce financial information for the Authority's Board, management, and for external financial reporting. Written accounting policies and procedures support management's risk identification, evaluation, and mitigation and enables monitoring. Monitoring is required to evaluate whether controls are operating as intended and changes to controls are made when necessary. Significant internal controls to be documented would include areas such as receipts, disbursements, capital assets, and journal entries.

Condition: Inquiries of the Administrator found that significant internal controls of the accounting system have not been documented. The Authority does not have a current and comprehensive accounting policies and procedures manual, including risk assessment and monitoring procedures. Although the Authority may informally assess risks and adjust internal control procedures to address those risks, there are no formal procedures or documentation of those procedures in place.

Context: Documentation and monitoring of internal controls is necessary to determine controls are in place and operating effectively. Changes may be necessary due to such things as organizational restructuring, updates to information systems, or changes to services being provided. An accounting policies and procedures manual provides guidance when staffing changes occur, enhances understanding of roles and functions of those involved in the internal control system, establishes responsibilities, improves efficiency and consistency of transaction processing, and improves compliance with established policies. It can also help to prevent deterioration of key elements in the Authority's internal control system and can help to avoid circumvention of the Authority's policies.

Effect: As a result of this condition, the Authority's practices may not be followed as intended by management, and staff may not understand the purpose of internal controls. Weaknesses in internal control may go undetected, which could affect the Authority's ability to detect material misstatements in the financial statements. The lack of risk assessment and monitoring procedures increases the risk of fraud.

Cause: The Authority's Administrator and Board have not adopted policies related to controls over accounting or financial reporting. There is no formal documentation identifying management's risk assessment process, how current policies and procedures address the identified risks, and how management monitors the controls established to ensure they are working as planned.

Recommendation: We recommend the Authority document the process it uses to identify and respond to risks that may affect accounting or financial reporting. The Authority should establish an accounting policies and procedures manual for significant internal control systems. 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. We recommend the manual be approved by the Authority's Board to emphasize its importance and authority. We also recommend that a formal plan be developed that calls for monitoring internal controls on a regular basis, no less than annually, to determine whether the established internal controls are still effective or if changes are needed. The monitoring activity should also be documented to show the results of the review, any changes required, and who performed the work.

Client's Response:

This will be addressed in the accounting and internal controls policy manual that is being developed. The RADC has its own internal controls policy and this would apply to the MVRRA.

III. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARD PROGRAMS

ITEM ARISING THIS YEAR

12-1 Identification of Federal Awards

Program: U.S. Department of Transportation's Federal Railroad Administration (FRA) Rail Line Relocation and Improvement (CFDA No 20.320).

Pass-Through Agency: Minnesota Department of Transportation

Criteria: OMB Circular A-133, Subpart C, § .300, indicates auditee responsibilities include the identification of all federal awards received and expended and the federal programs under which they were received, including identifying programs funded by the American Recovery and Reinvestment Act (ARRA).

Condition: The Minnesota Valley Regional Rail Authority does not prepare a Schedule of Expenditures of Federal Awards (SEFA), nor does it adequately identify federal programs by amount received and expended, federal grantor agency, pass-through agency, and Catalog of Federal Domestic Assistance (CFDA) title and number as required under OMB Circular A-133. In addition, the Minnesota Valley Regional Rail Authority is not properly identifying federal revenues in the general ledger system. The $1,950,000 of Rail Line Relocation and Improvement grant received was improperly classified as state revenues in the general ledger accounts.

Questioned Costs: None.

Context: In 2012, the Authority expended $1,979,057 in total federal awards.

Effect: The inability to identify and accurately record federal financial assistance in the Authority's accounting records in order to prevent misstatements in the SEFA increases the likelihood that the SEFA would not be fairly stated. This condition results in a deficiency in internal control over SEFA preparation and the reporting of federal financial assistance in accordance with OMB Circular A-133.

Cause: The Authority does not have procedures in place to ensure that federal award programs are adequately identified, accounted for, and reported on the SEFA.

Recommendation: We recommend that Authority management develop a process, including written procedures that will allow staff to adequately identify federal revenues and accumulate the information needed to prepare the SEFA. Specific measures could include holding in suspense accounts until properly identified as to nature and source any intergovernmental revenue receipts, properly classifying the receipts into appropriate federal revenue accounts in the general ledger system, and comparison of the prior year SEFA to the current year. For each federal award identified, the Authority should determine the correct program CFDA title and number, award number and year, federal grantor agency, pass-through agency, amount received and expended, and whether ARRA funding is involved. The federal CFDA website is available to assist in this process. Where a determination is unclear, the pass-through or federal agency should be contacted to verify the federal program in accordance with the requirements of OMB Circular A-133. Those responsible for compiling the SEFA should understand the components of the SEFA and properly gather the correct information and maintain supporting documentation. The Authority should also reconcile the SEFA amounts to the general ledger and financial statements.

Corrective Action Plan:

Name of Contact Person Responsible for Corrective Action:

Julie Rath, MVRRA Administrator

Corrective Action Planned:

Our 2012 Rehab project used our entire Federal appropriation from 2009 for the project so there will not be any federal funding in the future for our projects. The MVRRA will take this under advisement and adopt a policy to address this if the need arises again. In the past we had received Federal funding which was a pass-through from the FRA to the Minnesota Department of Transportation and they handled all the fiscal management of our funding previously so this was new to us for 2012.

Anticipated Completion Date:

June 2014

IV. OTHER FINDINGS AND RECOMMENDATIONS

MANAGEMENT PRACTICES

PREVIOUSLY REPORTED ITEM RESOLVED

Deficit Fund Balance (11-1)

As of December 31, 2011, the General Fund reported a deficit fund balance of $330,538.

Resolution

As of December 31, 2012, the General Fund assets exceeded liabilities, resulting in a positive fund balance of $213,280.

STATE OF MINNESOTA
OFFICE OF THE STATE AUDITOR

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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*

Independent Auditor's Report

Board Members
Minnesota Valley Regional Rail Authority

We have audited, 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, the financial statements of the governmental activities and the General Fund of the Minnesota Valley Regional Rail Authority as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated October 31, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Minnesota Valley Regional Rail Authority's internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances 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 material weaknesses or significant deficiencies and, therefore, material weaknesses may exist that have not been identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified a deficiency in internal control over financial reporting that we consider to be a material weakness and other deficiencies that we consider to be significant deficiencies.

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 deficiency described in the accompanying Schedule of Findings and Questioned Costs as item 07-1 to be a material weakness.

A significant deficiency is a deficiency, or combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs as items 00-1, 07-2, and 10-2 to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Minnesota Valley Regional Rail Authority's financial statements are free from 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

The *Minnesota Legal Compliance Audit Guide for Political Subdivisions*, promulgated by the State Auditor pursuant to Minn. Stat. § 6.65, 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 audit considered all of the listed categories.

In connection with our audit, nothing came to our attention that caused us to believe that the Minnesota Valley Regional Rail Authority failed to comply with the provisions of the *Minnesota Legal Compliance Audit Guide for Political Subdivisions*. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the Authority's noncompliance with the above referenced provisions.

Other Matters

The Minnesota Valley Regional Rail Authority's responses to the internal control findings identified in our audit have been included in the Schedule of Findings and Questioned Costs. The Authority's responses were not subject to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control over financial reporting, compliance and the provisions of the *Minnesota Legal Compliance Audit Guide for Political Subdivisions* and the results of that testing, and not to provide an opinion on the effectiveness of the Authority's internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance. Accordingly, this communication is not suitable for any other purpose.

/s/Rebecca Otto

REBECCA OTTO
STATE AUDITOR

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

October 31, 2013

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REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE

Independent Auditor's Report

Board Members
Minnesota Valley Regional Rail Authority

Report on Compliance for Each Major Federal Program

We have audited the Minnesota Valley Regional Rail Authority's compliance with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that could have a direct and material effect on the Authority's major federal program for the year ended December 31, 2012. The Minnesota Valley Regional Rail Authority's major federal program is identified in the Summary of Auditor's Results section of the accompanying Schedule of Findings and Questioned Costs.

Management's Responsibility
Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its federal programs.

Auditor's Responsibility
Our responsibility is to express an opinion on compliance for the Minnesota Valley Regional Rail Authority's major federal program based on our audit of the types of compliance requirements referred to above. 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 the Minnesota Valley Regional Rail Authority'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 on compliance for the major federal program. However, our audit does not provide a legal determination of the Authority's compliance with those requirements.

Opinion on Each Major Federal Program
In our opinion, the Minnesota Valley Regional Rail Authority complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended December 31, 2012.

Report on Internal Control Over Compliance

Management of the Minnesota Valley Regional Rail Authority is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Authority's internal control over compliance with the types of requirements that could have a direct and material effect on the major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing our opinion on compliance for the major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, 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 Authority's internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as discussed below, we identified a deficiency in internal control over compliance that we consider to be a material weakness.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiency in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as item 12-1 to be a material weakness.

The Minnesota Valley Regional Rail Authority's response to the internal control over compliance finding identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs as a Corrective Action Plan. The Minnesota Valley Regional Rail Authority's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

Purpose of This Report

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

/s/Rebecca Otto	*/s/Greg Hierlinger*
REBECCA OTTO STATE AUDITOR	GREG HIERLINGER, CPA DEPUTY STATE AUDITOR

October 31, 2013