

# STATE OF MINNESOTA

## Office of the State Auditor



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

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**KNIFE RIVER-LARSMONT SANITARY DISTRICT**  
**KNIFE RIVER, MINNESOTA**

FOR THE YEAR ENDED DECEMBER 31, 2006

## **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.

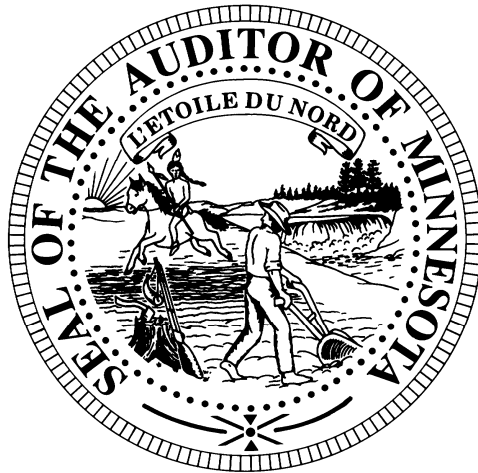
The State Auditor serves on the State Executive Council, State Board of Investment, Land Exchange Board, Public Employees Retirement Association Board, Minnesota Housing Finance Agency, and the Rural Finance Authority Board.

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**KNIFE RIVER-LARSMONT SANITARY DISTRICT  
KNIFE RIVER, MINNESOTA**

**For the Year Ended December 31, 2006**



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

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**KNIFE RIVER-LARSMONT SANITARY DISTRICT  
KNIFE RIVER, MINNESOTA**

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**KNIFE RIVER-LARSMONT SANITARY DISTRICT  
KNIFE RIVER, MINNESOTA**

ORGANIZATION  
DECEMBER 31, 2006

<u>Board of Managers</u>	<u>Term Ending</u>
Robert Mitchell, Chair	January 1, 2009
Mike Ojard, Vice Chair	January 1, 2007
Robert Entzion, Treasurer	January 1, 2009
Randy Ellestad, Member	January 1, 2009
Tom Bothwell, Member	January 1, 2008

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REBECCA OTTO  
STATE AUDITOR

# STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

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## INDEPENDENT AUDITOR'S REPORT

Board of Managers  
Knife River-Larsmont Sanitary District

We have audited the accompanying basic financial statements of the Knife River-Larsmont Sanitary District as of and for the year ended December 31, 2006, as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion 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 basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of the Knife River-Larsmont Sanitary District as of and for the year ended December 31, 2006, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Knife River-Larsmont Sanitary District has not presented a Management's Discussion and Analysis that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be part of, the basic financial statements.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 10, 2008, on our consideration of the Knife River-Larsmont Sanitary District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

*/s/Rebecca Otto*

REBECCA OTTO  
STATE AUDITOR

March 10, 2008

*/s/Greg Hierlinger*

GREG HIERLINGER, CPA  
DEPUTY STATE AUDITOR

## **BASIC FINANCIAL STATEMENTS**

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**KNIFE RIVER-LARSMONT SANITARY DISTRICT  
KNIFE RIVER, MINNESOTA**

**EXHIBIT A**

**STATEMENT OF NET ASSETS  
DECEMBER 31, 2006**

**Assets**

**Current assets**

Cash	\$ 192,203
Petty cash	50
Taxes receivable	2,597
Accounts receivable	46,510
Inventories	8,815
	<hr/>

**Total current assets** **\$ 250,175**

**Capital assets**

Depreciable, net of accumulated depreciation	3,199,583
	<hr/>

**Total Assets** **\$ 3,449,758**

**Liabilities**

**Current liabilities**

Accounts payable	\$ 25,567
Due to other governments	24,726
Deferred revenue	658
Public Facilities Authority (PFA) loans payable	41,000
	<hr/>

**Total current liabilities** **\$ 91,951**

**Noncurrent liabilities**

PFA loans payable	835,212
	<hr/>

**Total Liabilities** **\$ 927,163**

**Net Assets**

Invested in capital assets, net of related debt	\$ 2,323,371
Unrestricted	199,224
	<hr/>

**Total Net Assets** **\$ 2,522,595**

**KNIFE RIVER-LARSMONT SANITARY DISTRICT  
KNIFE RIVER, MINNESOTA**

**EXHIBIT B**

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS  
FOR THE YEAR ENDED DECEMBER 31, 2006**

<b>Operating Revenues</b>	
Charges for services	\$ 102,174
Licenses and permits	13,120
Miscellaneous	482
	<hr/>
<b>Total Operating Revenues</b>	<b>\$ 115,776</b>
<b>Operating Expenses</b>	
Contracted services	\$ 54,153
Professional services	32,234
Repair and maintenance	23,261
Supplies	980
Utilities	9,638
Other services and charges	24,136
Depreciation	118,916
Interest expense	5,734
	<hr/>
<b>Total Operating Expenses</b>	<b>\$ 269,052</b>
<b>Operating Income (Loss)</b>	<b>\$ (153,276)</b>
<b>Nonoperating Revenues (Expenses)</b>	
Property taxes and aids	\$ 59,631
Interest income	1,272
	<hr/>
<b>Total Nonoperating Revenues (Expenses)</b>	<b>\$ 60,903</b>
<b>Capital contributions</b>	
Corp of Engineers Section 569 grant	\$ 189,579
	<hr/>
<b>Change in Net Assets</b>	<b>\$ 97,206</b>
<b>Net Assets - January 1, 2006</b>	<b>2,425,389</b>
	<hr/>
<b>Net Assets - December 31, 2006</b>	<b>\$ 2,522,595</b>
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**KNIFE RIVER-LARSMONT SANITARY DISTRICT  
KNIFE RIVER, MINNESOTA**

**EXHIBIT C**

**STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED DECEMBER 31, 2006**

<b>Cash Flows from Operating Activities</b>	
Cash received from customers	\$ 103,245
Cash paid to suppliers	<u>(230,107)</u>
<b>Net cash provided by (used for) operating activities</b>	<b><u>\$ (126,862)</u></b>
<b>Cash Flows from Noncapital Financing Activities</b>	
Property taxes and aids	<b><u>\$ 58,899</u></b>
<b>Cash Flows from Capital and Related Financing Activities</b>	
Proceeds from Public Facilities Authority general obligation note	\$ 6,845
Proceeds from a Corp of Engineers Section 569 grant	285,763
Payments for acquisition or construction of capital assets	(78,505)
Principal paid on long-term debt	(6,000)
Interest paid on long-term debt	<u>(5,734)</u>
<b>Net cash provided by (used for) capital and related financing activities</b>	<b><u>\$ 202,369</u></b>
<b>Cash Flows from Investing Activities</b>	
Interest income	<b><u>\$ 1,272</u></b>
<b>Net Increase (Decrease) in Cash</b>	<b>\$ 135,678</b>
<b>Cash - January 1, 2006</b>	<b><u>56,575</u></b>
<b>Cash - December 31, 2006</b>	<b><u><u>\$ 192,253</u></u></b>
<b>Reconciliation of Operating Income (Loss) to Net Cash Provided by (Used for) Operating Activities</b>	
Net operating income (loss)	\$ (153,276)
Adjustments to reconcile net operating income (loss) to net cash provided by (used for) operating activities	
Depreciation	118,916
Decrease (increase) in receivables	(12,531)
Decrease (increase) in inventory	(8,815)
Increase (decrease) in payables	(76,890)
Increase (decrease) in debt-related costs	<u>5,734</u>
<b>Net Cash Provided by (Used for) Operating Activities</b>	<b><u><u>\$ (126,862)</u></u></b>

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**KNIFE RIVER-LARSMONT SANITARY DISTRICT  
KNIFE RIVER, MINNESOTA**

**NOTES TO THE FINANCIAL STATEMENTS  
AS OF AND FOR THE YEAR ENDED DECEMBER 31, 2006**

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1. Summary of Significant Accounting Policies

The accounting policies of the Knife River-Larsmont Sanitary District conform to generally accepted accounting principles.

A. Financial Reporting Entity

The Knife River-Larsmont Sanitary District was formed May 8, 2001, pursuant to Minn. Stat. §§ 115.18 to 115.37. The District was created for the purpose of promoting the public health and welfare by providing an adequate and efficient means of collecting, conveying, pumping, treating, and disposing of domestic sewage and industrial waste within the District. The District is governed by a five-member Board. Each member of the Board must be a voter residing in the District.

The Knife River-Larsmont Sanitary District is a primary government, as defined by Governmental Accounting Standards Board (GASB) Statement 14, and there are no component units for which the District is financially accountable.

B. Basis of Presentation

The accounts of the Knife River-Larsmont Sanitary District 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.

Operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of the District. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as taxes, grants, and investment earnings, result from nonexchange transactions or incidental activities. The District's net assets are reported in two parts: (1) invested in capital assets, net of related debt; and (2) unrestricted net assets.

**KNIFE RIVER-LARSMONT SANITARY DISTRICT  
KNIFE RIVER, MINNESOTA**

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1. Summary of Significant Accounting Policies (Continued)

C. Basis of Accounting

The District uses the accrual basis of accounting. Revenues are recognized when earned, and expenses are recognized when incurred. Pursuant to GASB Statement 20, the District has elected to not apply accounting standards issued after November 30, 1989, by the Financial Accounting Standards Board.

D. Assets and Liabilities

Cash

Cash consists of an operations checking account, a repair and replacement savings account, and a project savings account. Cash and cash equivalents include cash and petty cash.

Taxes Receivable and Revenue

A property tax levy was established to finance operations. In Minnesota, counties act as collection agents for all property taxes. Tax settlements are received four times a year--in January, June, July, and December. The December 2006 settlement was not received by the District until January 2007. The tax levy is recognized as revenue in the year of the levy.

Inventory

Inventory is valued at cost using the first in/first out (FIFO) method. Inventory is recorded as an expense when consumed.

Capital Assets

Capital assets are stated at cost. Depreciation is determined using the straight-line method for the estimated useful lives of the assets.

<u>Classification</u>	<u>Estimated Life</u>
Sewer plant	15 years
Collection system	40 years
Equipment	5 years

**KNIFE RIVER-LARSMONT SANITARY DISTRICT  
KNIFE RIVER, MINNESOTA**

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1. Summary of Significant Accounting Policies (Continued)

E. 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 these estimates.

2. Detailed Notes

A. Deposits

Minn. Stat. § 118A.02 authorizes the District to deposit its cash and to invest in certificates of deposit in financial institutions designated by the District's Board. The District does not have a policy on custodial credit risk. At December 31, 2006, the District's deposits totaled \$202,409, all of which were cash deposits insured as required by Minnesota statutes. The carrying value of these deposits was \$192,203. During the year, the District did not have an adequate amount of insurance and collateral pledged to cover its deposits.

B. Capital Assets

A summary of the changes in capital assets for the year ended December 31, 2006, follows:

	Balance January 1, 2006	Additions	Transfer/ Reclassify	Balance December 31, 2006
Capital assets not depreciated				
Construction in progress	\$ 1,578,162	\$ 72,050	\$ (1,650,212)	\$ -
Capital assets depreciated				
Sewer plant	\$ 661,237	\$ -	\$ -	\$ 661,237
Collection system	3,054,790	-	1,650,212	4,705,002
Equipment	1,188	6,455	-	7,643
Total capital assets depreciated	\$ 3,717,215	\$ 6,455	\$ 1,650,212	\$ 5,373,882

**KNIFE RIVER-LARSMONT SANITARY DISTRICT  
KNIFE RIVER, MINNESOTA**

2. Detailed Notes

B. Capital Assets (Continued)

	Balance January 1, 2006	Additions	Transfer/ Reclassify	Balance December 31, 2006
Less: accumulated depreciation for				
Sewer plant	\$ 661,237	\$ -	\$ -	\$ 661,237
Collection system	1,392,958	117,625	-	1,510,583
Equipment	1,188	1,291	-	2,479
Total capital assets depreciated	\$ 2,055,383	\$ 118,916	\$ -	\$ 2,174,299
Total capital assets depreciated, net	\$ 1,661,832	\$ (112,461)	\$ 1,650,212	\$ 3,199,583
Total Capital Assets, Net	\$ 3,239,994	\$ (40,411)	\$ -	\$ 3,199,583

On June 24, 2004, the Knife River-Larsmont Sanitary District Board voted to terminate operations at its treatment plant and to connect to the Duluth/North Shore Sanitary District sewer line. On March 3, 2006, the Knife River-Larsmont Sanitary District's sewer line was connected to the Duluth/North Shore Sanitary District, with the flowage going to the Western Lake Superior Sanitary District. As of March 2006, the District is no longer operating its sewer treatment plant.

C. Construction Funding Sources

Cumulative construction and debt-related costs and funding sources as of December 31, 2006, follow:

Construction costs	
Engineering and design	\$ 110,526
Construction	930,276
Legal costs	6,171
Accounting costs	2,639
Hook-up fee paid to Duluth/North Shore Sanitary District	600,600
Total construction costs	\$ 1,650,212
Debt-related costs	17,389
Total Construction and Debt-Related Costs	\$ 1,667,601



**KNIFE RIVER-LARSMONT SANITARY DISTRICT  
KNIFE RIVER, MINNESOTA**

2. Detailed Notes

C. Construction Funding Sources (Continued)

Funding sources		
Minnesota Public Facilities loan	\$	882,212
Minnesota Public Facilities grant		620,000
Corps of Engineers Section 569 grant		165,389
Total Funding Sources	\$	1,667,601

D. Long-Term Obligations

The following is a summary of the District's long-term debt activity for the year ended December 31, 2006:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Public Facilities Authority general obligation notes	\$ 875,367	\$ 6,845	\$ 6,000	\$ 876,212	\$ 41,000

Long-term debt is composed of the following:

\$882,212 General Obligation Note issued to the Minnesota Public Facilities Authority. Amounts drawn or receivable on this note as of December 31, 2006, were \$876,212. Note payments are due semi-annually on February 20 and August 20, 2006 through 2025, at an interest rate of 1.31 percent.

Debt service requirements at December 31, 2006, are as follows:

Year Ending December 31	General Obligation Revenue Note	
	Principal	Interest
2007	\$ 41,000	\$ 11,469
2008	41,000	10,942
2009	42,000	10,404
2010	43,000	9,854
2011	43,000	9,290
2012 - 2016	224,000	37,834
2017 - 2021	239,000	22,768
2022 - 2025	203,212	6,706
Total	\$ 876,212	\$ 119,267

**KNIFE RIVER-LARSMONT SANITARY DISTRICT  
KNIFE RIVER, MINNESOTA**

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2. Detailed Notes

D. Long-Term Obligations (Continued)

The general obligation note will be retired with income from operations, property taxes, investment income, and unused construction funding and are exempt from the limitations on net debt imposed by Minnesota law.

3. Risk Management

The Knife River-Larsmont Sanitary District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters. The District has purchased commercial insurance to insure these risks. There are no employees of the Knife River-Larsmont Sanitary District as the District has hired independent contractors to operate the plant and perform its accounting functions. There were no significant reductions in insurance coverage from the previous year. There were no settlements in excess of insurance during the audit period.

4. Summary of Significant Contingencies and Other Items

Contingent Liability

Lake County has paid for certain engineering and other expenses on behalf of the Knife River-Larsmont Sanitary District for the period of 1997 to 2005, with the understanding that if funding becomes available to the District, these expenses would be reimbursed to Lake County. According to Lake County records, the amount owed from the Knife River-Larsmont Sanitary District to Lake County at December 31, 2006, is \$462,372. This is not reported as a liability on the Knife River-Larsmont Sanitary District's financial statements.



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**KNIFE RIVER-LARSMONT SANITARY DISTRICT  
KNIFE RIVER, MINNESOTA**

**SCHEDULE OF FINDINGS AND RECOMMENDATIONS  
FOR THE YEAR ENDED DECEMBER 31, 2006**

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

INTERNAL CONTROL

PREVIOUSLY REPORTED ITEMS NOT RESOLVED

02-1 Internal Control/Segregation of Duties

The Knife River-Larsmont Sanitary District's Board of Managers is responsible for establishing and maintaining internal control. This responsibility includes the internal control over the various accounting cycles, the fair presentation of the financial statements and related notes, and the accuracy and completeness of all financial records and related information. Adequate segregation of duties is a key internal control in an organization's accounting system. The size of the Knife River-Larsmont Sanitary District and its staffing limits the internal control that management can design and implement into the organization. The Board of Managers should be aware that segregation of duties is not adequate from an internal control point of view.

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

The Board of Managers has requested that we prepare the annual financial statements and related notes. This arrangement is not unusual for an organization the size of the Knife River-Larsmont Sanitary District. This decision was based on the availability of the District's staff and the cost benefit of using our expertise.

During our audit, we proposed numerous adjustments to convert the District's financial records to the financial statements as reported. These adjustments, which were determined to be material to the financial statements, decreased assets, liabilities, net assets, and revenues and increased expenses.

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

Client's Response:

*Board members are aware of all transactions made by the bookkeeper. Monthly bank reconciliations and financial statements are reviewed by board members at monthly board meetings. The Board treasurer goes over all bills submitted to the District, and they are reviewed by the entire board at monthly meetings before payments are sent out.*

02-3 Delinquent Customer Receivables

The District's customer accounts receivable balance has been steadily increasing. The balance increased \$12,531 during 2006 to \$46,510 at December 31, 2006. Of the receivable balance at December 31, 2006, \$40,395 is over 90 days old.

The District has the option to certify delinquent customer receivables to Lake County to be collected as part of the customer's property taxes, but this option has not been exercised during the past seven years, resulting in increasing balances.

We recommend the Board of Managers review the detailed listing of receivables, identify troubled accounts, and implement collection procedures as deemed necessary.

Client's Response:

*Arrangements will be made for collections of delinquent customer accounts with the County Auditor's Office. The Board has decided to put delinquent accounts on taxes twice each year.*

02-4 Capital Assets

The Knife River-Larsmont Sanitary District does not maintain detailed capital asset records. The District's records of capital assets are summarized and do not include details such as the contractor or architect, date of acquisition, cost, or payment voucher number.

The above condition results in a lack of documentation of District assets. Because of the absence of specific detailed capital records documenting original cost, it would be difficult to identify and remove a capital asset from the records if one is disposed of at some point in the future.

We recommend the District bookkeeper prepare or obtain detailed capital asset records and retain all pertinent documents and records in its files.

Client's Response:

*There are no records of previous capital assets. Detailed records are being kept of any current capital assets.*

ITEM ARISING THIS YEAR

06-1 Checking Account Reconciliation

The District's checking account is not being reconciled to the general ledger. As a result, the amount recorded at year-end in the checking account was overstated by \$1,330. This overstatement was caused by an error and several unrecorded items in the District's general ledger.

By not reconciling the District's checking account on a regular basis, the District does not have an accurate cash balance at year-end.

We recommend that the District bookkeeper reconcile the bank balance to the general ledger balance on a monthly basis. Any discrepancies between the bank balance and the general ledger balance should be resolved in a timely manner.

Client's Response:

*The bookkeeper will make sure that the checking account balances with the general ledger on a monthly basis.*

**II. OTHER FINDINGS AND RECOMMENDATIONS**

MINNESOTA LEGAL COMPLIANCE

PREVIOUSLY REPORTED ITEM NOT RESOLVED

05-1 Collateral Pledged to Secure Deposits

Minn. Stat. § 118A.03 requires funds on deposit in excess of available federal deposit insurance to be secured by a corporate surety bond or pledged collateral. "The total amount of the collateral computed at its market value shall be at least ten percent more than the amount on deposit plus accrued interest at the close of the financial institution's banking day." Unsecured District deposits expose the District to loss if the financial institution fails.

In the prior audit, the District had deposits at the Lake Bank N.A. in excess of insurance for deposits, which resulted in unsecured deposits of \$812,390. No collateral was pledged to the District to cover the unsecured deposits. This also occurred in the current

audit. On January 9, 2006, the District had unsecured deposits of \$87,411, and no collateral was pledged to the District.

We recommend the District obtain the required collateral and closely monitor deposits and the related collateral pledged to secure those deposits to ensure sufficient coverage.

Client's Response:

*The District has worked with our banking institution, The Lake Bank N.A., on this requirement. This will be reviewed periodically.*

ITEM ARISING THIS YEAR

06-2 Board Minutes

Minn. Stat. § 13D.01, subd. 4, requires the District to record the votes of its governing body in a journal which must be kept accessible to the public. This journal must be kept as a permanent record under Minn. Stat. §§ 15.17; 138.17.

Legally, the minutes must record the vote of each member on each action taken by the Board (except for payments of judgments, claims, and amounts fixed by statute). We recommend that minutes also include: the subject matter of a motion; the persons making and seconding the motion; the character of resolutions or ordinances offered, including a brief description of their subject matter; and whether the motion was defeated or adopted.

The District Board cannot act without voting, and all votes must be recorded in the minutes. We found that, in 2006, the District opened a new bank account not approved in the Board minutes. The District also raised its user fee rate from \$48 to \$58, which also was not approved in the Board minutes.

The District was also unable to locate the May, June, and July 2006 minutes. These minutes were either not prepared or lost, as the Board was unable to provide those minutes to us. The minutes are considered public records of the District and must be maintained by the District.

We recommend that the District prepare and maintain its Board minutes in accordance with Minnesota statutes.

Client's Response:

*Board minutes will be more precise. The Board will make sure they make a motion for actions taken. Safety precautions have been implemented to make sure that minutes are not lost again.*





REBECCA OTTO  
STATE AUDITOR

# 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***

Board of Managers  
Knife River-Larsmont Sanitary District

We have audited the basic financial statements of the Knife River-Larsmont Sanitary District as of and for the year ended December 31, 2006, and have issued our report thereon dated March 10, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

#### Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Knife River-Larsmont Sanitary District's internal control over financial reporting as a basis for designing our auditing procedures 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 District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over financial reporting.

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

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination

of control deficiencies, that adversely affects the District's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the District's financial statements that is more than inconsequential will not be prevented or detected by the District's internal control. We considered the deficiencies described in the accompanying Schedule of Findings and Recommendations as items 02-1 through 02-4 and 06-1 to be significant deficiencies in internal control over financial reporting.

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider item 02-1 to be a material weakness.

#### Compliance and Other Matters

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

#### Minnesota Legal Compliance

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

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

The results of our tests indicate that, for the items tested, the District complied with the material terms and conditions of applicable legal provisions, except as described in the Schedule of Findings and Recommendations as items 05-1 and 06-2.

The Knife River-Larsmont Sanitary District's written responses to the significant deficiencies, material weakness, and legal compliance findings identified in our audit have not been subjected to any auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the District's Board of Managers, management, and others within the Knife River-Larsmont Sanitary District and is not intended to be, and should not be, used by anyone other than those specified parties.

*/s/Rebecca Otto*

REBECCA OTTO  
STATE AUDITOR

*/s/Greg Hierlinger*

GREG HIERLINGER, CPA  
DEPUTY STATE AUDITOR

March 10, 2008