

# STATE OF MINNESOTA

## Office of the State Auditor



**Rebecca Otto**  
**State Auditor**

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**DULUTH AIRPORT AUTHORITY**  
**(A COMPONENT UNIT OF THE**  
**CITY OF DULUTH, MINNESOTA)**

FOR THE YEARS ENDED DECEMBER 31, 2013 & 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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**DULUTH AIRPORT AUTHORITY  
(A COMPONENT UNIT OF THE  
CITY OF DULUTH, MINNESOTA)**

**For the Years Ended December 31, 2013 & 2012**



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

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**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

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**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

ORGANIZATION  
DECEMBER 31, 2013

	<u>Term Ending</u>
Directors	
Kenneth D. Butler	July 1, 2015
Michael G. Lundstrom	July 1, 2015
Patrick Mullen	July 1, 2015
Heather Rand	July 1, 2016
Sue Ross	July 1, 2014
Kenneth J. Stromquist	July 1, 2016
Roger D. Wedin	July 1, 2014
Executive Director	
Tom Werner	
Officers	
President	
Michael G. Lundstrom	
Vice President	
Roger D. Wedin	
Secretary	
Kenneth J. Stromquist	

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REBECCA OTTO  
STATE AUDITOR

# STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

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1-800-627-3529 (Relay Service)

## INDEPENDENT AUDITOR'S REPORT

Mayor and City Council  
City of Duluth

Board of Directors  
Duluth Airport Authority

### Report on the Financial Statements

We have audited the accompanying financial statements of the Duluth Airport Authority, a component unit of the City of Duluth, as of and for the years ended December 31, 2013 and 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 an opinion on these financial statements based on our audits. We conducted our audits 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 opinion.

### ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Duluth Airport Authority as of December 31, 2013 and 2012, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### ***Emphasis of Matter - Change in Accounting Principle***

As discussed in Note 1 to the financial statements, in 2013 the Authority adopted new accounting guidance by implementing the provisions of Governmental Accounting Standards Board (GASB) Statement No. 65, *Items Previously Reported as Assets and Liabilities*, which represents a change in accounting principle. Our opinion is not modified with respect to this matter.

### ***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 GASB, 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 audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Duluth Airport Authority's basic financial statements. The supplementary information, listed in the table of contents, is presented for purposes of additional analysis and is not a required part of the basic financial statements.

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 audits 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 June 6, 2014, on our consideration of the Duluth Airport Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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 Duluth Airport 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 an opinion 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*

REBECCA OTTO  
STATE AUDITOR

*/s/Greg Hierlinger*

GREG HIERLINGER, CPA  
DEPUTY STATE AUDITOR

June 6, 2014

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## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

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**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
DECEMBER 31, 2013  
(Unaudited)**

Our discussion and analysis of the Duluth Airport Authority's (Authority) financial performance provides an overview of the Authority's financial activities for the fiscal year ended December 31, 2013. Please read it in conjunction with the financial statements.

**FINANCIAL HIGHLIGHTS**

- Operating expenses (before depreciation and amortization) increased \$716.8 thousand, or 21.8 percent, compared to fiscal year 2012, due to increased costs for utilities and operating supplies and other services and charges.
- Operating revenues increased \$137.1 thousand, or 3.4 percent, primarily due to the rate increases on space as well as restaurant concessions and parking lot receipts.
- Nonoperating federal and state grant revenues decreased \$17.6 million, or 66.3 percent, from 2012; the decreases are due to the completion of the new terminal project. Total net position decreased \$799.7 thousand, or 0.71 percent, compared to fiscal year 2012.
- Total number of passengers decreased by 8.4 thousand, or 2.6 percent, for a total of 313.8 thousand in 2013. The decrease was due to a reduction in Allegiant flights for part of the winter season.
- Total traffic count as recorded by the FAA tower decreased by 7.7 thousand, or 12.6 percent, to 53,716. Of this figure, approximately 94 percent is commercial and general aviation traffic, with the remaining 6 percent military traffic.
- Landing fee revenues for 2013 decreased by \$15.7 thousand, or 5.8 percent.
- Passenger facility charge revenue decreased by \$4.8 thousand in 2013, or 0.76 percent, compared to 2012, which is attributed to the passenger count decrease from 2012.
- 2013 was only the second full year of collecting customer facility charges (CFCs) which support capital improvements and operating costs associated with rental car occupied space. CFCs collected in 2013 decreased by only \$24 from 2012.

- Total parking lot sales increased by \$51 thousand, or 6 percent, for 2013.
- Total car rental concession sales increased by 7.4 thousand, or 1.6 percent, for 2013.
- The 2012/2013 State Maintenance and Operations Agreement, which became effective October 27, 2011, provided for \$168.6 thousand of state aid.
- The Transportation Security Administration's agreement with the Authority, effective October 1, 2012, through September 30, 2015, reimbursed the Authority 16.5 hours per day for contracted law enforcement personnel, or approximately \$8.5 thousand per month.

## **OVERVIEW OF ANNUAL FINANCIAL REPORT**

The Management's Discussion and Analysis (MD&A) serves as an introduction to the Duluth Airport Authority's financial statements. The MD&A represents management's examination and analysis of the Authority's financial condition and well-being. Summary financial statement data, key financial and operational indicators used in the Authority's strategic plan, budget, and other management tools were used for this analysis.

The financial statements report information about the Authority using full accrual accounting methods as utilized by similar business activities in the private sector.

The financial statements include a statement of net position; a statement of revenues, expenses, and changes in net position; a statement of cash flows; and notes to the financial statements. The statement of net position presents the financial position of the Authority on a full accrual historical cost basis. While the statement of net position provides information about the nature and amount of resources and obligations at year-end, the statement of revenues, expenses, and changes in net position presents the results of the business activities over the course of the fiscal year and information as to how the net position changed during the year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. This statement also provides certain information about the Authority's recovery of its costs.

The statement of cash flows presents changes in cash and cash equivalents resulting from operational, financing, and investing activities. This statement presents cash receipts and cash disbursement information without consideration of the earnings event, when an obligation arises, or depreciation of capital assets.

The notes to the financial statements provide required disclosures and other information that are essential to a full understanding of material data provided in the statements. The notes present information about the Authority's accounting policies, significant account balances and activities, material risks, obligations, commitments, contingencies, and subsequent events, if any. The financial statements were prepared by the Authority's staff from the detailed books and records of the Authority. The financial statements were audited and adjusted during the independent external audit process.

## **SUMMARY OF ORGANIZATION AND BUSINESS**

The Legislative Act of 1969, Chapter 577, as approved on May 22, 1969, authorized the organization of the Authority. The purpose of this act was to promote the public welfare and to serve the public interest, convenience and necessity, promote air navigation and transportation, national, state and local; and to these ends, to develop full potentials of aviation in the City of Duluth as an aviation center; and to provide for the most economical and effective use of aeronautical facilities and services in the City of Duluth; and to this end, the Authority shall cooperate with and assist the federal government and the Director of Aeronautics of this state, and shall seek to coordinate its aeronautic activities with these bodies. This Legislative Act established a Board of seven Directors appointed by the Mayor and conferred upon this Board the power and duty to administer, promote, control, direct, and manage and operate all airports owned. On October 9, 1985, the Bylaws were adopted (amended October 16, 1986, and September 16, 1997). These Bylaws established regular monthly meetings, a term for officers, and the appointment of an Executive Director.

The Duluth Airport Authority's vision is to be the region's center of aviation, supporting economic development by growing travel, cargo, and business services for our customers and communities. Their mission is, "We are committed to providing our customers with superior services in a safe, secure, professional environment."

The Duluth International Airport consists of two runways, which provide take-off and landing facilities for all types of commercial and general aviation aircraft, as well as military aircraft. The main runway 9-27 is 10,152 feet long by 150 feet wide and can handle the world's largest aircraft. The cross runway 3-21 is 5,699 feet long by 150 feet wide. The Duluth International Airport is located on 3,294 acres of land and encompasses approximately one-half of the old Duluth Air Force Base. The Authority also operates Sky Harbor Airport, which is both a sea plane base and a general aviation airport. The landside runway is 3,050 long by 75 feet wide. In the bay, there is also a 10,000-foot by 2,000-foot water runway.

Operating revenue for the Authority comes from a variety of sources including: car rental concessions, parking, space and land rentals, Fixed Base Operator (FBO) concessions, Transportation Security Agency reimbursement for law enforcement, maintenance and operations grant funds from the State of Minnesota, and landing fees. The Authority is self-sufficient and is not subsidized by the City of Duluth for operations or capital improvement costs.

## FINANCIAL ANALYSIS

The following comparative condensed financial statements and other selected information serve as the key financial data and indicators for management, monitoring, and planning.

### Condensed Statement of Net Position (000s)

	FY 2013	FY 2012	FY 2011
Current and other assets	\$ 13,853	\$ 16,311	\$ 5,473
Capital assets	110,891	64,904	70,800
Construction in progress	3,112	50,053	17,416
<b>Total Assets</b>	<b>\$ 127,856</b>	<b>\$ 131,268</b>	<b>\$ 93,689</b>
Current liabilities	\$ 5,248	\$ 10,843	\$ 3,568
Long-term liabilities	11,346	8,363	1,583
<b>Total Liabilities</b>	<b>\$ 16,594</b>	<b>\$ 19,206</b>	<b>\$ 5,151</b>
Net Position			
Invested in capital assets, net of related debt	\$ 110,276	\$ 111,626	\$ 87,974
Unrestricted	986	436	564
<b>Total Net Position</b>	<b>\$ 111,262</b>	<b>\$ 112,062</b>	<b>\$ 88,538</b>

As the table illustrates, net position decreased by \$800 thousand to \$111 million in 2013. The decrease in net position was primarily due to significant changes in capital assets in 2013 with an overall decrease of \$3.4 million, as well as a decrease of \$2.6 million in liabilities.

### Condensed Statement of Revenues, Expenses, and Changes in Net Position (000s)

	FY 2013		FY 2012	FY 2011
	Budget	Actual	Actual	Actual
Total operating revenues	\$ 3,985	\$ 4,213	\$ 4,076	\$ 3,645
Total operating expenses	(9,326)	(12,256)	(8,911)	(9,226)
<b>Income (Loss)</b>	<b>\$ (5,341)</b>	<b>\$ (8,043)</b>	<b>\$ (4,835)</b>	<b>\$ (5,581)</b>
Nonoperating revenues	615	659	659	579
Other revenues	3,128	9,927	29,280	13,423
Nonoperating expenses	(734)	(3,343)	(1,581)	(52)
<b>Change in Net Position</b>	<b>\$ (2,332)</b>	<b>\$ (800)</b>	<b>\$ 23,523</b>	<b>\$ 8,369</b>

## **REVENUES**

Operating revenues increased by \$137.1 thousand, or 3.3 percent, in 2013 relative to 2012. The operating revenue increase is due primarily to the rate and charges changes, which increased space rental in the terminal by \$279.6 thousand. The increased activity in the parking lot also increased revenues by \$51 thousand.

## **EXPENSES**

Duluth Airport Authority's operating expenses increased by \$3,345 thousand to \$12,256 thousand in 2013, up from \$8,911 thousand in 2012. Depreciation changed significantly due to the demolition of the old terminal building as well as including new depreciation on the new terminal building. This change accounted for \$2,558 thousand of the total increase. Utilities expenses increased by \$127 thousand to \$690 thousand in 2013, personal services expenses increased by \$109 thousand and other services and charges increased by \$488 thousand in 2013 compared to 2012.

## **BUDGETARY HIGHLIGHTS**

The Duluth Airport Authority develops an annual operating budget which includes proposed expenses as well as proposed sources of revenue to pay for them. The Authority Board approves the operating budget, and it also receives final approval from the Duluth City Council. The Authority's operating budget remains in effect for the entire fiscal year without being revised. The Authority plans to update the budget quarterly from 2014 going forward. Management and the Board of Directors are presented detailed monthly financial statements as well as an in-depth quarterly analysis of key indicators and budgetary progress.

The airline industry remains competitive and fluid with fuel cost continuing to plague profitability and continued service to smaller and marginally profitable markets. Positive for Duluth, Allegiant Airlines now has had several full and productive years of service to Las Vegas; Phoenix/Mesa; and Sanford, Florida, from Duluth weekly. Additionally, three daily flights from United Airlines between Duluth and its Chicago O'Hare hub have been successfully in place for more than four years. The establishment of additional air service to our market is continually being pursued with various carriers. Finally, Monaco Air continues to have productive and successful operations as the FBO offering quality service with a well-respected reputation. Monaco's services and operations have led to more activity for international, corporate, charter, and general aviation users of the Duluth Airport as well as increased revenues for the Authority.

The Authority continued to make improvements to facilities and infrastructure and respond to new security directives. In 2013, the following projects or additions to projects reached completion and were transferred to fixed asset records: (1) New Terminal Building Construction and Equipment - \$54,311 thousand; (2) Apron Construction - \$1,907 thousand; (3) Master Plan - \$727 thousand; (4) Addition of Hangar 104 - \$704 thousand; (5) Sky Harbor Layout Plan \$60 thousand; (6) Runway Crack Sealing - \$47 thousand, Taxiway repair of \$47 thousand, and a tower roof repair as well as building 103 alarm system - \$16 thousand.

Ground breaking began in 2009 for the new \$77 million Passenger Terminal Building and supporting infrastructure. During 2010, Phase I, consisting of site work, new roadways, infrastructure, and new parking lots, was completed. Phase II, involving New Terminal Building foundation, structure, and enclosure, was completed early 2013. Demolition of the former terminal began on February 1, 2013, with apron completion in the Fall of 2013. Federal, state, and local airport dollars have funded the project. The parking structure ground breaking began in early 2014 and is expected to be completed in the Fall of 2014.

The union contract between the Authority and AFSCME Local 66 was renegotiated with minor changes in 2012 for the 2013 year. The contract was negotiated again in 2013 effective 2014 through December 31, 2016.

**Capital Assets  
(000s)**

	FY 2013	FY 2012	Dollar Change Increase (Decrease)	Total Percent (%) Change
Land	\$ 3,361	\$ 3,361	\$ -	0.00%
Runways	82,172	80,173	1,999	2.49
Buildings	74,840	35,113	39,727	113.14
Equipment	15,866	10,097	5,769	57.14
Construction in progress	3,112	50,053	(46,941)	93.78
<b>Total capital assets</b>	<b>\$ 179,351</b>	<b>\$ 178,797</b>	<b>\$ 554</b>	<b>0.31</b>
Less: accumulated depreciation	(65,349)	(63,841)	(1,508)	2.36
<b>Net Capital Assets</b>	<b>\$ 114,002</b>	<b>\$ 114,956</b>	<b>\$ (954)</b>	<b>0.83</b>

At the end of 2013, the Authority has invested approximately \$179.3 million in capital assets since its inception. The \$554 thousand increase in capital assets this past year is due to several major projects, including the new terminal building construction, and equipment and building repairs.

The Authority recently updated its Airport Capital Improvement Program through 2018, which includes for 2014:

- \$8,648 thousand for the construction of a parking ramp,
- \$790 thousand for the overhead walkway,
- \$265 thousand for air traffic control tower repairs,



- \$295 thousand for Sky Harbor apron reconstruction, and
- \$25 thousand for Sky Harbor apron design.

**DEBT ADMINISTRATION**

The City of Duluth obtained a \$500,000 loan from the Minnesota Investment Fund to remedy soil conditions on Duluth Airport Authority property in support of new business development. On December 20, 2005, the Authority entered into an agreement with the Duluth Economic Development Authority that provided the Authority make payments due on the loan in the amount of \$400,000. The loan is noninterest-bearing, payable in 180 monthly installments of \$2,222 beginning February 2006. The noncurrent portion of the loan payable is \$162,222.

The Authority entered into a Lease Acquisition Agreement with North Country Aviation (NCA) on November 1, 2005. The agreement required the Authority pay NCA \$497,379 in order to acquire NCA’s FBO lease agreement and facilitate its transfer to Monaco Air Duluth. The note is payable by the Authority as Airport Facility Revenue Note, Series 2005A. The note is for a term of 13 years, payable each June 1 and December 1 commencing June 1, 2007. Interest is compounded at 8.85 percent per annum.

**Debt  
(000s)**

A summary of changes in the revenue note balances are:

	<u>FY 2013</u>
Balance - January 1	\$ 365
Additions	-
Payments	<u>44</u>
Balance - December 31	<u>\$ 321</u>

The City of Duluth issued General Obligation Airport Improvement Bonds for the Authority with a face value of \$7,650,000 in May 2012. These bonds will be repaid over 15 years. The bond proceeds are being used as the local match on federal and state grants for the “project” including the terminal, access roads, apron, and parking ramp.

The City of Duluth also issued General Obligation Airport Improvement Bonds for the Authority with a face value of \$3,400,000 in December 2013. These bonds will be repaid over 16 years. The bond proceeds are also being used as the local match on federal and state grants for the “project” including the terminal, access roads, apron, and parking ramp.

## **ECONOMIC AND OTHER FACTORS**

When setting the 2013 budget, the Authority took many factors into consideration: the prolonged and severe economic recession and slow recovery still underway; the continuing financial and operational turmoil of the commercial aviation sector; the continuing vigilance of security requirements and its effects on commercial air travel and airport passenger handling; weather conditions which dictate utility costs and overtime for snow removal crews, energy, operating supplies, labor, and benefits price increases; and a general review of all rates and services so that revenue will keep pace with expenses. The Authority has taken steps to raise all rental and concession fees to competitive rates and carefully manages its costs for equipment, supplies, and services. The Authority actively seeks new lessees to occupy vacant space as well as economic development opportunities that are a good fit for the aviation sector. Examples of this are the Authority's development efforts and partnership with the Duluth Economic Development Authority to facilitate usage of the former Northwest Airlines Maintenance Facility by AAR. The Authority will continue to seek diversifying revenue sources in order to be less reliant on airline revenue sources.

## **FINANCIAL CONTACT**

This financial report is designed to provide our customers and creditors with a general overview of the Authority's finances and to demonstrate the Authority's accountability for the money it receives. If you have any questions about this report or need additional financial information, contact the Director of Finance, Duluth Airport Authority, 4701 Grinden Drive, Duluth, Minnesota 55811.

## **BASIC FINANCIAL STATEMENTS**

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**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

*EXHIBIT 1*

**COMPARATIVE STATEMENT OF NET POSITION  
DECEMBER 31, 2013 AND 2012**

	<b>2013</b>	<b>2012</b>
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 617,031	\$ 283,504
Accounts receivable	495,025	455,800
Grants receivable	19,807	48,081
Inventory	83,447	73,929
Prepaid items	193,183	41,971
Assets restricted for construction		
Cash and cash equivalents	6,631,795	4,731,598
Accounts receivable	84,605	80,963
Grants receivable	4,245,279	9,697,317
<b>Total current assets</b>	<b>\$ 12,370,172</b>	<b>\$ 15,413,163</b>
<b>Noncurrent assets</b>		
<b>Capital assets</b>		
Nondepreciable	\$ 6,473,465	\$ 53,414,081
Depreciable	172,878,264	125,383,569
Less: allowance for depreciation	(65,349,013)	(63,841,519)
<b>Net capital assets</b>	<b>\$ 114,002,716</b>	<b>\$ 114,956,131</b>
<b>Other assets</b>		
Airport planning costs - net of accumulated amortization of \$470,189 in 2013 and \$978,739 in 2012	\$ 1,279,881	\$ 661,716
Lease buyout costs - net of accumulated amortization of \$324,184 in 2013 and \$290,823 in 2012	203,197	236,558
<b>Total other assets</b>	<b>\$ 1,483,078</b>	<b>\$ 898,274</b>
<b>Total noncurrent assets</b>	<b>\$ 115,485,794</b>	<b>\$ 115,854,405</b>
<b>Total Assets</b>	<b>\$ 127,855,966</b>	<b>\$ 131,267,568</b>

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

**EXHIBIT 1  
(Continued)**

**COMPARATIVE STATEMENT OF NET POSITION  
DECEMBER 31, 2013 AND 2012**

	<b>2013</b>	<b>2012</b>
<b>Liabilities</b>		
<b>Current liabilities payable from unrestricted assets</b>		
Accounts payable	\$ 324,595	\$ 213,963
Due to the City of Duluth	3,500,000	4,000,000
Accrued salaries payable	69,905	60,367
Accrued vacation payable	82,583	84,002
Construction contracts payable	205,755	17,694
Unearned revenue	19,781	19,781
Revenue notes payable	47,612	43,662
Loans payable - City of Duluth	455,000	445,000
Loans payable	26,667	26,667
<b>Total current liabilities payable from unrestricted assets</b>	<b>\$ 4,731,898</b>	<b>\$ 4,911,136</b>
<b>Current liabilities payable from restricted assets</b>		
Construction contracts payable	515,895	5,931,937
<b>Total current liabilities</b>	<b>\$ 5,247,793</b>	<b>\$ 10,843,073</b>
<b>Noncurrent liabilities</b>		
Unearned revenue	\$ 295,498	\$ 316,431
Revenue notes payable	273,503	321,115
Loans payable - City of Duluth	9,715,000	6,770,000
Loans payable	162,222	188,889
Net other postemployment benefits liability	899,868	766,236
<b>Total noncurrent liabilities</b>	<b>\$ 11,346,091</b>	<b>\$ 8,362,671</b>
<b>Total Liabilities</b>	<b>\$ 16,593,884</b>	<b>\$ 19,205,744</b>
<b>Net Position</b>		
Net investment in capital assets	\$ 110,275,622	\$ 111,626,361
Unrestricted	986,460	435,463
<b>Total Net Position</b>	<b>\$ 111,262,082</b>	<b>\$ 112,061,824</b>

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

*EXHIBIT 2*

**COMPARATIVE STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION  
YEARS ENDED DECEMBER 31, 2013 AND 2012**

	2013	2012
<b>Operating Revenues</b>		
Charges for services	\$ 4,212,773	\$ 4,075,644
<b>Operating Expenses</b>		
Personal services	\$ 1,684,200	\$ 1,574,714
Supplies	60,588	68,523
Utilities	690,249	563,351
Other services and charges	1,573,825	1,085,461
Depreciation	8,044,434	5,486,475
Amortization	202,332	132,687
<b>Total Operating Expenses</b>	<b>\$ 12,255,628</b>	<b>\$ 8,911,211</b>
<b>Operating Income (Loss)</b>	<b>\$ (8,042,855)</b>	<b>\$ (4,835,567)</b>
<b>Nonoperating Revenues (Expenses)</b>		
Investment earnings	\$ 38,533	\$ 33,518
Passenger facility charge	620,914	625,680
Gain (loss) on disposal of capital assets	(3,000,917)	(1,104,442)
Net loan issuance expense	(63,544)	(87,480)
Interest expense	(279,012)	(388,859)
<b>Total Nonoperating Revenues (Expenses)</b>	<b>\$ (2,684,026)</b>	<b>\$ (921,583)</b>
<b>Net Income (Loss) Before Capital Contributions</b>	<b>\$ (10,726,881)</b>	<b>\$ (5,757,150)</b>
<b>Capital Contributions</b>		
Capital grants		
Federal	\$ 6,156,814	\$ 18,088,144
State	2,791,234	8,457,365
Contributed capital		
Contributed capital - Transportation Security Administration	275,491	2,138,540
Contributed capital - other	703,600	596,729
<b>Total Capital Contributions</b>	<b>\$ 9,927,139</b>	<b>\$ 29,280,778</b>
<b>Change in Net Position</b>	<b>\$ (799,742)</b>	<b>\$ 23,523,628</b>
<b>Net Position - January 1</b>	<b>112,061,824</b>	<b>88,538,196</b>
<b>Net Position - December 31</b>	<b>\$ 111,262,082</b>	<b>\$ 112,061,824</b>

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

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

*EXHIBIT 3*

**COMPARATIVE STATEMENT OF CASH FLOWS  
YEARS ENDED DECEMBER 31, 2013 AND 2012**

	<b>2013</b>	<b>2012</b>
<b>Cash Flows from Operating Activities</b>		
Cash received from customers	\$ 3,896,630	\$ 3,654,241
Cash paid to suppliers	(2,374,760)	(1,658,371)
Cash paid to employees	(1,542,449)	(1,470,403)
Other cash receipts	305,292	262,753
	<b>\$ 284,713</b>	<b>\$ 788,220</b>
<b>Net cash provided by (used in) operating activities</b>		
<b>Cash Flows from Noncapital Financing Activities</b>		
Principal paid on revenue note	\$ (43,662)	\$ (40,040)
Interest paid on revenue note	(31,338)	(34,960)
	<b>\$ (75,000)</b>	<b>\$ (75,000)</b>
<b>Net cash provided by (used in) noncapital financing activities</b>		
<b>Cash Flows from Capital and Related Financing Activities</b>		
Net cash withdrawals on line of credit	\$ (500,000)	\$ 3,375,000
Principal paid on loans	(471,666)	(461,667)
Loan proceeds	3,400,000	7,650,000
Loan issuance and interest costs	(311,218)	(441,379)
Capital grants - federal	9,331,319	14,315,990
Capital grants - state	4,460,902	6,596,125
Capital contributions - TSA	874,590	1,444,415
Passenger facility charge	617,272	616,143
Acquisition or construction of capital assets	(15,415,721)	(29,328,395)
	<b>\$ 1,985,478</b>	<b>\$ 3,766,232</b>
<b>Net cash provided by (used in) capital and related financing activities</b>		
<b>Cash Flows from Investing Activities</b>		
Interest on investments	\$ 38,533	\$ 33,518
	<b>\$ 38,533</b>	<b>\$ 33,518</b>
<b>Net Increase (Decrease) in Cash and Cash Equivalents</b>	<b>\$ 2,233,724</b>	<b>\$ 4,512,970</b>
<b>Cash and Cash Equivalents - January 1</b>	<b>5,015,102</b>	<b>502,132</b>
<b>Cash and Cash Equivalents - December 31</b>	<b>\$ 7,248,826</b>	<b>\$ 5,015,102</b>

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



**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

**EXHIBIT 3  
(Continued)**

**COMPARATIVE STATEMENT OF CASH FLOWS  
YEARS ENDED DECEMBER 31, 2013 AND 2012**

	2013	2012
<b>Reconciliation of Operating Income (Loss) to Net Cash Provided by (Used in) Operating Activities</b>		
<b>Operating income (loss)</b>	<b>\$ (8,042,855)</b>	<b>\$ (4,835,567)</b>
<b>Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities</b>		
Depreciation	8,044,434	5,486,475
Amortization	202,332	132,687
Changes in assets and liabilities		
(Increase) decrease in receivables	(10,951)	(158,650)
(Increase) decrease in inventories	(9,518)	24,980
(Increase) decrease in prepaid items	(151,212)	(1,878)
Increase (decrease) in payables	252,383	140,173
Increase (decrease) in unearned revenue	100	-
	<b>\$ 284,713</b>	<b>\$ 788,220</b>
<b>Net Cash Provided by (Used in) Operating Activities</b>		
<b>Noncash Investing, Capital, and Financing Activities</b>		
Capital assets acquired by construction		
Contracts payable	\$ -	\$ 3,412,406
Carrying value of capital assets disposed of	3,000,916	1,104,442

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**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

NOTES TO THE FINANCIAL STATEMENTS  
AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

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1. Summary of Significant Accounting Policies

The accounting policies of the Duluth Airport Authority conform with generally accepted accounting principles. During 2013, the Authority adopted new accounting guidance by implementing the provisions of Governmental Accounting Standards Board (GASB) Statement No. 65, *Items Previously Reported as Assets and Liabilities*, which represents a change in accounting principle. The more significant accounting policies established in GAAP and used by the Authority are discussed below.

A. Financial Reporting Entity

The Duluth Airport Authority was created by the Legislature of the State of Minnesota in 1969 to operate and maintain the aeronautic facilities and services in the City of Duluth. The Authority is a component unit of the City of Duluth according to criteria established by the GASB for determining the financial reporting entity. Specific criteria include: the management of the Authority is vested in seven Directors appointed by the Mayor of Duluth and approved by the City Council, and the City Council approves the budget of the Authority.

B. Basis of Presentation

The accounts of the Duluth Airport Authority are presented as an enterprise fund. Enterprise funds are used to account for operations financed and operated in a manner similar to private business enterprises--where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

Enterprise funds distinguish operating revenues from nonoperating items. Operating revenues generally result from providing and delivering services in connection with a principal ongoing activity. The principal operating revenues of the Authority are charges to customers for the use and lease of airport facilities. All revenues not meeting this definition are reported as nonoperating revenues.

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

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1. Summary of Significant Accounting Policies (Continued)

C. Basis of Accounting

The Authority uses the accrual basis of accounting. Revenues are recognized when they are earned, and expenses are recognized when they are incurred.

D. Budget

The Authority adopts an annual budget, which is approved by the Duluth City Council. The budget is prepared on the accrual basis of accounting.

E. Cash and Cash Equivalents

Cash and cash equivalents consist of cash and investments held by the Duluth City Treasurer. Investments are stated at fair value. For purposes of the statement of cash flows, all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased are considered to be cash equivalents.

F. Accounts Receivable

Amounts due from individuals and organizations are recorded as receivables at year-end. These include amounts owed pursuant to lease agreements.

G. Inventory

Inventories of materials and supplies are priced at the lower of cost or market on a first-in, first-out basis.

H. Restricted Assets

Monies restricted for the payment of construction contracts and passenger facility charge revenues are accounted for as restricted assets. 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.

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

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1. Summary of Significant Accounting Policies (Continued)

I. Capital Assets

Purchased or constructed capital assets are stated at cost. Donated capital assets are stated at their estimated fair value at the time of the donation. The Authority's policy is to capitalize assets with a useful life of one year or more and a minimum cost of \$5,000.

J. Depreciation

Depreciation of capital assets is determined using the straight-line method. The estimated useful lives of the assets are:

<u>Classification</u>	<u>Years</u>
Runways	15
Buildings	30
Equipment	5 to 10

K. Other Assets

Airport planning costs and lease buyout costs are being amortized by the straight-line method over 10 to 20 years.

L. Unearned Revenue

Amounts received as advance payments for construction, rentals, and commissions are reported as unearned revenue until they are earned.

M. Passenger Facility Charges

The Duluth Airport Authority has been authorized by the Federal Aviation Administration to collect passenger facility charges to finance capital improvements at Duluth International Airport and Duluth Sky Harbor Airport.

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

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1. Summary of Significant Accounting Policies (Continued)

N. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles 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. Deposits and Investments

The Authority and the City Council of Duluth are authorized by Minn. Stat. §§ 118A.02 and 118A.04 to designate a depository of public funds and to invest in certificates of deposit. 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 and 118A.05.

Additional disclosures, as required by GASB Statement No. 3, *Deposits with Financial Institutions, Investments (Including Repurchase Agreements), and Reverse Repurchase Agreements*, and GASB Statement No. 40, *Deposit and Investment Risk Disclosures*, are disclosed on an entity-wide basis in the City of Duluth's Comprehensive Annual Financial Report. The Duluth Airport Authority is a component unit of the City of Duluth.

The following is a summary of the Authority's cash:

	December 31	
	2013	2012
City's pooled cash and investments	\$ 7,245,346	\$ 4,374,145
Authority's checking accounts	3,361	640,838
Petty cash funds	119	119
Total	\$ 7,248,826	\$ 5,015,102

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

2. Detailed Notes

A. Deposits and Investments (Continued)

Detail as shown on Comparative Balance Sheet

Current assets

Cash and cash equivalents	\$ 617,031	\$ 283,504
Assets restricted for construction		
Cash and cash equivalents	6,631,795	4,731,598
Total Cash and Cash Equivalents	\$ 7,248,826	\$ 5,015,102

B. Capital Assets

A summary of changes in capital assets at December 31, 2013 and 2012, follows:

	Balance January 1, 2013	Increase	Decrease	Transfers/ Reclassifications	Balance December 31, 2013
Capital assets not depreciated					
Land	\$ 3,361,434	\$ -	\$ -	\$ -	\$ 3,361,434
Construction in progress	50,052,647	10,164,892	6,000	(57,099,508)	3,112,031
Total capital assets not depreciated	\$ 53,414,081	\$ 10,164,892	\$ 6,000	\$ (57,099,508)	\$ 6,473,465
Capital assets depreciated					
Buildings	\$ 35,113,702	\$ 720,180	\$ 8,591,214	\$ 47,597,219	\$ 74,839,887
Runways	80,172,803	-	1,590	2,001,272	82,172,485
Equipment	10,097,064	-	945,052	6,713,880	15,865,892
Total capital assets depreciated	\$ 125,383,569	\$ 720,180	\$ 9,537,856	\$ 56,312,371	\$ 172,878,264
Less: accumulated depreciation for					
Buildings	\$ 11,852,490	\$ 2,452,150	\$ 5,638,383	\$ -	\$ 8,666,257
Runways	46,563,455	3,968,895	1,590	-	50,530,760
Equipment	5,425,574	1,623,389	896,967	-	6,151,996
Total accumulated depreciation	\$ 63,841,519	\$ 8,044,434	\$ 6,536,940	\$ -	\$ 65,349,013
Total capital assets depreciated, net	\$ 61,542,050	\$ (7,324,254)	\$ 3,000,916	\$ 56,312,371	\$ 107,529,251
Capital Assets, Net	\$ 114,956,131	\$ 2,840,638	\$ 3,006,916	\$ (787,137)	\$ 114,002,716

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

2. Detailed Notes

B. Capital Assets (Continued)

	Balance January 1, 2012	Increase	Decrease	Transfers/ Reclassifications	Balance December 31, 2012
Capital assets not depreciated					
Land	\$ 3,361,434	\$ -	\$ -	\$ -	\$ 3,361,434
Construction in progress	17,416,275	32,753,520	-	(117,148)	50,052,647
Total capital assets not depreciated	<u>\$ 20,777,709</u>	<u>\$ 32,753,520</u>	<u>\$ -</u>	<u>\$ (117,148)</u>	<u>\$ 53,414,081</u>
Capital assets depreciated					
Buildings	\$ 37,506,371	\$ 601,897	\$ 2,995,104	\$ 538	\$ 35,113,702
Runways	80,172,803	-	-	-	80,172,803
Equipment	10,004,994	-	-	92,070	10,097,064
Total capital assets depreciated	<u>\$ 127,684,168</u>	<u>\$ 601,897</u>	<u>\$ 2,995,104</u>	<u>\$ 92,608</u>	<u>\$ 125,383,569</u>
Less: accumulated depreciation for					
Buildings	\$ 12,714,212	\$ 1,028,940	\$ 1,890,662	\$ -	\$ 11,852,490
Runways	42,639,821	3,923,634	-	-	46,563,455
Equipment	4,891,673	533,901	-	-	5,425,574
Total accumulated depreciation	<u>\$ 60,245,706</u>	<u>\$ 5,486,475</u>	<u>\$ 1,890,662</u>	<u>\$ -</u>	<u>\$ 63,841,519</u>
Total capital assets depreciated, net	<u>\$ 67,438,462</u>	<u>\$ (4,884,578)</u>	<u>\$ 1,104,442</u>	<u>\$ 92,608</u>	<u>\$ 61,542,050</u>
Capital Assets, Net	<u>\$ 88,216,171</u>	<u>\$ 27,868,942</u>	<u>\$ 1,104,442</u>	<u>\$ (24,540)</u>	<u>\$ 114,956,131</u>

Transfers and reclassifications for 2013 and 2012 do not net out to zero because there was construction in progress transferred to "Other Assets - Airport Planning Costs" which is not included on this summary (\$787,137 in 2013 and \$24,540 in 2012).



**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

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2. Detailed Notes

B. Capital Assets (Continued)

As of December 31, 2013, the Authority had the following commitments with respect to unfinished construction projects:

<u>Projects</u>	<u>Remaining Construction Commitment</u>
AIP 53	\$ 198,582
AIP 54	458,113
Parking Ramp	<u>8,468,985</u>
Total	<u>\$ 9,125,680</u>

As of December 31, 2012, the Authority had the following commitments with respect to unfinished construction projects:

<u>Projects</u>	<u>Remaining Construction Commitment</u>
AIP 48	\$ 805,017
AIP 49	247,981
AIP 51	368,572
AIP 52	519,228
AIP 53	<u>8,431,844</u>
Total	<u>\$ 10,372,642</u>

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

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2. Detailed Notes (Continued)

C. Vacation and Sick Leave

Full-time employees are granted from 12 to 28 days of vacation time per year depending on their years of service. Maximum amounts of vacation time that can be accumulated range from 18 to 42 days. Unpaid vacation time earned at year-end is recognized as a liability in the financial statements. Sick leave is accrued by employees at the rate of 4 hours per pay period and may be accumulated to a maximum of 120 days, 60 days, or 30 days, depending on the employee's start date. Sick leave is recorded as an expense when paid. Employees are not compensated for unused sick leave. Any liability for earned, unused sick leave is not recognized in the financial statements.

D. Leases

The Authority leases space and other facilities under various rates and terms. All such leases are considered to be operating leases.

Minimum future rents receivable on noncancelable leases are:

2014	\$ 129,133
2015	130,848
2016	132,308
2017	132,308
2018	131,308
After 2018	<u>1,345,013</u>
Total	<u>\$ 2,000,918</u>

Contingent rental income from operating leases for 2013 and 2012 was \$253,686 and \$272,235 respectively.

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

2. Detailed Notes (Continued)

E. Budgets

The Duluth Airport Authority adopts a budget to be approved by the Duluth City Council. A summary of the operating budget for the fiscal years ended December 31, 2013 and 2012, is:

	2013		Variance Favorable (Unfavorable)
	Budget	Actual	
Operating Revenues			
Charges for services	\$ 3,985,400	\$ 4,212,773	\$ 227,373
Operating Expenses			
Personal services	\$ 1,660,328	\$ 1,684,200	\$ (23,872)
Supplies	300,000	60,588	239,412
Utilities	500,000	690,249	(190,249)
Other services and charges	1,136,900	1,573,825	(436,925)
Depreciation	5,595,951	8,044,434	(2,448,483)
Amortization	133,233	202,332	(69,099)
Total Operating Expenses	\$ 9,326,412	\$ 12,255,628	\$ (2,929,216)
Net Operating Income (Loss)	\$ (5,341,012)	\$ (8,042,855)	\$ (2,701,843)
Nonoperating Revenues (Expenses)			
Investment earnings	\$ 15,000	\$ 38,533	\$ 23,533
Passenger facility charge	600,000	620,914	20,914
Gain (loss) on disposal of capital assets	-	(3,000,917)	(3,000,917)
Net loan issuance expense	-	(63,544)	(63,544)
Interest expense	(734,000)	(279,012)	454,988
Total Nonoperating Revenues (Expenses)	\$ (119,000)	\$ (2,684,026)	\$ (2,565,026)
Net Income (Loss) Before Capital Contributions	\$ (5,460,012)	\$ (10,726,881)	\$ (5,266,869)
Capital Contributions			
Capital grants - federal	\$ 3,084,600	\$ 6,156,814	\$ 3,072,214
Capital grants - state	43,400	2,791,234	2,747,834
Contributed capital - TSA	-	275,491	275,491
Contributed capital - Federal Prison Bureau	-	703,600	703,600
Total Capital Contributions	\$ 3,128,000	\$ 9,927,139	\$ 6,799,139
Change in Net Position	\$ (2,332,012)	\$ (799,742)	\$ 1,532,270

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

2. Detailed Notes

E. Budgets (Continued)

	2012		Variance Favorable (Unfavorable)
	Budget	Actual	
Operating Revenues			
Charges for services	\$ 3,759,000	\$ 4,075,644	\$ 316,644
Operating Expenses			
Personal services	\$ 1,568,000	\$ 1,574,714	\$ (6,714)
Supplies	225,000	68,523	156,477
Utilities	565,000	563,351	1,649
Other services and charges	1,073,900	1,085,461	(11,561)
Depreciation	5,122,000	5,486,475	(364,475)
Amortization	104,800	132,687	(27,887)
Total Operating Expenses	\$ 8,658,700	\$ 8,911,211	\$ (252,511)
Net Operating Income (Loss)	\$ (4,899,700)	\$ (4,835,567)	\$ 64,133
Nonoperating Revenues (Expenses)			
Investment earnings	\$ 10,000	\$ 33,518	\$ 23,518
Passenger facility charge	600,000	625,680	25,680
Gain (loss) on disposal of capital assets	-	(1,104,442)	(1,104,442)
Net loan issuance expense	-	(87,480)	(87,480)
Interest expense	(49,394)	(388,859)	(339,465)
Total Nonoperating Revenues (Expenses)	\$ 560,606	\$ (921,583)	\$ (1,482,189)
Net Income (Loss) Before Capital Contributions	\$ (4,339,094)	\$ (5,757,150)	\$ (1,418,056)
Capital Contributions			
Capital grants - federal	\$ 16,783,500	\$ 18,088,144	\$ 1,304,644
Capital grants - state	7,323,300	8,457,365	1,134,065
Contributed capital - TSA	1,797,200	2,138,540	341,340
Contributed capital - Federal Prison Bureau	-	596,729	596,729
Total Capital Contributions	\$ 25,904,000	\$ 29,280,778	\$ 3,376,778
Change in Net Position	\$ 21,564,906	\$ 23,523,628	\$ 1,958,722

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

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2. Detailed Notes (Continued)

F. Long-Term Debt

On November 1, 2005, the Authority issued an Airport Facility Revenue Note, Series 2005A, to finance the lease buyout of the Authority's Fixed Base Operator. The principal of the note is \$497,379, payable in semi-annual payments on June 1 and December 1 each year, commencing June 1, 2007, until final maturity on June 1, 2019, with an annual interest rate of 8.85 percent.

The City of Duluth obtained a loan from the Minnesota Investment Fund (MIF). Proceeds from the loan have been used to remedy soil conditions on Duluth Airport Authority property. The Duluth Airport Authority has agreed to make payments when due on the loan in the total amount of \$400,000. Payments are due in 180 monthly installments of \$2,222 from February 2006 to January 2021. There is no interest charged on this loan.

In May 2012, the City of Duluth issued General Obligation Airport Improvement Bonds, Series 2012B, on behalf of the Duluth Airport Authority. The bonds have a face value of \$7,650,000 and will be repaid over a period of 15 years. Proceeds of the bonds will be used to provide the local match of federal and state grants in relation to a new terminal facility and for funding involved with a new parking ramp, access road, and aprons. The Duluth Airport Authority entered into a loan agreement with the City of Duluth and makes loan payments to the City in sufficient amounts for the City to make the required payments on the bonds.

In December 2013, the City of Duluth issued General Obligation Airport Improvement Bonds, Series 2013B, on behalf of the Duluth Airport Authority. The bonds have a face value of \$3,400,000 and will be repaid over a period of 16 years. Proceeds of the bonds will be used to provide funding in completion of the parking ramp facilities. The Duluth Airport Authority entered into a loan agreement with the City of Duluth and makes loan payments to the City in sufficient amounts for the City to make the required payments on the bonds.

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

2. Detailed Notes

F. Long-Term Debt (Continued)

The annual requirements to service the debt follow:

Year Ended December 31	Revenue Note		MIF Loan
	Principal	Interest	Principal
2014	\$ 47,612	\$ 27,338	\$ 26,667
2015	51,919	23,081	26,667
2016	56,615	18,385	26,667
2017	61,737	13,263	26,667
2018	67,321	7,679	26,667
2019 to 2026	35,911	1,589	55,554
Total	\$ 321,115	\$ 91,335	\$ 188,889

Year Ended December 31	City of Duluth Loan 2012B		City of Duluth Loan 2013B	
	Principal	Interest	Principal	Interest
2014	\$ 455,000	\$ 169,381	\$ -	\$ 115,718
2015	465,000	160,281	220,000	118,981
2016	470,000	150,981	225,000	115,571
2017	485,000	141,581	225,000	111,071
2018	490,000	131,881	230,000	105,446
2019 to 2026	4,405,000	601,489	2,500,000	543,400
Total	\$ 6,770,000	\$ 1,355,594	\$ 3,400,000	\$ 1,110,187

A summary of the changes in the long-term debt follows:

	2013	2012
Balance - January 1	\$ 7,795,333	\$ 647,039
Additions	3,400,000	7,650,000
Payments	(515,329)	(501,706)
Balance - December 31	\$ 10,680,004	\$ 7,795,333
Due Within One Year	\$ 529,279	\$ 515,329

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

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2. Detailed Notes (Continued)

G. Line of Credit

The City of Duluth has extended the Duluth Airport Authority a line of credit of up to \$4,000,000 to assist in the management of cash flows in connection with the Authority's new airport terminal construction project. Interest at a rate of 2.5 percent is charged on drawn funds.

At December 31, 2012, there was \$4,000,000 outstanding. During 2013, draws on the line of credit were taken by the Authority totaling \$3,985,000, and repayments of \$4,485,000 were made on the draws. The remaining balance outstanding of \$3,500,000 is reported as Due to the City of Duluth on the Comparative Statement of Net Position at December 31, 2013.

3. Risk Management

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; employee health and dental; and natural disasters. The Authority participates in the City of Duluth Joint Powers Enterprise Trust to provide its employees health and dental benefits. The Authority purchases commercial insurance for all other risks of loss. 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.

Employee health and dental benefits are provided through the City of Duluth Joint Powers Enterprise Trust at premium rates established by the Trust for all plan participants.

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

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4. Major Customers

Major customers of services provided by the Duluth Airport Authority in 2013 were:

	<u>Operating Revenues</u>	<u>Percentage of Total Operating Revenues</u>
DELTA Airlines	<u>\$ 471,834</u>	11.2%

Major customers of services provided by the Duluth Airport Authority in 2012 were:

	<u>Operating Revenues</u>	<u>Percentage of Total Operating Revenues</u>
DELTA Airlines	<u>\$ 434,606</u>	10.7%

5. Pension Plans

A. Defined Benefit Plans

Plan Description

All full-time and certain part-time employees of the Duluth Airport Authority are covered by defined benefit 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 and benefits vest after three years of credited service (five years for those first eligible for membership after June 30, 2010). No Authority members belong to the Basic Plan.



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5. Pension Plans

A. Defined Benefit Plans

Plan Description (Continued)

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. Defined retirement benefits are based on a member's highest average salary for any five successive years of allowable service, age, and years of credit at termination of service.

Two methods are used to compute benefits for Coordinated 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 is 1.2 percent of average salary for each of the first ten years of service and 1.7 percent for each successive year. Using Method 2, the annuity accrual rate is 1.7 percent for Coordinated Plan members for each year of service.

For General Employees Retirement Fund members hired prior to July 1, 1989, 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 or 66 (depending on date hired) for General Employees Retirement Fund members. A reduced retirement annuity is also available to eligible members seeking early retirement.

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

PERA issues a publicly available financial report that includes financial statements and required supplementary information for the General Employees Retirement Fund. That report may be obtained on the internet at [www.mnpera.org](http://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.

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

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5. Pension Plans (Continued)

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 Duluth Airport Authority makes annual contributions to the pension plans equal to the amount required by state statutes. General Employees Retirement Fund Coordinated Plan members are required to contribute 6.25 percent of their annual covered salary.

The Duluth Airport Authority is required to contribute the following percentages of annual covered payroll in 2013:

General Employees Retirement Fund Coordinated Plan members	7.25%
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The Authority's contributions for the years ending December 31, 2013, 2012, and 2011, for the General Employees Retirement Fund were:

<u>2013</u>	<u>2012</u>	<u>2011</u>
\$ 76,081	\$ 71,779	\$ 73,362

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

6. Other Postemployment Benefits (OPEB)

A. Plan Description and Funding Policy

The Authority provides postemployment health care benefits and term life insurance coverage in accordance with union contract or Authority policy. Union contract postemployment benefits extend to Authority employees retiring on or after January 1, 1983, who receive retirement benefits from the PERA. In addition, the Authority has extended the same postemployment benefits to Authority employees retired prior to January 1, 1983. Fourteen retirees meet these eligibility requirements.

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

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6. Other Postemployment Benefits (OPEB) (Continued)

B. Annual OPEB Cost and Net OPEB Obligation

The Authority participates in the City of Duluth Joint Powers Enterprise Trust and pays the required premiums to provide health care benefits and term life insurance for eligible retirees and claimed dependents. Health care premiums are paid by the Authority to the same extent as active employees for the life of the retiree or the surviving spouse. Life insurance premiums are also paid by the Authority for the life of the retiree. Premiums paid for eligible retirees and claimed dependents for health care insurance in 2013 totaled \$64,181. In 2012, the amount paid was \$97,544.

The Authority's annual OPEB cost is calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial accrued liabilities (or funding excess) over a period not to exceed 30 years. The following table shows the components of the Authority's annual OPEB cost for 2013, the amount actually contributed to the plan, and changes in the Authority's net OPEB obligation:

ARC	\$	208,028
Interest on net OPEB obligation		43,676
Adjustment to ARC		(53,891)
		(53,891)
Annual OPEB cost	\$	197,813
Contributions during the year		(64,181)
		(64,181)
Increase in net OPEB obligation	\$	133,632
Net OPEB - Beginning of Year		766,236
		766,236
Net OPEB - End of Year	\$	899,868

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

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6. Other Postemployment Benefits (OPEB)

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

The Authority's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for 2012 and 2013 were as follows:

	Fiscal Year Ended December 31	
	2012	2013
Percentage of Annual OPEB Cost Contributed	49.11%	32.45%
Annual OPEB cost	\$ 198,641	\$ 197,813
Employer contributions	<u>97,544</u>	<u>64,181</u>
Net Increase in Net OPEB Obligation	<u>\$ 101,097</u>	<u>\$ 133,632</u>

C. Funded Status and Funding Progress

The actuarial accrued liability for benefits at January 1, 2013, as of the most recent actuarial valuation date, is \$1,891,190. The Authority currently has no assets that have been irrevocably deposited in a trust for future health benefits; thus, the entire amount is unfunded. The covered payroll (annual payroll of active employees covered by the plan) is \$1,010,000. The ratio of the unfunded actuarially accrued liabilities to covered payroll is 187.25 percent.

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

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

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6. Other Postemployment Benefits (OPEB) (Continued)

D. Actuarial Methods and Assumptions

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

In the January 1, 2013, actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions included a 5.7 percent discount rate, which is based on the estimated long-term investment yield on the general assets of the Authority. The annual health care cost trend rate is 10.0 percent initially, reduced incrementally to an ultimate rate of 5.0 percent after 10 years. The unfunded actuarial accrued liability is being amortized as a level dollar amount over 30 years.

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**REQUIRED SUPPLEMENTARY INFORMATION**

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**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

**EXHIBIT A-1**

**SCHEDULE OF FUNDING PROGRESS - OTHER POSTEMPLOYMENT BENEFITS  
DECEMBER 31, 2013**

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded Actuarial Accrued Liability (UAAL) (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b - a)/c)
January 1, 2013	\$ -	\$ 1,891,190	\$ 1,891,190	0.00%	\$ 1,010,000	187.25%
June 1, 2011	-	1,911,042	1,911,042	0.00	858,000	222.73
June 1, 2009	-	2,085,377	2,085,377	0.00	1,073,859	194.19

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**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

**NOTES TO THE SCHEDULE OF FUNDING  
PROGRESS - OTHER POSTEMPLOYMENT BENEFITS  
DECEMBER 31, 2013**

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The Duluth Airport Authority implemented Governmental Accounting Standards Board Statement 45 for the fiscal year ended December 31, 2007.

Actuarial valuations were performed in 2007, 2009, 2011, and 2013. No valuations were performed in 2008, 2010, or 2012; therefore, funding progress information for 2008, 2010, and 2012 are not included on this schedule. Standards require reporting the three most recent actuarial valuations.

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

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**SUPPLEMENTARY INFORMATION**

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**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

*EXHIBIT B-1*

**COMPARATIVE STATEMENT OF OPERATING REVENUES  
YEARS ENDED DECEMBER 31, 2013 AND 2012**

	2013	2012
<b>Operating Revenues</b>		
<b>Charges for services</b>		
<b>Tower building</b>		
Space rental and services	\$ 209,316	\$ 201,389
<b>Terminal building</b>		
Loading bridges rent	\$ -	\$ 50,866
Space rental	675,957	396,316
Utility sales	10,487	42,175
Car rental commissions	458,385	450,959
Other commissions	5,097	6,079
Percentage of lessees' sales	778	7,093
Other income	281,903	311,056
<b>Total terminal building</b>	\$ 1,432,607	\$ 1,264,544
<b>Parking lot</b>		
Parking lot commissions	\$ 896,907	\$ 845,878
<b>Land, field, and runways</b>		
Transportation Security Administration charges	\$ 103,778	\$ 90,077
State aid for maintenance and operation	168,569	168,569
Rental income	314,957	339,315
Customer facility charge	250,264	250,288
Fuel flowage fees	106,050	109,656
Landing fees	255,870	271,597
Percentage of lessees' sales	61,451	124,294
Utility sales	11,883	13,986
<b>Total land, field, and runways</b>	\$ 1,272,822	\$ 1,367,782
<b>Hangar</b>		
Space rental	\$ 208,694	\$ 214,481
Utility sales	48,409	24,122
<b>Total hangar</b>	\$ 257,103	\$ 238,603
<b>Sky Harbor</b>		
State aid for maintenance and operation	\$ 20,285	\$ 20,285
Rental income	34,228	29,120
Fuel sales	79,634	102,452
Percentage of lessees' sales	3,110	920
Other income	6,761	4,671
<b>Total Sky Harbor</b>	\$ 144,018	\$ 157,448
<b>Total Operating Revenues</b>	\$ 4,212,773	\$ 4,075,644

**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

*EXHIBIT C-1*

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED DECEMBER 31, 2013**

<b>Federal Grantor Pass-Through Agency Grant Program Title</b>	<b>Federal CFDA Number</b>	<b>Pass-Through Grant Number</b>	<b>Expenditures</b>
<b>Federal Aviation Administration</b>			
Passed Through Minnesota Department of Transportation - Aeronautics			
Airport Improvement Program	20.106	Various	<b><u>\$ 6,156,814</u></b>



**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED DECEMBER 31, 2013**

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1. Reporting Entity

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

2. Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of the Duluth Airport Authority under programs of the federal government for the year ended December 31, 2013. 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 Duluth Airport Authority, it is not intended to and does not present the financial position, changes in net position, or cash flows of the Duluth Airport Authority.

3. Summary of Significant Accounting Policies

Expenditures reported on the schedule are reported on the 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 entity identifying numbers are presented where available.

4. Subrecipients

Of the expenditures presented in the schedule, the Duluth Airport Authority did not provide federal awards to any subrecipients.

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**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

*EXHIBIT C-2*

**SCHEDULE OF PASSENGER FACILITY CHARGES COLLECTED AND EXPENDED  
FOR THE YEAR AND EACH QUARTER WITHIN THE YEAR ENDED DECEMBER 31, 2013**

	<u>Seventh Application*</u>	<u>Eighth Application**</u>	<u>Ninth Application**</u>	<u>Tenth Application**</u>	<u>Eleventh Application**</u>
Passenger Facility Charge Collections***					
Prior to January 1, 2013	\$ 2,446,424	\$ 514,305	\$ 201,822	\$ 1,288,058	\$ -
Collections in 2013					
First quarter	\$ -	\$ -	\$ -	\$ 148,475	\$ -
Second quarter	-	-	-	35,587	119,747
Third quarter	-	-	-	164,819	-
Fourth quarter	-	-	-	148,644	-
<b>Total collections in 2013</b>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 497,525</u>	<u>\$ 119,747</u>
<b>Total Collected Through December 31, 2013</b>	<b>\$ 2,446,424</b>	<b>\$ 514,305</b>	<b>\$ 201,822</b>	<b>\$ 1,785,583</b>	<b>\$ 119,747</b>
<b>Approved expenses through December 31, 2013</b>	<u>(2,113,428)</u>	<u>(514,305)</u>	<u>(201,822)</u>	<u>(1,506,509)</u>	<u>(702,584)</u>
<b>Unexpended Balance - December 31, 2013</b>	<u><u>\$ 332,996</u></u>	<u><u>\$ -</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 279,074</u></u>	<u><u>\$ (582,837)</u></u>

\*Federal Aviation Administration Record of Decision passenger facility charge effective date for Application Seven is April 1, 2005.

\*\*Federal Aviation Administration's Acknowledgment of Intent of passenger facility charge effective date for Application Eight is September 30, 2008; Application Nine is October 1, 2010; Application Ten is January 20, 2011; and Application Eleven is January 16, 2013.

\*\*\*Cash basis of accounting - reported when received rather than when earned in accordance with passenger facility charge reporting guidelines.

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**DULUTH AIRPORT AUTHORITY  
DULUTH, MINNESOTA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED DECEMBER 31, 2013**

**I. SUMMARY OF AUDITOR'S RESULTS**

**Financial Statements**

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

Internal control over financial reporting:

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

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

**Federal Awards**

Internal control over major programs:

- Material weaknesses identified? **No**
- 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? **No**

The major program is:

Airport Improvement Program

CFDA #20.106

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

Duluth Airport Authority qualified as a low-risk auditee? **Yes**

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

### INTERNAL CONTROL

#### PREVIOUSLY REPORTED ITEM NOT RESOLVED

Finding 2006-001

#### 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:** 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.

**Context:** This is not unusual in operations the size of the Duluth Airport Authority; however, the Authority's 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 employees in the normal course of performing their assigned functions.

**Cause:** The size of the Duluth Airport Authority and its staffing limits the internal control that management can design and implement into the organization.

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

#### Client's Response:

*We are aware of the limited number of personnel. The Authority management has implemented oversight procedures and will continue to monitor the staff to help assure controls and procedures are being followed.*



**III. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARD PROGRAMS**

None.

**IV. FINDINGS - PASSENGER FACILITY CHARGE (PFC) REGULATIONS**

None.

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REBECCA OTTO  
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

Mayor and City Council  
City of Duluth

Board of Directors  
Duluth Airport 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 Duluth Airport Authority, a component unit of the City of Duluth, as of and for the year ended December 31, 2013, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated June 6, 2014.

### **Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Duluth Airport Authority's internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion 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.

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. 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 the attention of those charged with governance.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section 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 or significant deficiencies may exist that were not identified. Given these limitations, during our audit, we did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify a deficiency in internal control over financial reporting, described in the accompanying Schedule of Findings and Questioned Costs as item 2006-001, that we consider to be a significant deficiency.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Duluth Airport 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**

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 in connection with the audit of the Authority's financial statements: 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 Duluth Airport 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.

## **Duluth Airport Authority's Response to Findings**

The Duluth Airport Authority's response to the internal control finding identified in our audit has been included in the Schedule of Findings and Questioned Costs. The Authority's response was not subject to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

### **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

June 6, 2014

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REBECCA OTTO  
STATE AUDITOR

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### **REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM AND FOR THE PASSENGER FACILITY CHARGE PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE**

#### Independent Auditor's Report

Mayor and City Council  
City of Duluth

Board of Directors  
Duluth Airport Authority

#### **Report on Compliance for Each Major Federal Program and for the Passenger Facility Charge Program**

We have audited the compliance of the Duluth Airport Authority, a component unit of the City of Duluth, 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, 2013. The Duluth Airport Authority's major federal program is identified in the Summary of Auditor's Results section of the accompanying Schedule of Findings and Questioned Costs.

We have also audited the Duluth Airport Authority's compliance with requirements applicable to its passenger facility charge (PFC) funds collected and expended for the year ended December 31, 2013.

#### ***Management's Responsibility***

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

#### ***Auditor's Responsibility***

Our responsibility is to express an opinion on compliance for the Duluth Airport Authority's major federal program and PFC 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; OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*; and the *Passenger Facility Charge Audit Guide for Public Agencies*, issued by the Federal Aviation Administration. 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 or PFC program occurred. An audit includes examining, on a test basis, evidence about the Duluth Airport 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 its major federal program and its PFC program. However, our audit does not provide a legal determination of the Authority's compliance with those requirements.

#### ***Opinion on Each Major Federal Program and the Passenger Facility Charge Program***

In our opinion, the Duluth Airport 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 or its PFC program for the year ended December 31, 2013.

#### **Report on Internal Control Over Compliance**

Management of the Duluth Airport 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 its major federal program or on its PFC 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 the PFC program and to test and report on internal control over compliance in accordance with OMB Circular A-133, and the *Passenger Facility Charge Audit Guide for Public Agencies*, 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.

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 or the PFC program will not be prevented, or detected and corrected, on a timely basis. A significant deficiency in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program or the PFC program that is less severe than a material weakness in internal control over compliance, yet important enough to merit the attention of those charged with governance.



Our consideration of the internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

### **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 and Passenger Facility Charge requirements. Accordingly, this report is not suitable for any other purpose.

*/s/Rebecca Otto*

*/s/Greg Hierlinger*

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