

STATE OF MINNESOTA

Office of the State Auditor



**Rebecca Otto
State Auditor**

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

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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**LINCOLN COUNTY
IVANHOE, MINNESOTA**

Year Ended December 31, 2006



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

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**LINCOLN COUNTY
IVANHOE, MINNESOTA**

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IVANHOE, MINNESOTA**

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**LINCOLN COUNTY
IVANHOE, MINNESOTA**

ORGANIZATION
2006

<u>Office</u>	<u>Name</u>	<u>Term Expires</u>
Commissioners		
1st District	Jim Johansen	January 2009
2nd District	Larry Hansen ²	January 2007
3rd District	Deane Sagmoe	January 2009
4th District	Curtis Blumeyer ¹	January 2007
5th District	Joan Jagt	January 2009
Officers		
Elected		
Attorney	Glen Petersen	January 2007
Auditor	Kathy Schreurs	January 2007
District Judges		
	George I. Harrelson	January 2009
	Lee Bush	January 2009
	David W. Peterson	January 2009
County Recorder	Loretta Lundberg	January 2007
Registrar of Titles	Loretta Lundberg	January 2007
Sheriff	Jack Vizecky	January 2007
Treasurer	Mark R. Leibfried	January 2007
Appointed		
Acting Assessor	Bruce Nielsen	Indefinite
Coroner	Richard D. Mulder, M.D.	Indefinite
Environmental Officer	Robert Olsen	Indefinite
Highway Engineer	Lee Amundson	May 2009
Veterans Service Officer	Gary Serie	Indefinite
Emergency Management	Norm VanOverbeke	Indefinite

¹Chair 2007

²Chair 2006

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

**ORGANIZATION SCHEDULE
LAKE BENTON LAKE IMPROVEMENT DISTRICT
BOARD OF DIRECTORS
2006**

<u>Name</u>	<u>Position</u>
Director	
Sam Hedge	Chair
Greg Peter	Vice Chair
Ed Gruhot	Treasurer
L. W. Kline	Secretary
Martin Ritter	Publicity Chair
Mark McCallum	Member
Betty Popkes	Member
Staff	
Glen Peterson	Attorney

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REBECCA OTTO
STATE AUDITOR

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INDEPENDENT AUDITOR'S REPORT

Board of County Commissioners
Lincoln County

We have audited the basic financial statements of the governmental activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of Lincoln County as of and for the year ended December 31, 2006, which collectively comprise the County's basic financial statements, as listed in the table of contents. These financial statements are the responsibility of the County's management. Our responsibility is to express opinions on these financial statements based on our audit.

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

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of Lincoln County as of December 31, 2006, and the changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis and the budgetary comparison schedules 1 through 4 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the basic financial statements of Lincoln County. The statements and schedules listed as supplementary information in the table of contents are presented for the purpose of additional analysis and are not a required part of the basic financial statements of Lincoln County. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented in all material respects in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 14, 2008, on our consideration of the Lincoln County's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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 14, 2008

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

MANAGEMENT'S DISCUSSION AND ANALYSIS

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**LINCOLN COUNTY
IVANHOE, MINNESOTA**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2006
(Unaudited)**

As management of Lincoln County, Minnesota, we offer the readers of the Lincoln County financial statements this narrative overview and analysis of its financial activities for the fiscal year ended December 31, 2006. We encourage readers to consider the information presented here in conjunction with the basic financial statements that follow this section. All amounts, unless otherwise indicated, are expressed in whole dollars.

FINANCIAL HIGHLIGHTS

- The assets of Lincoln County exceeded its liabilities on December 31, 2006, by \$36,408,613 (net assets). Of this amount, \$5,941,187 (unrestricted net assets) may be used to meet the County's ongoing obligations to citizens and creditors.
- Lincoln County's total net assets increased by \$2,158,546 in 2006. This shows up primarily in the County's investment in capital assets, net of accumulated depreciation.
- As of the close of 2006, Lincoln County's governmental funds reported combined ending fund balances of \$6,489,800, a decrease of \$145,388 in comparison with 2005. Of this balance amount, \$5,018,880 was unreserved and undesignated by Lincoln County, and thus available for spending at the County's discretion.
- At the end of 2006, unreserved, undesignated fund balance for the General Fund was \$2,642,991, or 70 percent, of the total General Fund expenditures for that year.
- Lincoln County's total debt decreased by \$1,621,136, or 33 percent, during 2006. The key factor in this decrease was the payment of the G.O. Refunding Bonds due in February 2006.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the Lincoln County basic financial statements. Lincoln County's financial statements are composed of three components: (1) government-wide financial statements, (2) fund level financial statements, and (3) notes to the financial statements. This report also contains other supplementary information.

Government-Wide Financial Statements

Government-wide financial statements are designed to provide readers with a broad overview of Lincoln County's finances in a manner similar to a private-sector business.

The statement of net assets presents information on all of Lincoln County's assets and liabilities, with the difference being reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of Lincoln County is improving or deteriorating.

The statement of activities presents information showing how the County's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows only in future fiscal periods (for example, uncollected taxes and earned but unused vacation leave).

Lincoln County's government-wide financial statements distinguish functions of the County that are principally supported by taxes and intergovernmental revenues (governmental activities). The governmental activities of Lincoln County include general government, public safety, highways, sanitation, human services, health, culture and recreation, conservation of natural resources, economic development, and interest. Lincoln County has no business-type activities.

The government-wide financial statements include not only Lincoln County (known as the primary government), but also a legally separate entity known as Lake Benton Lake Improvement District, for which Lincoln County is financially accountable. Financial information for this component unit is reported separately from the financial information presented for the primary government itself.

Fund Level Statements

A fund is a grouping of related accounts used to maintain control over resources that have been segregated for specific activities or objectives. Lincoln County, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with financial-related legal requirements. All of the funds of Lincoln County can be divided into two categories: governmental funds and fiduciary funds.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financial requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financial decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

Lincoln County adopts an annual appropriated budget for its General Fund, Road and Bridge Special Revenue Fund, Human Services Special Revenue Fund, Ditch Special Revenue Fund, and Jail Facility Debt Service Fund. Supplementary budgetary comparison schedules have been provided for these funds to demonstrate compliance with the budget. The basic governmental fund financial statements can be found on Exhibits 3 through 6 of this report.

Fiduciary funds are used to account for resources held for the benefit of parties outside of Lincoln County. Fiduciary funds are not reflected in the government-wide statements because the resources of those funds are not available to support Lincoln County's own programs or activities. The accounting for fiduciary funds is much like that used for business-type funds.

Notes to the Financial Statements

Notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 24 through 52 of this report.

Other Information

Other information is provided in addition to the basic financial statements and accompanying notes, this report also presents certain supplementary information. The budgetary comparison for the Jail Facility Debt Service Fund, combining statements referred to earlier in connection with fiduciary funds, component unit statements, and information regarding Lincoln County's intergovernmental revenues are presented.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Over time, net assets serve as a useful indicator of the County's financial position. Lincoln County's assets exceeded liabilities by \$36,408,613 at the close of 2006. The largest portion of Lincoln County's net assets (78 percent) reflects the County's investment in capital assets (for example, land, buildings, equipment, and infrastructure such as roads and bridges), less any related debt used to acquire those assets (that is still outstanding). However, it should be noted that these assets are not available for future spending or for liquidating any remaining debt.

Net Assets

	Governmental Activities	
	2006	2005
Assets		
Current and other assets	\$ 9,736,866	\$ 10,335,476
Capital assets	30,389,427	29,402,820
Total Assets	\$ 40,126,293	\$ 39,738,296
Liabilities		
Long-term liabilities	\$ 2,966,686	\$ 2,881,367
Other liabilities	750,994	2,606,862
Total Liabilities	\$ 3,717,680	\$ 5,488,229
Net Assets		
Invested in capital assets, net of related debt	\$ 28,572,723	\$ 27,571,569
Restricted	1,894,703	1,470,361
Unrestricted	5,941,187	5,208,137
Total Net Assets	\$ 36,408,613	\$ 34,250,067

The unrestricted net assets amount of \$5,941,187 as of December 31, 2006, may be used to meet the County's ongoing obligations to citizens and creditors.

Governmental Activities

Lincoln County's activities increased Lincoln County's net assets during 2006 by \$2,158,546, representing a 6.3 percent increase, primarily because of the County's investment in capital assets. Key elements in this increase in net assets are as follows:

Changes in Net Assets

	2006	2005
Revenues		
Program revenues		
Charges for services	\$ 1,262,786	\$ 974,902
Operating grants and contributions	3,386,926	2,007,109
Capital grants and contributions	519,333	1,485,908
General revenues		
Property taxes	2,834,907	2,634,704
Other	1,790,273	1,697,341
Total Revenues	\$ 9,794,225	\$ 8,799,964

	2006	2005
Expenses		
General government	\$ 1,485,807	\$ 1,337,932
Public safety	895,554	854,236
Highways and streets	2,979,961	2,928,517
Sanitation	110,956	125,443
Human services	832,102	732,471
Health	37,087	37,080
Culture and recreation	194,921	156,542
Conservation of natural resources	949,681	607,800
Economic development	53,351	53,783
Interest	96,259	192,373
	<u>\$ 7,635,679</u>	<u>\$ 7,026,177</u>
Total Expenses		
Increase in Net Assets	\$ 2,158,546	\$ 1,773,787
Net Assets - January 1	<u>34,250,067</u>	<u>32,476,280</u>
Net Assets - December 31	<u>\$ 36,408,613</u>	<u>\$ 34,250,067</u>

FINANCIAL ANALYSIS OF THE GOVERNMENT'S FUNDS

As noted earlier, Lincoln County uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds

The focus of the County's governmental funds is to provide information on short-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the County's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

As of the end of the current fiscal year, Lincoln County's governmental funds reported combined ending fund balances of \$6,489,800, a decrease of \$145,388 in comparison with the prior year. Of the ending fund balance, \$5,251,905 represents unreserved fund balance, which is available for spending at the County's discretion. The remainder of fund balance is reserved to indicate that it is not available for new spending because it has already been committed for various reasons.

The General Fund is the chief operating fund for Lincoln County. At the end of the current fiscal year, it had an unreserved fund balance of \$2,760,290. As a measure of the General Fund's liquidity, it may be useful to compare unreserved fund balance to total expenditures. General Fund unreserved fund balance represents 73 percent of total General Fund expenditures. In 2006, fund balance in the General Fund increased by \$345,362. The primary reasons for this increase were increases in special assessments and charges for services.

The Road and Bridge Special Revenue Fund's unreserved fund balance of \$2,203,674 at year-end represents 56 percent of the fund's annual expenditures. Unreserved fund balance increased \$1,130,970 during 2006, primarily due to the reduction of road projects and costs associated with those projects.

The Human Services function for Lincoln County is performed through a joint powers agreement between Lincoln, Lyon, and Murray Counties, and is known as Lincoln, Lyon, & Murray Human Services. Lincoln County participates in this joint powers authority and annually levies a human service levy on Lincoln County property as required by the governing Human Services Board. Detailed financial information of the activities of Human Services can be addressed to Lincoln, Lyon, & Murray Human Services, 607 West Main Street, Marshall, Minnesota 56258.

The Ditch Special Revenue Fund had an unreserved ending balance of \$287,941. This ending balance represents a \$96,652 decrease in fund balance from the prior year. The decrease is attributed to more than expected expenditures for the various County ditches.

General Fund Budgetary Highlights

The final General Fund expenditure budget exceeded the original amended budget by \$191,587.

Actual General Fund revenues exceeded budgeted revenues by \$776,761, primarily due to more pass-through intergovernmental receipts and more than expected investment earnings.

Actual expenditures exceeded budgeted expenditures by \$151,816. The more than expected expenditures reflect higher than anticipated operating costs. Water quality loan program expenses of \$293,875 were not included in the 2006 budget.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

Lincoln County's depreciable capital assets for its governmental activities at December 31, 2006, totaled \$29,811,732 (net of accumulated depreciation). This investment in capital assets includes land improvements, buildings, equipment, and infrastructure. The County's investment in depreciable capital assets increased \$3,210,935, or 12.1 percent, from the previous year. The major capital asset event was Road and Bridge projects of \$3.9 million.

Governmental Capital Assets

	2006	2005
Capital assets depreciated		
Land improvements	\$ 254,940	\$ 243,048
Buildings	4,134,598	2,621,524
Machinery and equipment	3,463,345	3,232,775
Infrastructure	32,123,231	29,793,285
 Total capital assets depreciated	 \$ 39,976,114	 \$ 35,890,632
Less: accumulated depreciation for		
Land improvements	\$ 99,452	\$ 88,607
Buildings	790,578	726,864
Machinery and equipment	2,551,665	2,351,426
Infrastructure	6,722,687	6,122,938
 Total accumulated depreciation	 \$ 10,164,382	 \$ 9,289,835
 Total Capital Assets Depreciated, Net	 \$ 29,811,732	 \$ 26,600,797

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

Long-Term Debt

At the end of the current fiscal year, the County had a total outstanding debt of \$3,233,525 for governmental activities, which was backed by the full faith and credit of the government. Other liabilities and contingencies are described in the notes to the financial statements.

Outstanding Debt

	2006	2005
Special assessment debt	\$ 12,000	\$ 74,000
General obligation bonds	1,790,000	3,560,000
Leases payable	26,704	41,251
Loans payable	1,259,277	1,049,661
Compensated absences	145,544	129,749
 Total	 \$ 3,233,525	 \$ 4,854,661

The County's debt related to special assessment obligation bonds and notes decreased by \$62,000 (84 percent) during the fiscal year due to repayment of principal. General obligation bonded debt decreased by \$1,770,000 (50 percent) during the fiscal year due to repayment of principal of the G.O. Refunding Bonds held by the escrow agent and paid in February of 2006.

Minnesota statutes limit the amount of debt a county may levy to two percent of its total market value of \$621,809,300. At the end of 2006, Lincoln County's debt was less than one percent of its total market value.

Additional information on the County's long-term debt can be found in the notes to the financial statements of this report.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS

The unemployment rate for Lincoln County at the end of 2006 was 4.2 percent. This compares with the state unemployment rate of 4.2 percent and shows a decrease from the 4.3 percent rate of one year ago.

Mortgage interest rates have been extremely low, causing many to refinance their mortgages and/or finance new construction.

On December 20, 2005, the Lincoln County Board of Commissioners approved the 2006 budget and adopted a property tax levy of \$3,262,590, which represents an 8.31 percent increase over the 2005 property tax levy of \$3,012,365.

LAKE BENTON LAKE IMPROVEMENT DISTRICT

Lake Benton Lake Improvement District is a component unit of the County. The component unit is included in the County's financial report because of the significance of its operational and financial relationship with the County. It is reported in a separate column to emphasize that it is legally separate from the County.

Financial Highlights

The Lake Benton Lake Improvement District's governmental activities' total net assets are a deficit of \$120,975. The District had immaterial activity in 2004 and became a component unit of Lincoln County in 2005.

Government-Wide Financial Analysis

Over time, net assets serve as a useful indicator of the District's financial position. The District's liabilities exceeded assets by \$120,975 at the close of 2006.

Lake Benton Lake Improvement District Net Assets

	<u>Governmental Activities 2006</u>
Assets	
Current and other assets	\$ 19,025
Liabilities	
Due to primary government	<u>140,000</u>
Net Assets	
Restricted	<u>\$ (120,975)</u>

REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of Lincoln County's finances. Questions concerning any of the information provided in this report, or requests for additional financial information, should be addressed to Kathy Schreurs, Lincoln County Auditor, 319 North Rebecca Street, Ivanhoe, Minnesota 56142.

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BASIC FINANCIAL STATEMENTS

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GOVERNMENT-WIDE FINANCIAL STATEMENTS

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**LINCOLN COUNTY
IVANHOE, MINNESOTA**

EXHIBIT 1

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

	Primary Government Governmental Activities	Discretely Presented Component Unit
<u>Assets</u>		
Cash and pooled investments	\$ 5,764,065	\$ 17,278
Receivables - net	3,543,239	1,747
Due from component unit	140,000	-
Inventories	266,918	-
Deferred charges	22,644	-
Capital assets		
Nondepreciable capital assets	577,695	-
Depreciable capital assets - net of accumulated depreciation	29,811,732	-
Total Assets	\$ 40,126,293	\$ 19,025
<u>Liabilities</u>		
Accounts payable and other current liabilities	\$ 483,279	\$ -
Due to primary government	-	140,000
Accrued interest payable	28,203	-
Long-term liabilities		
Due within one year	239,512	-
Due in more than one year	2,966,686	-
Total Liabilities	\$ 3,717,680	\$ 140,000
<u>Net Assets</u>		
Invested in capital assets, net of related debt	\$ 28,572,723	\$ -
Restricted for		
Debt service	241,824	-
Public safety	142,446	-
Highways and streets	1,333,248	-
Conservation of natural resources	120,279	-
Other purposes	56,906	-
Unrestricted	5,941,187	(120,975)
Total Net Assets	\$ 36,408,613	\$ (120,975)

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

**STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2006**

	Expenses	Fees, Charges, Fines, and Other
<u>Functions/Programs</u>		
Primary Government		
Governmental activities		
General government	\$ 1,485,807	\$ 321,347
Public safety	895,554	117,268
Highways and streets	2,979,961	238,985
Sanitation	110,956	81,501
Human services	832,102	-
Health	37,087	-
Culture and recreation	194,921	59,635
Conservation of natural resources	949,681	444,050
Economic development	53,351	-
Interest	96,259	-
Total Primary Government	\$ 7,635,679	\$ 1,262,786
Component Unit		
Lake Benton Lake Improvement District	\$ 134,848	\$ -

General Revenues

Property taxes
Mortgage registry and deed tax
Wind production tax
Payments in lieu of tax
Grants and contributions not restricted to specific programs
Investment earnings
Miscellaneous

Total general revenues

Change in Net Assets

Net Assets - Beginning

Net Assets - Ending

EXHIBIT 2

Program Revenues		Net (Expense) Revenue and Changes in Net Assets	
Operating Grants and Contributions	Capital Grants and Contributions	Primary Government Governmental Activities	Discretely Presented Component Unit
\$ 303,517	\$ -	\$ (860,943)	
129,044	-	(649,242)	
2,666,403	519,333	444,760	
49,079	-	19,624	
-	-	(832,102)	
-	-	(37,087)	
31,083	-	(104,203)	
207,800	-	(297,831)	
-	-	(53,351)	
-	-	(96,259)	
\$ 3,386,926	\$ 519,333	\$ (2,466,634)	
\$ 47,500	\$ 5,990		\$ (81,358)
		\$ 2,834,907	\$ 22,195
		15,282	-
		328,074	-
		66,404	-
		1,032,903	-
		262,361	-
		85,249	2,359
		\$ 4,625,180	\$ 24,554
		\$ 2,158,546	\$ (56,804)
		34,250,067	(64,171)
		\$ 36,408,613	\$ (120,975)

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FUND FINANCIAL STATEMENTS

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GOVERNMENTAL FUNDS

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**LINCOLN COUNTY
IVANHOE, MINNESOTA**

EXHIBIT 3

**BALANCE SHEET
GOVERNMENTAL FUNDS
DECEMBER 31, 2006**

	<u>General</u>	<u>Road and Bridge</u>	<u>Human Services</u>	<u>Ditch</u>	<u>Jail Facility Debt Service</u>	<u>Total</u>
<u>Assets</u>						
Cash and pooled investments	\$ 3,244,335	\$ 1,804,630	\$ 106,452	\$ 287,768	\$ 264,554	\$ 5,707,739
Undistributed cash in agency funds	25,346	13,651	11,947	853	2,739	54,536
Petty cash and change funds	1,790	-	-	-	-	1,790
Taxes receivable						
Prior	17,744	13,370	11,942	-	2,734	45,790
Special assessments receivable						
Prior	5,472	-	-	955	-	6,427
Noncurrent	1,107,704	-	-	81,035	-	1,188,739
Accounts receivable	80,692	2,877	-	697	-	84,266
Accrued interest receivable	53,813	-	-	-	-	53,813
Due from other governments	37,326	2,126,878	-	-	-	2,164,204
Due from component unit	140,000	-	-	-	-	140,000
Inventories	-	266,918	-	-	-	266,918
Total Assets	<u>\$ 4,714,222</u>	<u>\$ 4,228,324</u>	<u>\$ 130,341</u>	<u>\$ 371,308</u>	<u>\$ 270,027</u>	<u>\$ 9,714,222</u>

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

**EXHIBIT 3
(Continued)**

**BALANCE SHEET
GOVERNMENTAL FUNDS
DECEMBER 31, 2006**

	<u>General</u>	<u>Road and Bridge</u>	<u>Human Services</u>	<u>Ditch</u>	<u>Jail Facility Debt Service</u>	<u>Total</u>
<u>Liabilities and Fund Balances</u>						
Liabilities						
Accounts payable	\$ 37,479	\$ 43,971	\$ -	\$ 1,377	\$ -	\$ 82,827
Salaries payable	59,590	28,742	-	-	-	88,332
Contracts payable	13,485	104,991	-	-	-	118,476
Due to other governments	75,245	-	118,399	-	-	193,644
Deferred revenue - unavailable	1,156,155	1,488,322	11,942	81,990	2,734	2,741,143
Total Liabilities	\$ 1,341,954	\$ 1,666,026	\$ 130,341	\$ 83,367	\$ 2,734	\$ 3,224,422
Fund Balances						
Reserved for						
Debt service	\$ -	\$ -	\$ -	\$ -	\$ 267,293	\$ 267,293
Encumbrances	-	91,706	-	-	-	91,706
Inventories	-	266,918	-	-	-	266,918
Missing heirs	268	-	-	-	-	268
Law library	774	-	-	-	-	774
Recorder's technology fund	17,592	-	-	-	-	17,592
Recorder's compliance fund	27,732	-	-	-	-	27,732
Enhanced 911	125,898	-	-	-	-	125,898
Sheriff's contingency	14,055	-	-	-	-	14,055
Attorney's forfeited property	772	-	-	-	-	772
Gun permit fees	2,493	-	-	-	-	2,493
Due from component unit	140,000	-	-	-	-	140,000
Septic/sewer loans	151,573	-	-	-	-	151,573
Election equipment	10,542	-	-	-	-	10,542
Unspent grant monies	120,279	-	-	-	-	120,279
Unreserved						
Designated for future expenditures	55,980	110,000	-	-	-	165,980
Designated for recycling	61,319	-	-	-	-	61,319
Designated for debt service	-	-	-	5,726	-	5,726
Undesignated	2,642,991	2,093,674	-	282,215	-	5,018,880
Total Fund Balances	\$ 3,372,268	\$ 2,562,298	\$ -	\$ 287,941	\$ 267,293	\$ 6,489,800
Total Liabilities and Fund Balances	\$ 4,714,222	\$ 4,228,324	\$ 130,341	\$ 371,308	\$ 270,027	\$ 9,714,222

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

EXHIBIT 4

**RECONCILIATION OF GOVERNMENTAL FUNDS BALANCE SHEET TO
THE GOVERNMENT-WIDE STATEMENT OF NET ASSETS--GOVERNMENTAL ACTIVITIES
DECEMBER 31, 2006**

Fund balances - total governmental funds (Exhibit 3)	\$	6,489,800
Amounts reported for governmental activities in the statement of net assets are different because:		
Capital assets, net of accumulated depreciation, used in governmental activities are not financial resources and, therefore, are not reported in the governmental funds.		30,389,427
Other long-term assets are not available to pay for current period expenditures and, therefore, are deferred in the governmental funds.		2,741,143
Long-term liabilities are not due and payable in the current period and, therefore, are not reported in the governmental funds.		
General obligation bonds	\$	(1,802,000)
Capital leases		(26,704)
Loans payable		(1,259,277)
Compensated absences		(145,544)
Accrued interest payable		(28,203)
Unamortized discount on G.O. bonds		27,327
Deferred debt issuance charges		22,644
		(3,211,757)
Net Assets of Governmental Activities (Exhibit 1)	\$	<u>36,408,613</u>

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

EXHIBIT 5

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2006**

	<u>General</u>	<u>Road and Bridge</u>	<u>Human Services</u>	<u>Ditch</u>	<u>Jail Facility Debt Service</u>	<u>Total</u>
Revenues						
Taxes	\$ 1,478,878	\$ 826,005	\$ 723,572	\$ -	\$ 165,874	\$ 3,194,329
Special assessments	175,680	-	-	57,684	-	233,364
Licenses and permits	23,355	4,125	-	-	-	27,480
Intergovernmental	1,560,650	3,811,334	108,530	-	24,856	5,505,370
Charges for services	303,249	205,713	-	-	-	508,962
Fines and forfeits	6,271	-	-	-	-	6,271
Gifts and contributions	1,813	-	-	-	-	1,813
Investment earnings	225,851	-	-	-	19,682	245,533
Miscellaneous	278,530	29,716	-	2,745	-	310,991
Total Revenues	\$ 4,054,277	\$ 4,876,893	\$ 832,102	\$ 60,429	\$ 210,412	\$ 10,034,113
Expenditures						
Current						
General government	\$ 1,650,391	\$ -	\$ -	\$ -	\$ -	\$ 1,650,391
Public safety	829,908	-	-	-	-	829,908
Highways and streets	-	3,766,065	-	-	-	3,766,065
Sanitation	110,956	-	-	-	-	110,956
Health	421	-	-	-	-	421
Culture and recreation	195,225	-	-	-	-	195,225
Conservation of natural resources	772,373	-	-	100,460	-	872,833
Economic development	52,935	-	-	-	-	52,935
Intergovernmental	36,666	196,859	832,102	-	-	1,065,627
Debt service						
Principal	97,828	-	-	62,000	1,770,000	1,929,828
Interest	14,481	-	-	2,085	118,271	134,837
Administrative (fiscal) fees	-	-	-	-	814	814
Total Expenditures	\$ 3,761,184	\$ 3,962,924	\$ 832,102	\$ 164,545	\$ 1,889,085	\$ 10,609,840
Excess of Revenues Over (Under) Expenditures	\$ 293,093	\$ 913,969	\$ -	\$ (104,116)	\$ (1,678,673)	\$ (575,727)
Other Financing Sources (Uses)						
Transfers in	\$ -	\$ 264,565	\$ -	\$ 7,464	\$ -	\$ 272,029
Transfers out	(272,029)	-	-	-	-	(272,029)
Proceeds from sale of assets	34,000	-	-	-	-	34,000
Loans issued	290,298	-	-	-	-	290,298
Total Other Financing Sources (Uses)	\$ 52,269	\$ 264,565	\$ -	\$ 7,464	\$ -	\$ 324,298

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

**EXHIBIT 5
(Continued)**

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2006**

	<u>General</u>	<u>Road and Bridge</u>	<u>Human Services</u>	<u>Ditch</u>	<u>Jail Facility Debt Service</u>	<u>Total</u>
Net Change in Fund Balances	\$ 345,362	\$ 1,178,534	\$ -	\$ (96,652)	\$ (1,678,673)	\$ (251,429)
Fund Balances - January 1	3,026,906	1,277,723	-	384,593	1,945,966	6,635,188
Increase (decrease) in reserved for inventories	-	106,041	-	-	-	106,041
Fund Balances - December 31	<u>\$ 3,372,268</u>	<u>\$ 2,562,298</u>	<u>\$ -</u>	<u>\$ 287,941</u>	<u>\$ 267,293</u>	<u>\$ 6,489,800</u>

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

EXHIBIT 6

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND
CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE
GOVERNMENT-WIDE STATEMENT OF ACTIVITIES--GOVERNMENTAL ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2006**

Net change in fund balances - total governmental funds (Exhibit 5) **\$ (251,429)**

Amounts reported for governmental activities in the statement of activities are different because:

In the funds, under the modified accrual basis, receivables not available for expenditure are deferred. In the statement of activities, those revenues are recognized when earned. The adjustment to revenues between the fund statements and the statement of activities is the increase (decrease) in revenues deferred as unavailable.

Deferred revenue - December 31	\$ 2,741,143	
Deferred revenue - January 1	(3,084,344)	(343,201)

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

Expenditures for general capital assets, including infrastructure	\$ 1,912,607	
Current year depreciation	(926,019)	986,588

Repayment of debt principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets.

Principal repayments		
General obligation bonds	\$ 1,832,000	
Loans payable	83,262	
Capital leases	14,566	1,929,828

Debt issuance proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the statement of net assets. The net proceeds for debt issuance are:

Septic/ISTS loans		(292,878)
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Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.

Change in accrued interest payable	\$ 42,962	
Amortization of discounts and deferred issuance charges	(3,570)	
Change in compensated absences	(15,795)	
Change in inventories	106,041	129,638

Change in Net Assets of Governmental Activities (Exhibit 2) **\$ 2,158,546**

FIDUCIARY FUNDS

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LINCOLN COUNTY
IVANHOE, MINNESOTA

EXHIBIT 7

STATEMENT OF FIDUCIARY NET ASSETS
AGENCY FUNDS
DECEMBER 31, 2006

Assets

Cash and pooled investments	<u>\$ 57,134</u>
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Liabilities

Due to other governments	<u>\$ 57,134</u>
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**LINCOLN COUNTY
IVANHOE, MINNESOTA**

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

1. Summary of Significant Accounting Policies

Lincoln County’s financial statements are prepared in accordance with generally accepted accounting principles (GAAP) as of and for the year ended December 31, 2006. The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (statements and interpretations). Governments are also required to follow the pronouncements of the Financial Accounting Standards Board issued through November 30, 1989, (when applicable) that do not conflict with or contradict GASB pronouncements. More significant accounting policies established in GAAP and used by the County are discussed below.

A. Financial Reporting Entity

Lincoln County was established March 6, 1873, and is an organized county having the powers, duties, and privileges granted counties by Minn. Stat. ch. 373. As required by accounting principles generally accepted in the United States of America, these financial statements present Lincoln County (primary government) and its component unit. The County is governed by a five-member Board of Commissioners elected from districts within the County. The Board is organized with a chair and vice chair elected at the annual meeting in January of each year. The County Auditor, elected on a County-wide basis, serves as the clerk of the Board of Commissioners, but has no vote.

Discretely Presented Component Unit

While part of the reporting entity, the discretely presented component unit is presented in a separate column in the government-wide financial statements to emphasize that it is legally separate from the County. Disclosures relating to the discretely presented component unit are reported with those of the primary government. The County’s significant accounting policies are also used by the discretely presented component unit. The following component unit of Lincoln County is discretely presented:

<u>Component Unit</u>	<u>Component Unit Included in Reporting Entity Because</u>	<u>Separate Financial Statements</u>
Lake Benton Lake Improvement District	County is financially accountable for the District as a result of fiscal dependency; the District cannot levy taxes without County Board approval.	Separate financial statements are not prepared.

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

1. Summary of Significant Accounting Policies

A. Financial Reporting Entity (Continued)

The County participates in several joint ventures described in Note 5.C. The County also participates in jointly-governed organizations and a related organization described in Note 5.D. and Note 5.E., respectively.

B. Basic Financial Statements

1. Government-Wide Statements

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

In the government-wide statement of net assets, the governmental activities are presented on a consolidated basis and are reported on a full accrual, economic resource basis, which recognizes all long-term assets and receivables as well as long-term debt and obligations. The County's net assets are reported in three parts: (1) invested in capital assets, net of related debt; (2) restricted net assets; and (3) unrestricted net assets. The County first utilizes restricted resources to finance qualifying activities.

The statement of activities demonstrates the degree to which the direct expenses of each function of the County's governmental activities are offset by program revenues. Direct expenses are those clearly identifiable with a specific function or activity. Program revenues include: (1) fees, fines, and charges paid by the recipients of goods, services, or privileges provided by a given function or activity; and (2) grants and contributions restricted to meeting the operational or capital requirements of a particular function or activity. Revenues not classified as program revenues, including all taxes, are presented as general revenues.

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

1. Summary of Significant Accounting Policies

B. Basic Financial Statements (Continued)

2. Fund Financial Statements

The fund financial statements provide information about the County's funds, including its fiduciary funds. Separate statements for each fund category--governmental and fiduciary--are presented. The emphasis of governmental fund financial statements is on major individual governmental funds, with each displayed as a separate column in the fund financial statements. The County reports all of its governmental funds as major funds.

The County reports the following major governmental funds:

- The General Fund is the County's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.
- The Road and Bridge Special Revenue Fund is used to account for revenues and expenditures of the County Highway Department, which is responsible for the construction and maintenance of roads, bridges, and other projects affecting County roadways.

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

- The Ditch Special Revenue Fund is used to account for the cost of constructing and maintaining an agricultural drainage ditch system. Financing is provided by special assessments levied against benefited property.
- The Jail Facility Debt Service Fund is used to account for the accumulation of resources for, and the payment of, bond principal, interest, and related costs of general obligation bonds.

The County reports no proprietary funds.

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

1. Summary of Significant Accounting Policies

B. Basic Financial Statements

2. Fund Financial Statements (Continued)

Additionally, the County reports the following fund types:

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

C. Measurement Focus and Basis of Accounting

The government-wide and fiduciary fund financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Lincoln County considers all revenues as available if collected within 60 days after the end of the current period. Property and other taxes, licenses, and interest are all considered susceptible to accrual. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on long-term debt, compensated absences, and claims and judgments, which are recognized as expenditures to the extent that they have matured. Proceeds of long-term debt and acquisitions under capital leases are reported as other financing sources.

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

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

1. Summary of Significant Accounting Policies (Continued)

D. Assets, Liabilities, and Net Assets or Equity

1. Deposits and Investments

The cash balances of substantially all funds are pooled and invested by the County Treasurer for the purpose of increasing earnings through investment activities. Pooled and fund investments are reported at fair value at December 31, 2006, based on market prices. Pursuant to Minn. Stat. § 385.07, investment earnings on cash and pooled investments are credited to the General Fund. Other funds received investment earnings based on other state statutes, grant agreements, contracts, and bond covenants. Pooled investment earnings for 2006 were \$226,923.

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

2. Receivables and Payables

Activity between funds representative of lending/borrowing arrangements outstanding at the end of the fiscal year is referred to as either "due to/from other funds" (the current portion of interfund loans) or "advances to/from other funds" (the noncurrent portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds."

Advances between funds, as reported in the fund financial statements, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

All receivables are shown net of an allowance for uncollectibles.

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Assets or Equity

2. Receivables and Payables (Continued)

Property taxes are levied as of January 1 on property values assessed as of the same date. The tax levy notice is mailed in March with the first half payment due May 15 and the second half payment due October 15. Unpaid taxes at December 31 become liens on the respective property and are classified in the financial statements as delinquent taxes receivable.

Special assessments receivable consist of delinquent special assessments and deferred special assessments. All special assessments receivable are shown net of allowance for uncollectibles. No provision has been made for an estimated uncollectible amount.

3. Inventories and Prepaid Items

All inventories are valued at cost using the first in/first out (FIFO) method. Inventories in governmental funds are recorded as expenditures when purchased rather than when consumed. Inventories at the government-wide level are recorded as expenses when consumed.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

4. Capital Assets

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

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

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Assets or Equity

4. Capital Assets (Continued)

Major outlays for capital assets and improvements are capitalized as projects are constructed.

Property, plant, and equipment are depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Buildings	25 - 40
Improvements to land	20 - 35
Public domain infrastructure	15 - 70
Machinery and equipment	3 - 15

5. Compensated Absences

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

6. Deferred Revenue

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

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

1. Summary of Significant Accounting Policies

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

7. Long-Term Obligations

In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of the debt issued is reported as an other financing source. Premiums received on debt issuances are reported as other financing sources, while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

8. Fund Equity

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

9. Use of Estimates

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

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

2. Stewardship, Compliance, and Accountability

A. Deficit Fund Equity

The Lake Benton Lake Improvement District discretely presented component unit had deficit net assets as of December 31, 2006, of \$120,975. The deficit will be eliminated through future tax levies.

B. Excess of Expenditures Over Budget

<u>Fund</u>	<u>Expenditures</u>	<u>Final Budget</u>	<u>Excess</u>
General	\$ 3,761,184	\$ 3,609,368	\$ 151,816
Special Revenue			
Road and Bridge	3,962,924	3,681,300	281,624
Ditch	164,545	84,085	80,460
Jail Facility Debt Service	1,889,085	191,100	1,697,985

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

Reconciliation of the County's total deposits, cash on hand, and investments to the basic financial statements follows:

Government-wide statement of net assets		
Cash and pooled investments		
Primary government	\$ 5,764,065	
Lake Benton Lake Improvement District	17,278	
Agency funds		
Cash and pooled investments	57,134	
Total Cash and Investments	\$ 5,838,477	
Deposits		
Checking	\$ 177,273	
Money market savings	204,036	
Certificates of deposit	683,108	
Invested in MAGIC Fund	1,776,590	
Invested in U.S. government agency securities	1,154,160	
Invested in negotiable certificates of deposit	1,841,520	
Petty cash and change funds	1,790	
Total Deposits, Cash on Hand, and Investments	\$ 5,838,477	

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments (Continued)

a. Deposits

Minn. Stat. §§ 118A.02 and 118A.04 authorize the County to designate a depository for public funds and to invest in certificates of deposit. Minn. Stat. § 118A.03 requires that all County deposits be protected by insurance, surety bond, or collateral. The market value of collateral pledged shall be at least ten percent more than the amount on deposit plus accrued interest at the close of the financial institution's banking day, not covered by insurance or bonds.

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

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a financial institution failure, the County's deposits may not be returned to it. The County does not have a deposit policy for custodial credit risk. As of December 31, 2006, the County's deposits were not exposed to custodial credit risk.

b. Investments

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

- (1) securities which are direct obligations or are guaranteed or insured issues of the United States, its agencies, its instrumentalities, or organizations created by an act of Congress, except mortgage-backed securities defined as "high risk" by Minn. Stat. § 118A.04, subd. 6;

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

b. Investments (Continued)

- (2) mutual funds through shares of registered investment companies provided the mutual fund receives certain ratings depending on its investments;
- (3) general obligations of the State of Minnesota and its municipalities, and in certain state agency and local obligations of Minnesota and other states provided such obligations have certain specified bond ratings by a national bond rating service;
- (4) bankers' acceptances of United States banks;
- (5) commercial paper issued by United States corporations or their Canadian subsidiaries that is rated in the highest quality category by two nationally recognized rating agencies and matures in 270 days or less; and
- (6) with certain restrictions, in repurchase agreements, securities lending agreements, joint powers investment trusts, and guaranteed investment contracts.

Interest Rate Risk

Interest rate risk is the risk that changes in the market interest rates will adversely affect the fair value of an investment. The County's investment policy is to invest in both short-term and long-term investments to limit exposure to interest rate risk.

Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. It is the County's policy to invest only in securities that meet the ratings requirements set by state statute.

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

b. Investments (Continued)

Custodial Credit Risk

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities in the possession of an outside party. The County does not have an investment policy for custodial credit risk. At December 31, 2006, \$824,161 of U.S. government agency securities and \$415,000 of negotiable certificates of deposit held by brokers were subject to custodial credit risk.

Concentration of Credit Risk

The concentration of credit risk is the risk of loss that may be caused by the County's investment in a single issuer. It is the County's policy that U.S. Treasury securities, U.S. agency securities, and obligations backed by U.S. Treasury and/or U.S. agency securities, may be held without limit.

The following table presents the County's cash and investment balances at December 31, 2006, and information relating to potential investment risks:

Investment Type	Credit Risk		Concentration Risk	Interest Rate Risk	Carrying (Fair) Value
	Credit Rating	Rating Agency	Over 5 Percent of Portfolio	Maturity Date	
U.S. government agency securities					
Government National Mortgage Association	N/A	N/A		12/15/2016	\$ 10,945
Federal Home Loan Bank Note	AAA	S&P		11/15/2007	\$ 500,156
Federal Home Loan Bank Note	AAA	S&P		11/09/2007	493,969
Federal Home Loan Bank Note	AAA	S&P		02/09/2007	149,090
Total Federal Home Loan Bank			24.0%		\$ 1,143,215

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments (Continued)

Investment Type	Credit Risk		Concentration	Interest	Carrying (Fair) Value
	Credit Rating	Rating Agency	Over 5 Percent of Portfolio	Rate Risk Maturity Date	
Investment pools/mutual funds					
MAGIC Fund	N/R	N/A	N/A	N/A	\$ 1,776,590
Negotiable certificates of deposit					
Capital One Bank	N/A	N/A		03/06/2007	\$ 100,000
Florida Bank	N/A	N/A		02/27/2007	96,000
Cross Country Bank	N/A	N/A		01/16/2007	95,616
MBNA American Bank	N/A	N/A		02/05/2007	95,904
LaSalle Bank	N/A	N/A		11/02/2007	99,000
LaSalle Bank Midwest	N/A	N/A		12/14/2007	98,000
Howard Bank	N/A	N/A		09/29/2007	99,000
Colorado Bank	N/A	N/A		02/28/2007	99,000
Peoples Bank	N/A	N/A		07/28/2008	99,000
Americas Bank	N/A	N/A		01/10/2007	96,000
Appalachian Community Bank	N/A	N/A		04/27/2007	96,000
Chevy Chase Bank	N/A	N/A		04/27/2007	96,000
First Community Bank - Batesville	N/A	N/A		04/27/2007	96,000
First International Bank	N/A	N/A		01/10/2007	96,000
Flagstar Bank	N/A	N/A		01/10/2007	96,000
FNB - Damariscotta	N/A	N/A		01/10/2007	96,000
Granite Community Bank	N/A	N/A		01/10/2007	96,000
Guard Security Bank	N/A	N/A		04/27/2007	96,000
Imperial Capital Bank	N/A	N/A		04/27/2007	96,000
Total negotiable certificates of deposit			N/A		\$ 1,841,520
Total investments					\$ 4,772,270
Checking					177,273
Money market savings					204,036
Certificates of deposit					683,108
Petty cash					1,790
Total Cash and Investments					\$ 5,838,477

N/A - Not Applicable
N/R - Not Rated
S&P - Standard & Poor's

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets (Continued)

2. Receivables

Receivables as of December 31, 2006, for the County's governmental activities are as follows:

	Total Receivables	Amounts Not Scheduled for Collection During the Subsequent Year
Governmental Activities		
Taxes	\$ 45,790	\$ -
Special assessments	1,195,166	1,032,876
Accounts	84,266	-
Interest	53,813	-
Due from other governments	2,164,204	-
Total Governmental Activities	\$ 3,543,239	\$ 1,032,876

Governmental activities and the General Fund also report a \$140,000 receivable from the Lake Benton Lake Improvement District component unit. None of this receivable is expected to be received within the next year.

3. Capital Assets

Capital asset activity for the year ended December 31, 2006, was as follows:

	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets not depreciated				
Land	\$ 270,699	\$ 62	\$ 1,230	\$ 269,531
Right-of-way	290,793	17,371	-	308,164
Construction in progress	2,240,531	-	2,240,531	-
Total capital assets not depreciated	\$ 2,802,023	\$ 17,433	\$ 2,241,761	\$ 577,695
Capital assets depreciated				
Land improvements	\$ 243,048	\$ 11,892	\$ -	\$ 254,940
Buildings	2,621,524	1,513,074	-	4,134,598
Machinery and equipment	3,232,775	282,042	51,472	3,463,345
Infrastructure	29,793,285	2,329,946	-	32,123,231
Total capital assets depreciated	\$ 35,890,632	\$ 4,136,954	\$ 51,472	\$ 39,976,114

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

3. Capital Assets (Continued)

	<u>Beginning Balance</u>	<u>Increase</u>	<u>Decrease</u>	<u>Ending Balance</u>
Less: accumulated depreciation for				
Land improvements	\$ 88,607	\$ 10,845	\$ -	\$ 99,452
Buildings	726,864	63,714	-	790,578
Machinery and equipment	2,351,426	251,711	51,472	2,551,665
Infrastructure	6,122,938	599,749	-	6,722,687
	<u>\$ 9,289,835</u>	<u>\$ 926,019</u>	<u>\$ 51,472</u>	<u>\$ 10,164,382</u>
Total accumulated depreciation				
Total capital assets depreciated, net	<u>\$ 26,600,797</u>	<u>\$ 3,210,935</u>	<u>\$ -</u>	<u>\$ 29,811,732</u>
Governmental Activities Capital Assets, Net	<u>\$ 29,402,820</u>	<u>\$ 3,228,368</u>	<u>\$ 2,241,761</u>	<u>\$ 30,389,427</u>

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

Governmental Activities	
General government	\$ 32,078
Public safety	93,080
Highways and streets, including depreciation of infrastructure assets	787,704
Culture and recreation	11,650
Conservation of natural resources	1,507
	<u>1,507</u>
Total Depreciation Expense - Governmental Activities	<u>\$ 926,019</u>

B. Interfund Receivables, Payables, and Transfers

Interfund Transfers

Interfund transfers for the year ended December 31, 2006, consisted of the following:

Transfer to Road and Bridge Fund from General Fund	\$ 264,565	Provide funding
Transfer to Ditch Fund from General Fund	<u>7,464</u>	Provide funding
Total Interfund Transfers	<u>\$ 272,029</u>	

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

3. Detailed Notes on All Funds (Continued)

C. Liabilities

1. Payables

Payables at December 31, 2006, were as follows:

	Governmental Activities
Accounts	\$ 82,827
Salaries	88,332
Contracts	118,476
Due to other governments	193,644
Total Payables	\$ 483,279

2. Construction Commitments

The government has active construction projects as of December 31, 2006. The projects include the following:

	Spent-to-Date	Remaining Commitment
Governmental Activities		
Roads and bridges	\$ 1,660,130	\$ 91,706

3. Capital Leases

In 2003, Lincoln County entered into an \$81,520 capital lease arrangement with the Hutchinson Telephone Company to finance the purchase of E-911 equipment. The agreement is to pay \$8,161 (plus tax) for installation and 60 monthly payments of \$1,214 with no specified interest rate.

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities

3. Capital Leases (Continued)

This lease agreement qualifies as a capital lease for accounting purposes and, therefore, has been recorded at the present value of its future minimum lease payments as of the inception date. They consist of the following at December 31, 2006:

<u>Capital Lease</u>	<u>Final Maturity</u>	<u>Installment Amounts</u>	<u>Interest Rate (%)</u>	<u>Original Issue Amount</u>	<u>Outstanding Balance December 31, 2006</u>
E-911 equipment	2008	\$ 1,214	None stated	<u>\$ 81,520</u>	<u>\$ 26,704</u>

Payments on the capital lease are made from the General Fund. The future lease obligations and the net present value of these minimum lease payments as of December 31, 2006, were as follows:

<u>Year Ending December 31</u>	<u>Governmental Activities</u>
2007	\$ 14,566
2008	<u>12,138</u>
Total minimum lease payments	\$ 26,704
Less: amount representing interest	<u>-</u>
Present Value of Minimum Lease Payments	<u>\$ 26,704</u>

4. Long-Term Debt

Loans Payable

In 2002, the County agreed to act as loan and project sponsor for a project loan agreement made under the Clean Water Partnership Law with the State of Minnesota through its Pollution Control Agency. The loans are to be interest-free with repayment terms from 5 to 20 years and are used for a variety of groundwater

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities

4. Long-Term Debt

Loans Payable (Continued)

improvement projects. All loans are secured by special assessments placed on the individual parcels requesting repair of a failing system. Loan payments are reported in the General Fund.

<u>Type of Indebtedness</u>	<u>Final Maturity</u>	<u>Installment Amounts</u>	<u>Average Interest Rates (%)</u>	<u>Original Issue Amount</u>	<u>Outstanding Balance December 31, 2006</u>
General obligation bonds					
2004 G.O. Refunding Bonds	2020	\$105,000 - \$160,000	3.00 - 4.45	<u>\$ 1,790,000</u>	\$ 1,790,000
Less: unamortized discount					<u>(27,327)</u>
Total General Obligation Bonds, Net					<u>\$ 1,762,673</u>
Special assessment bonds with government commitment					
1997 G.O. drainage bonds	2007	\$12,000	5.75	<u>\$ 120,000</u>	\$ 12,000
Less: unamortized discount					<u>-</u>
Total Special Assessment Bonds with Government Commitment, Net					<u>\$ 12,000</u>

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities (Continued)

5. Debt Service Requirements

Payments on the special assessment bonds are made in the Ditch Special Revenue Fund. Debt service requirements at December 31, 2006, were as follows:

Year Ending December 31	General Obligation Bonds		Special Assessment Bonds	
	Principal	Interest	Principal	Interest
2007	\$ 105,000	\$ 65,973	\$ 12,000	\$ 345
2008	110,000	62,748	-	-
2009	110,000	59,447	-	-
2010	115,000	55,957	-	-
2011	115,000	52,105	-	-
2012 - 2016	635,000	192,574	-	-
2017 - 2021	600,000	53,682	-	-
Total	<u>\$ 1,790,000</u>	<u>\$ 542,486</u>	<u>\$ 12,000</u>	<u>\$ 345</u>

Year Ending December 31	Loans Payable	
	Principal	Interest
2007	\$ 82,198	\$ 13,878
2008	88,134	13,118
2009	89,906	11,346
2010	91,713	9,539
2011	93,557	7,696
2012 - 2016	309,383	12,658
2017 - 2021	5,125	51
Total	<u>\$ 760,016</u>	<u>\$ 68,286</u>

The loans payable to the Minnesota Pollution Control Agency and the Minnesota Department of Agriculture of \$499,261 do not have fixed amortization schedules at December 31, 2006, and are not included in the table above.

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities (Continued)

6. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2006, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Bonds payable					
Special assessment debt with government commitment	\$ 74,000	\$ -	\$ 62,000	\$ 12,000	\$ 12,000
General obligation bonds	3,560,000	-	1,770,000	1,790,000	105,000
Leases payable	41,251	-	14,547	26,704	14,566
Loans payable	1,049,661	292,878	83,262	1,259,277	96,715
Compensated absences	129,749	15,795	-	145,544	11,231
Long-Term Liabilities	<u>\$ 4,854,661</u>	<u>\$ 308,673</u>	<u>\$ 1,929,809</u>	<u>\$ 3,233,525</u>	<u>\$ 239,512</u>

4. Employee Retirement Systems and Pension Plans

A. Defined Benefit Plans

Plan Description

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

Public Employees Retirement Fund members belong to either the Coordinated Plan or the Basic Plan. Coordinated Plan members are covered by Social Security, and Basic Plan members are not. All new members must participate in the Coordinated Plan. All police officers, firefighters, and peace officers who qualify for membership by statute are covered by the Public Employees Police and Fire Fund. Members who are employed in a county correctional institution and have direct contact with inmates are covered by the Public Employees Correctional Fund.

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

4. Employee Retirement Systems and Pension Plans

A. Defined Benefit Plans

Plan Description (Continued)

The PERA provides retirement benefits as well as disability benefits to members and benefits to survivors upon death of eligible members. Benefits are established by state statute and vest after three years of credited service. The retirement benefits are based on a member's highest average salary for any five successive years of allowable service, age, and years of credit at termination of service.

Two methods are used to compute benefits for Coordinated and Basic Plan members. The retiring member receives the higher of a step-rate benefit accrual formula (Method 1) or a level accrual formula (Method 2). Under Method 1, the annuity accrual rate for a Basic Plan member is 2.2 percent of average salary for each of the first ten years of service and 2.7 percent for each year thereafter. For a Coordinated Plan member, the annuity accrual rate is 1.2 percent of average salary for each of the first ten years and 1.7 percent for each successive year. Under Method 2, the annuity accrual rate is 2.7 percent of average salary for Basic Plan members and 1.7 percent for Coordinated Plan members for each year of service. For Public Employees Police and Fire Fund members, the annuity accrual rate is 3.0 percent of average salary for each year of service. For Public Employees Correctional Fund members, the annuity accrual rate is 1.9 percent of average salary for each year of service.

For all Public Employees Retirement Fund members whose annuity is calculated using Method 1, and for all Public Employees Police and Fire Fund and Public Employees Correctional Fund members, a full annuity is available when age plus years of service equal 90. 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.

The PERA issues a publicly available financial report that includes financial statements and required supplementary information for the Public Employees Retirement Fund, the Public Employees Police and Fire Fund, and the Public Employees Correctional Fund.

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

4. Employee Retirement Systems and Pension Plans

A. Defined Benefit Plans

Plan Description (Continued)

That report may be obtained on the internet at www.mnpera.org; by writing to PERA at 60 Empire Drive, Suite 200, Saint Paul, Minnesota 55103-2088; or by calling 651-296-7460 or 1-800-652-9026.

Funding Policy

Pension benefits are funded from member and employer contributions and income from the investment of fund assets. Minn. Stat. ch. 353 sets the rates for employer and employee contributions. These statutes are established and amended by the State Legislature. The County makes annual contributions to the pension plans equal to the amount required by state statutes. Public Employees Retirement Fund Basic Plan members and Coordinated Plan members were required to contribute 9.10 and 5.50 percent, respectively, of their annual covered salary in 2006. Contribution rates in the Coordinated Plan increased in 2007 to 5.75 percent. Public Employees Police and Fire Fund members were required to contribute 7.00 percent of their annual covered salary in 2006. That rate increased to 7.80 percent in 2007. Public Employees Correctional Fund members are required to contribute 5.83 percent of their annual covered salary.

The County is required to contribute the following percentages of annual covered payroll in 2006 and 2007:

	<u>2006</u>	<u>2007</u>
Public Employees Retirement Fund		
Basic Plan members	11.78%	11.78%
Coordinated Plan members	6.00	6.25
Public Employees Police and Fire Fund	10.50	11.70
Public Employees Correctional Fund	8.75	8.75

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

4. Employee Retirement Systems and Pension Plans

A. Defined Benefit Plans

Funding Policy (Continued)

The County's contributions for the years ending December 31, 2006, 2005, and 2004, for the Public Employees Retirement Fund, the Public Employees Police and Fire Fund, and the Public Employees Correctional Fund were:

	Public Employees Retirement Fund	Public Employees Police and Fire Fund	Public Employees Correctional Fund
2006	\$ 100,068	\$ 16,563	\$ 2,909
2005	89,725	14,836	2,632
2004	83,024	13,999	2,824

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

B. Defined Contribution Plan

The Public Employees Defined Contribution Plan is a multiple-employer deferred compensation plan for local government officials, except elected county sheriffs. The plan is established and administered in accordance with Minn. Stat. ch. 353D. The plan is a tax qualified plan under Section 401(a) of the Internal Revenue Code, and all contributions by or on behalf of employees are tax deferred until time of withdrawal.

Plan benefits depend solely on amounts contributed to the plan plus investment earnings, less administrative expenses. Minn. Stat. § 353D.03 specifies the employee and employer contribution rates for those qualified personnel who elect to participate. An eligible elected official who decides to participate contributes five percent of salary, which is matched by the employer.

No vesting period is required to receive benefits in the Defined Contribution Plan. At the time of retirement or termination, the market value of the member's account is distributed to the member or another qualified plan.

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

4. Employee Retirement Systems and Pension Plans

B. Defined Contribution Plan (Continued)

The County's contributions for the years ending December 31, 2006, 2005, and 2004, were \$496, \$0, and \$0, respectively, equal to the contractually required contributions for each year as set by state statute.

5. Summary of Significant Contingencies and Other Items

A. Risk Management

The County and the Lake Benton Lake Improvement District are exposed to various risks of loss related to torts; theft of, damage to, or destruction of assets; errors or omissions; injuries to employees; or natural disasters for which the County carries commercial insurance. The County has entered into a joint powers agreement with other Minnesota counties to form the Minnesota Counties Insurance Trust (MCIT). The County is a member of both the MCIT Workers' Compensation and Property and Casualty Divisions. For other risk, the County carries commercial insurance. There were no significant reductions in insurance from the prior year. The amount of settlements did not exceed insurance coverage for the past three fiscal years.

The Workers' Compensation Division of MCIT is self-sustaining based on the contributions charged, so that total contributions plus compounded earnings on these contributions will equal the amount needed to satisfy claims liabilities and other expenses. MCIT participates in the Workers' Compensation Reinsurance Association with coverage at \$390,000 per claim in 2006 and \$400,000 per claim in 2007. Should the MCIT Workers' Compensation Division liabilities exceed assets, MCIT may assess the County in a method and amount to be determined by MCIT.

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

Premiums are paid by the General Fund, which is reimbursed from other funds for their shares.

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

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

B. Contingent Liabilities

Amounts received or receivable from grant agencies are subject to audit and adjustment by grantor agencies, principally the federal government. Any disallowed claims, including amounts already collected, may constitute a liability of the applicable funds. The amount, if any, of the expenditures that may be disallowed by the grantor cannot be determined at this time, although the County expects such amounts, if any, to be immaterial.

The County is a defendant in various lawsuits. Although the outcome of these lawsuits is not presently determinable, in the opinion of the County Attorney, the resolution of these matters will not have a material adverse effect on the financial condition of the government.

C. Joint Ventures

Lincoln, Lyon, & Murray Human Services

Lincoln, Lyon, & Murray Human Services (LLMHS) was formed pursuant to Minn. Stat. § 393.01, subd. 7, by Lincoln, Lyon, and Murray Counties. The Human Services Board began official operation on July 1, 1974, and performs welfare functions formerly performed by the individual counties. Local financing is provided by the three member counties on the basis of each County's welfare expenditures in 1973:

Lincoln County	20.90%
Lyon County	54.77
Murray County	24.33

LLMHS is governed by two County Commissioners from each of the participating counties, who are chosen by their respective County Boards, and one lay person from each participating County. At least one lay Board member is to be a woman. Financing is provided by state grants and appropriations from member counties. Lincoln County's contribution in 2006 was \$831,102.

At December 31, 2006, LLMHS reported a total fund balance of \$3,727,407. In addition, LLMHS reported total net assets of \$3,674,957. LLMHS's long-term debt at December 31, 2006, is composed of \$464,084 of compensated absences payable. The debt will be funded by intergovernmental revenue and revenue from computer services.

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

5. Summary of Significant Contingencies and Other Items

C. Joint Ventures

Lincoln, Lyon, & Murray Human Services (Continued)

Complete financial statements of Lincoln, Lyon, & Murray Human Services can be obtained at 607 West Main, Marshall, Minnesota 56258.

Lincoln, Lyon, Murray, Pipestone Public Health Services

Lincoln County has joined with surrounding counties to form a community health service agency under the authority of Minn. Stat. ch. 145A and Minn. Stat. § 471.59. This agency is known as the Lincoln, Lyon, Murray, Pipestone Public Health Services and was established August 1, 1978. The governing Board is composed of nine members: two Commissioners representing Lincoln County, one Board member from each of the other participating counties, and four lay members. Financing is provided by state grants, appropriations from member counties, and charges for services. Lincoln County's contribution in 2006 was \$36,666.

At December 31, 2005 (the latest information available), the Health Services had retained earnings of \$905,772 and long-term liabilities of \$98,580. Complete financial statements of the Lincoln, Lyon, Murray, Pipestone Public Health Services can be obtained at 607 West Main, Marshall, Minnesota 56258.

Lincoln-Pipestone Rural Water System

Lincoln County, along with Lyon, Murray, Nobles, Pipestone, Rock, and Yellow Medicine Counties, jointly established the Lincoln-Pipestone Rural Water System pursuant to Minn. Stat. ch. 116A. The system is responsible for storing, treating, and distributing water for domestic, commercial, and industrial use within the area it serves. The cost of providing these services is recovered through user charges. The Lincoln-Pipestone Rural Water System is governed by the District Court. The Water System's Board is solely responsible for the budgeting and financing of the Water System.

The Lincoln-Pipestone Rural Water System's 2006 financial report shows total net assets of \$38,147,114, including unrestricted net assets of \$20,545,521. The decrease in net assets for the year ended December 31, 2006, was \$(134,179). Outstanding noncurrent obligations at December 31, 2006, were \$21,957,644.

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

5. Summary of Significant Contingencies and Other Items

C. Joint Ventures

Lincoln-Pipestone Rural Water System (Continued)

Complete financial statements of the Lincoln-Pipestone Rural Water System can be obtained at East Highway 14, P. O. Box 188, Lake Benton, Minnesota 56149-0188.

D. Jointly-Governed Organizations

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

- Minnesota River Basin provides programs for flood reduction measures to the area between the Cities of Ortonville and Mankato. During the year, the County did not contribute to the project.
- The County Board is responsible for appointing two members of the Board of Managers for the Yellow Medicine River Watershed District, but the County's responsibility does not extend beyond making the appointments.
- The County Board is responsible for appointing two members of the Board of Managers for the Lac qui Parle-Yellow Bank Watershed District, but the County's responsibility does not extend beyond making the appointments.

E. Related Organization

Housing and Redevelopment Authority of Lincoln County

The five-member governing body of the Housing and Redevelopment Authority of Lincoln County is appointed by Lincoln County. Lincoln County is not financially responsible for the Authority. During 2006, there were no related-party transactions between Lincoln County and the Housing and Redevelopment Authority of Lincoln County.

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

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

F. Agriculture Best Management Loan Program

The County has entered into an agreement with the Minnesota Department of Agriculture and local lending institutions to jointly administer a loan program to individuals to implement projects that prevent or mitigate non-point source water pollution. While the County is not liable for repayment of the loans in any manner, it does have certain responsibilities under the agreement.

6. Component Unit Disclosures

A. Summary of Significant Accounting Policies

In addition to those policies identified in Note 1, the Lake Benton Lake Improvement District component unit has the following significant accounting policies.

Reporting Entity

The Lake Benton Lake Improvement District is governed by a seven-member elected board, with the first members appointed to staggered terms. The District was established to provide a means for property owners to meet and deal with specific needs relating to lake quality and lake management, including control of curly leaf pondweed.

The District is considered a component unit of Lincoln County because it cannot levy property taxes without approval of the County Board. The County acts as the fiscal agent for the District.

Basis of Presentation and Basis of Accounting

The District does not issue separate financial statements. It accounts for its funds on the modified accrual basis of accounting.

Cash and Pooled Investments

All cash of the District is on deposit with Lincoln County and included in pooled cash and investments. Disclosures included in Note 3.A.1. apply to the District as well as to the County.

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

6. Component Unit Disclosures (Continued)

B. Detailed Notes

Receivables

Receivables at December 31, 2006, for the Lake Benton Lake Improvement District are as follows:

Taxes	\$ 1,349
Special assessments	<u>398</u>
Total	<u>\$ 1,747</u>

All receivables are expected to be collected within the next year.

Liabilities

The District has a long-term loan from Lincoln County. It was received in two stages, carries an interest rate of four percent, and is to be repaid over seven years. A payment schedule has been agreed on. Payments are to be made from the General Fund. It is carried as Due to Primary Government on the balance sheet for December 31, 2006.

Changes in the loan during 2006 were as follows:

Balance, January 1	\$ 140,000
Additional loan received	<u>-</u>
Balance, December 31	<u>\$ 140,000</u>

Subsequent Event

In 2007, Lincoln County loaned the District an additional \$60,000, for a total of \$200,000. A payment schedule has been agreed upon for the total loan amount. Payments are to be made, including four percent interest, from 2007 through 2014.

Risk Management

See Note 5.A. for the District's risk management.

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REQUIRED SUPPLEMENTARY INFORMATION

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**LINCOLN COUNTY
IVANHOE, MINNESOTA**

Schedule 1

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2006**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Revenues				
Taxes	\$ 1,562,324	\$ 1,554,159	\$ 1,478,878	\$ (75,281)
Special assessments	-	-	175,680	175,680
Licenses and permits	28,350	28,350	23,355	(4,995)
Intergovernmental	954,899	948,299	1,560,650	612,351
Charges for services	219,080	218,580	303,249	84,669
Fines and forfeits	8,000	8,000	6,271	(1,729)
Gifts and contributions	-	-	1,813	1,813
Investment earnings	110,500	110,500	225,851	115,351
Miscellaneous	534,628	409,628	278,530	(131,098)
Total Revenues	\$ 3,417,781	\$ 3,277,516	\$ 4,054,277	\$ 776,761
Expenditures				
Current				
General government				
Commissioners	\$ 126,450	\$ 126,350	\$ 121,418	\$ 4,932
Courts	7,100	9,600	9,866	(266)
Law library	9,368	9,568	8,187	1,381
County administration	148,750	270,537	130,979	139,558
Auditor	195,975	195,975	188,357	7,618
Treasurer	101,864	101,864	101,746	118
Assessor	100,400	100,400	99,561	839
Elections	210,000	210,000	147,113	62,887
Data processing	66,200	66,200	62,302	3,898
Attorney	99,391	99,571	99,523	48
Recorder	185,007	190,108	192,090	(1,982)
Buildings and plant	189,825	203,225	195,014	8,211
Veterans service officer	18,216	18,216	17,291	925
Transportation	180,729	180,729	256,704	(75,975)
Safety officer	12,240	12,240	10,059	2,181
Other general government	(16,307)	15,693	10,181	5,512
Total general government	\$ 1,635,208	\$ 1,810,276	\$ 1,650,391	\$ 159,885
Public safety				
Sheriff	\$ 845,081	\$ 844,581	\$ 741,635	\$ 102,946
Boat and water safety	9,200	9,200	2,913	6,287
Coroner	3,000	3,000	2,136	864
E-911 system	70,500	70,500	9,211	61,289
Rural addressing	5,000	4,575	2,841	1,734
Probation and parole	26,000	26,000	33,420	(7,420)
Civil defense	22,185	22,185	37,752	(15,567)
Total public safety	\$ 980,966	\$ 980,041	\$ 829,908	\$ 150,133
Sanitation				
Solid waste	\$ 67,500	\$ 67,500	\$ 110,956	\$ (43,456)

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

Schedule 1
(Continued)

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2006**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Expenditures				
Current (Continued)				
Health				
Nursing service	\$ 421	\$ 421	\$ 421	\$ -
Culture and recreation				
Historical society	\$ 8,000	\$ 8,000	\$ 8,000	\$ -
Minnesota trails	18,000	26,640	25,517	1,123
Parks	120,992	130,992	129,820	1,172
Library	31,288	31,288	31,288	-
Other	600	600	600	-
Total culture and recreation	\$ 178,880	\$ 197,520	\$ 195,225	\$ 2,295
Conservation of natural resources				
Extension	\$ 105,000	\$ 105,000	\$ 101,989	\$ 3,011
Water quality loan program	-	-	293,875	(293,875)
ISTS projects	14,700	14,700	17,109	(2,409)
Geographic information	65,610	65,660	100,727	(35,067)
Water planning	22,035	22,035	28,264	(6,229)
Environmental officer	122,720	122,670	102,564	20,106
Wetland challenge	10,000	10,000	10,000	-
Other	117,845	117,845	117,845	-
Total conservation of natural resources	\$ 457,910	\$ 457,910	\$ 772,373	\$ (314,463)
Economic development				
Community development	\$ 45,000	\$ 45,000	\$ 40,000	\$ 5,000
Tourism	8,221	7,054	7,209	(155)
Other	5,430	5,430	5,726	(296)
Total economic development	\$ 58,651	\$ 57,484	\$ 52,935	\$ 4,549
Intergovernmental				
Health	\$ 38,245	\$ 38,216	\$ 36,666	\$ 1,550
Debt service				
Principal	\$ -	\$ -	\$ 97,828	\$ (97,828)
Interest	-	-	14,481	(14,481)
Total debt service	\$ -	\$ -	\$ 112,309	\$ (112,309)
Total Expenditures	\$ 3,417,781	\$ 3,609,368	\$ 3,761,184	\$ (151,816)
Excess of Revenues Over (Under) Expenditures	\$ -	\$ (331,852)	\$ 293,093	\$ 624,945

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

Schedule 1
(Continued)

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2006**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Other Financing Sources (Uses)				
Transfers out	\$ -	\$ (250,000)	\$ (272,029)	\$ (22,029)
Loans issued	-	-	290,298	290,298
Proceeds from sale of assets	-	-	34,000	34,000
Total Other Financing Sources (Uses)	<u>\$ -</u>	<u>\$ (250,000)</u>	<u>\$ 52,269</u>	<u>\$ 302,269</u>
Net Change in Fund Balance	<u>\$ -</u>	<u>\$ (581,852)</u>	<u>\$ 345,362</u>	<u>\$ 927,214</u>
Fund Balance - January 1	<u>3,026,906</u>	<u>3,026,906</u>	<u>3,026,906</u>	<u>-</u>
Fund Balance - December 31	<u>\$ 3,026,906</u>	<u>\$ 2,445,054</u>	<u>\$ 3,372,268</u>	<u>\$ 927,214</u>

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

Schedule 2

**BUDGETARY COMPARISON SCHEDULE
ROAD AND BRIDGE SPECIAL REVENUE FUND
FOR THE YEAR ENDED DECEMBER 31, 2006**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Revenues				
Taxes	\$ 960,350	\$ 960,350	\$ 826,005	\$ (134,345)
Licenses and permits	6,000	6,000	4,125	(1,875)
Intergovernmental	2,641,400	2,641,400	3,811,334	1,169,934
Charges for services	60,500	60,500	205,713	145,213
Interest on investments	1,100	1,100	-	(1,100)
Miscellaneous	11,950	11,950	29,716	17,766
Total Revenues	\$ 3,681,300	\$ 3,681,300	\$ 4,876,893	\$ 1,195,593
Expenditures				
Current				
Highways and streets				
Administration	\$ 369,385	\$ 369,385	\$ 292,344	\$ 77,041
Maintenance	925,491	925,491	792,617	132,874
Construction	1,777,414	1,777,414	1,979,525	(202,111)
Equipment and maintenance shops	609,010	609,010	701,579	(92,569)
Total highways and streets	\$ 3,681,300	\$ 3,681,300	\$ 3,766,065	\$ (84,765)
Intergovernmental				
Highways and streets	-	-	196,859	(196,859)
Total Expenditures	\$ 3,681,300	\$ 3,681,300	\$ 3,962,924	\$ (281,624)
Excess of Revenues Over (Under) Expenditures	\$ -	\$ -	\$ 913,969	\$ 913,969
Other Financing Sources (Uses)				
Transfers in	-	-	264,565	264,565
Net Change in Fund Balance	\$ -	\$ -	\$ 1,178,534	\$ 1,178,534
Fund Balance - January 1	1,277,723	1,277,723	1,277,723	-
Increase (decrease) in reserved for inventories	-	-	106,041	106,041
Fund Balance - December 31	\$ 1,277,723	\$ 1,277,723	\$ 2,562,298	\$ 1,284,575

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

Schedule 3

**BUDGETARY COMPARISON SCHEDULE
HUMAN SERVICES SPECIAL REVENUE FUND
FOR THE YEAR ENDED DECEMBER 31, 2006**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Revenues				
Taxes	\$ 833,516	\$ 833,516	\$ 723,572	\$ (109,944)
Intergovernmental	-	-	108,530	108,530
Total Revenues	\$ 833,516	\$ 833,516	\$ 832,102	\$ (1,414)
Expenditures				
Intergovernmental				
Human services	833,516	833,516	832,102	1,414
Net Change in Fund Balance	\$ -	\$ -	\$ -	\$ -
Fund Balance - January 1	-	-	-	-
Fund Balance - December 31	\$ -	\$ -	\$ -	\$ -

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

Schedule 4

**BUDGETARY COMPARISON SCHEDULE
DITCH SPECIAL REVENUE FUND
FOR THE YEAR ENDED DECEMBER 31, 2006**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Revenues				
Special assessments	\$ 37,000	\$ 37,000	\$ 57,684	\$ 20,684
Charges for services	23,385	23,385	-	(23,385)
Miscellaneous	-	-	2,745	2,745
Total Revenues	\$ 60,385	\$ 60,385	\$ 60,429	\$ 44
Expenditures				
Current				
Conservation of natural resources				
Other	-	20,000	100,460	(80,460)
Debt service				
Principal	62,000	62,000	62,000	-
Interest	2,085	2,085	2,085	-
Total Expenditures	\$ 64,085	\$ 84,085	\$ 164,545	\$ (80,460)
Excess of Revenues Over (Under) Expenditures	\$ (3,700)	\$ (23,700)	\$ (104,116)	\$ (80,416)
Other Financing Sources (Uses)				
Transfers in	3,700	3,700	7,464	3,764
Net Change in Fund Balance	\$ -	\$ (20,000)	\$ (96,652)	\$ (76,652)
Fund Balance - January 1	384,593	384,593	384,593	-
Fund Balance - December 31	\$ 384,593	\$ 364,593	\$ 287,941	\$ (76,652)

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

**NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION
FOR THE YEAR ENDED DECEMBER 31, 2006**

1. General Budget Policies

The County Board adopts estimated revenue and expenditure budgets for the General Fund and the special revenue funds. The expenditure budget is approved at the fund level.

The budgets may be amended or modified at any time by the County Board. In 2006, the County Board amended the following fund expenditure budgets as follows:

	Original Budget	Increase (Decrease)	Final Budget
General Fund	\$ 3,417,781	\$ 191,587	\$ 3,609,368
Ditch Special Revenue Fund	64,085	20,000	84,085

2. Budget Basis of Accounting

Budgets for the General Fund and the special revenue funds are adopted on a basis consistent with generally accepted accounting principles.

3. Excess of Expenditures Over Budget

Fund	Expenditures	Final Budget	Excess
General	\$ 3,761,184	\$ 3,609,368	\$ 151,816
Special Revenue			
Road and Bridge	3,962,924	3,681,300	281,624
Ditch	164,545	84,085	80,460

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SUPPLEMENTARY INFORMATION

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**LINCOLN COUNTY
IVANHOE, MINNESOTA**

Schedule 5

**BUDGETARY COMPARISON SCHEDULE
JAIL FACILITY DEBT SERVICE FUND
FOR THE YEAR ENDED DECEMBER 31, 2006**

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Revenues				
Taxes	\$ 191,100	\$ 191,100	\$ 165,874	\$ (25,226)
Intergovernmental	-	-	24,856	24,856
Investment earnings	-	-	19,682	19,682
Total Revenues	\$ 191,100	\$ 191,100	\$ 210,412	\$ 19,312
Expenditures				
Debt service				
Principal	\$ 80,000	\$ 80,000	\$ 1,770,000	\$ (1,690,000)
Interest	99,188	99,188	118,271	(19,083)
Administrative (fiscal) fees	11,912	11,912	814	11,098
Total Expenditures	\$ 191,100	\$ 191,100	\$ 1,889,085	\$ (1,697,985)
Net Change in Fund Balance	\$ -	\$ -	\$ (1,678,673)	\$ (1,678,673)
Fund Balance - January 1	1,945,966	1,945,966	1,945,966	-
Fund Balance - December 31	\$ 1,945,966	\$ 1,945,966	\$ 267,293	\$ (1,678,673)

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

Statement 1

**COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES
ALL AGENCY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2006**

	Balance January 1	Additions	Deductions	Balance December 31
<u>SOUTHWEST REGIONAL SOLID WASTE COMMISSION</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 2,862	\$ 2,422	\$ -	\$ 5,284
<u>Liabilities</u>				
Due to other governments	\$ 2,862	\$ 2,422	\$ -	\$ 5,284
 <u>TAXES AND PENALTIES</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 174,113	\$ 8,879,296	\$ 9,001,559	\$ 51,850
<u>Liabilities</u>				
Due to other governments	\$ 174,113	\$ 8,879,296	\$ 9,001,559	\$ 51,850
 <u>TOTAL ALL AGENCY FUNDS</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 176,975	\$ 8,881,718	\$ 9,001,559	\$ 57,134
<u>Liabilities</u>				
Due to other governments	\$ 176,975	\$ 8,881,718	\$ 9,001,559	\$ 57,134

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

Statement 2

**LAKE BENTON LAKE IMPROVEMENT DISTRICT
GENERAL FUND BALANCE SHEET AND STATEMENT OF NET ASSETS
WITH ADJUSTMENTS TO CONVERT MODIFIED TO FULL ACCRUAL
DECEMBER 31, 2006**

	General Fund	Adjustments	Statement of Net Assets
Assets			
Cash and pooled investments	\$ 17,278	\$ -	\$ 17,278
Taxes receivable			
Prior	1,349	-	1,349
Special assessments receivable			
Prior	398	-	398
Total Assets	\$ 19,025	\$ -	\$ 19,025
Liabilities			
Deferred revenue - unavailable	\$ 647	\$ (647)	\$ -
Due to primary government			
Due in more than one year	-	140,000	140,000
Total Liabilities	\$ 647	\$ 139,353	\$ 140,000
Fund Balances			
Unreserved			
Undesignated	18,378	\$ (18,378)	
Total Liabilities and Fund Balances	\$ 19,025		
Net Assets			
Unrestricted		\$ (120,975)	\$ (120,975)
Total Net Assets		\$ (120,975)	\$ (120,975)

Fund balance - total governmental fund **\$ 18,378**

Amounts reported for governmental activities in the statement of net assets are different because:

Other long-term assets are not available to pay for current period expenditures and, therefore, are deferred in the governmental funds. 647

Long-term liabilities are not due and payable in the current period and, therefore, are not reported in the governmental funds.

Advance from primary government (140,000)

Net Assets of Governmental Activities **\$ (120,975)**

**LINCOLN COUNTY
IVANHOE, MINNESOTA**

Statement 3

**LAKE BENTON LAKE IMPROVEMENT DISTRICT
GENERAL FUND STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCE AND STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2006**

	General Fund	Adjustments	Statement of Activities
Revenues			
Taxes	\$ 22,259	\$ (64)	\$ 22,195
Special assessments	6,260	(270)	5,990
Intergovernmental	47,500	-	47,500
Miscellaneous	2,359	-	2,359
	\$ 78,378	\$ (334)	\$ 78,044
Expenditures/Expenses			
Current			
Conservation of natural resources	134,848	-	134,848
	\$ (56,470)	\$ (334)	\$ (56,804)
Change in Fund Balance/ Net Assets			
Fund Balance/Net Assets - January 1	74,848	(139,019)	(64,171)
Fund Balance/Net Assets - December 31	\$ 18,378	\$ (139,353)	\$ (120,975)
Net change in fund balance - total governmental funds			\$ (56,470)
Amounts reported for governmental activities in the statement of activities are different because:			
In the funds, under the modified accrual basis, receivables not available for expenditures are deferred. In the statement of activities, those revenues are recognized when earned. The adjustment to revenues is the increase (decrease) in amounts of unavailable deferred revenues.			
Deferred revenue - December 31		\$ 647	
Deferred revenue - January 1		(981)	(334)
Change in Net Assets of Governmental Activities			\$ (56,804)

OTHER SCHEDULE

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**LINCOLN COUNTY
IVANHOE, MINNESOTA**

Schedule 6

**SCHEDULE OF INTERGOVERNMENTAL REVENUE
FOR THE YEAR ENDED DECEMBER 31, 2006**

	Primary Government	Component Unit
Shared Revenue		
State		
Highway users tax	\$ 3,626,897	\$ -
County program aid	606,013	-
PERA rate reimbursement	9,428	-
Disparity reduction aid	35,915	-
Police aid	14,836	-
Enhanced 911	77,181	-
Market value credit	381,547	-
	\$ 4,751,817	\$ -
Payments		
Local		
Payments in lieu of taxes	\$ 66,404	\$ -
Local grants	-	17,500
	\$ 66,404	\$ 17,500
Grants		
State		
Minnesota Department of Corrections	\$ 6,955	\$ -
Natural Resources	32,820	30,000
Transportation	86,858	-
Water and Soil Resources Board	192,203	-
Peace Officer Standards and Training Board	1,447	-
Pollution Control Agency	64,676	-
	\$ 384,959	\$ 30,000
Federal		
Department of Transportation	\$ 128,648	\$ -
Homeland Security	32,354	-
Election Assistance Commission	141,188	-
	\$ 302,190	\$ -
Total state and federal grants	\$ 687,149	\$ 30,000
Total Intergovernmental Revenue	\$ 5,505,370	\$ 47,500

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**LINCOLN COUNTY
IVANHOE, MINNESOTA**

Schedule 7

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

98-1 Departmental Internal Accounting Controls

Due to the limited number of office personnel within the various Lincoln County departments, proper segregation of the accounting functions necessary to ensure adequate internal accounting control is not possible. Although this is not unusual in small departmental situations, 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 internal control point of view.

We recommend that County management be aware of the lack of segregation of the accounting functions and, if possible, implement oversight procedures to ensure that the internal control policies and procedures are being implemented by staff.

Client's Response:

The County Board has been advised and is well aware of the lack of segregation of the accounting functions. All reasonable management procedures are in place with the number of employees Lincoln County currently has.

00-3 Budgeting Procedures

Although the County adopts a formal budget, expenditure estimates and the annual budget appropriations to the various operational funds within the County are not always clear. The County adopts the budget in summary form.

The Board-approved budget does not agree with the Revenue and Expenditure Budget Report on the County's general ledger system. The General Fund budget was different by \$310,204, which caused the required supplementary information budgetary comparison schedules in the financial report to be materially misstated. Some budget amendments were approved on January 16, 2007, but other changes to the budget were not approved.

Generally accepted accounting principles and the County Financial Accounting and Reporting Standards recommend that expenditure estimates and the annual budget be appropriated to the various operational entities within the County and that line-item budget detail by fund be available. The appropriations constitute maximum expenditure authorizations during the fiscal year and cannot legally be exceeded unless subsequently amended by the County Board. Good budget accounting requires: (1) an annual budget be adopted by every governmental unit; (2) the accounting system provide the basis for appropriate budgetary control; and (3) a common terminology and classification that can be used consistently throughout the budgets, accounts, and financial reports of each fund. The County Board should adopt an accurate budget, and it should be followed by the County. The adopted budget should be designed so that comparisons can be made between current year and budget year. Any amendments to the budget should be Board approved and documented in the Board minutes.

We recommend that the County implement procedures to improve its budgetary accounting by including in the County Board minutes the amounts approved for each fund's revenue and expenditure budget. We also recommend that any changes to the original budget be approved by formal Board resolution and be so documented.

Client's Response:

The County will continue to improve its budgetary accounting by including in the County Board minutes the amounts approved for each fund's revenue and expenditure budget, and changes to the original budget approved by formal Board resolution.

04-2 Untimely Transaction Recording

Personnel in the County Auditor's Office were late in recording various transactions in the general ledger. Interest income earned on the Minnesota Association of Governments Investing for Counties (MAGIC) account for January through November was not receipted until December 26, 2006, and interest on the main checking account for the period July through December 2006 was not receipted until January 12, 2007.

We recommend that all transactions be recorded in a timely manner.

Client's Response:

Interest income earned on the MAGIC account will be recorded on a monthly basis, and interest on the main checking account will also be receipted on a monthly basis.

05-1 Financial Reporting

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

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

The County's accounting system has been upgraded to accommodate the modified accrual and full accrual bases of accounting in separate general ledger systems to allow for the preparation of the annual financial statements in accordance with generally accepted accounting principles for governments. During our audit, we noted several deficiencies that prevented the accounting system from providing accurate modified and full accrual financial statements. These deficiencies resulted in additional audit time because significant audit adjustments were required to correct the financial statements prepared by the County.

Although Lincoln County has identified and has been training individuals to obtain the expertise to improve its preparation of financial statements, we recommend the County continue to obtain the training and expertise to internally prepare its annual financial statements in accordance with GAAP, including preparing and reporting appropriate government-wide and fund financial statements and including the related notes to the financial statements. Also, this process should be monitored by a knowledgeable person to ensure that the accounts are correctly summarized for financial statement purposes. As part of the financial statement preparation, summary schedules and worksheets should be prepared by County staff to document the various accrual adjusting journal entries and to

demonstrate how the accounts in the financial records are classified or summarized for the annual financial statements. When the financial statements are completed by the accounting system, County staff should review the statements to ensure that reported amounts can be traced back to the prepared supporting schedules and worksheets.

Client's Response:

The County will continue to seek training and expertise, when and where possible, to prepare its financial statements.

ITEMS ARISING THIS YEAR

06-1 Antifraud Programs and Controls

Responses of management and staff regarding the risks of fraud and how Lincoln County responds to those risks indicate deficiencies in antifraud programs and controls.

The Committee of Sponsoring Organizations (COSO) of the Treadway Commission's Internal Control - Integrated Framework specifies five components of an effective antifraud program: (1) performing fraud risk assessments, (2) creating a control environment, (3) designing and implementing antifraud control activities, (4) sharing information and communication, and (5) monitoring activities.

The County should communicate its philosophy on antifraud programs and controls throughout the organization. This should help ensure that employees understand the antifraud activities in place, know what is expected of them, and realize the organization takes fraud risks and prevention very seriously. All levels of the organization should have involvement in these communications and, if appropriate, communications should also be made to external parties (including clients, suppliers, and agents).

We recommend the County improve internal controls over antifraud programs and controls. The controls should address all five components of an effective antifraud program according to the COSO framework. We encourage Lincoln County to not only obtain the training and expertise to implement a program that prevents, deters, and detects fraud, but also to monitor and test the controls in place to evaluate whether the controls are operating effectively and in the intended manner.

Client's Response:

The County will seek antifraud training for employees when and where possible.

06-2 Computer Risk Management

The County has internal controls in place for its computer system. However, the County has not developed a formal plan to identify and manage risks associated with its computer system, tested its disaster recovery plan, required strong passwords, or limited the number of computers a user can be logged onto concurrently.

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

We recommend the County Board direct management to develop a plan to ensure that internal controls are in place to reduce the risk associated with the County's computer systems. These controls over the computer system are necessary to maintain proper controls over financial reporting. The controls implemented should include requiring strong passwords and setting a limit to the number of computers a user can be logged onto at any time. We also recommend the County update and test its disaster recovery plan.

Client's Response:

The County will work on a plan to improve internal control over its computer system.

06-3 Adding New Vendors to the Accounting System

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

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

Also, when invoices are submitted for vendors that have not previously done business with the County, some procedures should be required to verify whether the vendor is legitimate. Procedures could include looking up the vendor in the phone book or on the internet or requiring the company to send information about their business. Periodically, the vendor listing should be reviewed for old, unused vendors, and those vendors should be removed from the system.

Client's Response:

The County will work on a written policy. New vendor information will be printed out on a periodic basis and will be reviewed by appropriate personnel.

06-4 Audit Adjustments

A control deficiency exists when the design or operation of a control does not allow management or employees in the normal course of performing their assigned functions to prevent or detect misstatements of the financial statements on a timely basis. Two control deficiencies that typically are considered significant are restatement of previously issued financial statements to reflect the correction of a material misstatement or identification by the auditor of a material misstatement in the financial statements that was not initially identified by the entity's internal controls.

During our audit, we made adjustments that resulted in significant changes to the County's financial statements. The adjustments resulted from: County staff needing continued guidance on accounting principles and oversight to provide accurate and reliable information; accounting staff not keeping current on new accounting and reporting requirements; errors made in recording transactions and with mapping of various account codes; control over calculating the proper amounts of assets and liabilities that did not detect a number of errors, resulting in the client's records understating assets, liabilities, revenues, and expenditures and the County not considering the need for controls over the recording of certain accounting transactions. The inability to detect material misstatements in the financial statements increases the likelihood that the financial statements may not be fairly presented.

We recommend that the County review internal controls currently in place, then design and implement procedures to improve internal controls over financial reporting to detect misstatements in the financial statements. The updated controls should include review of the balances and supporting documentation by a qualified individual to identify potential misstatements.

Client's Response:

The County will work toward compliance.

06-5 Capital Assets Policies and Procedures

The County's current capital assets policy defines the County's accounting policies over capital assets, such as capitalization thresholds, useful lives, and depreciation methods; however, the policy does not address redetermination of the useful lives of the capital assets, nor when redetermination of the capital assets will take place. Also, it is not clear how the costs of replaced infrastructure assets are being deleted, if at all.

The County is carrying a significant amount of fully depreciated assets. Typically, a capital asset still in use should not be considered fully depreciated. For significant assets, the estimated useful lives assigned to capital assets should be reconsidered. At the time of redetermination, the estimated useful life of an asset includes both the years the asset has been in service and the estimated number of years of service remaining.

We recommend the County Board address these issues in the capital assets policy. The policy should establish procedures to address the point when useful lives of current capital assets should be reconsidered.

Client's Response:

The County will begin working on a written Fixed Asset Policy.

06-6 Controls Over the Accounting System Journal Entry Function

The County does not limit access to the accounting system journal entry function to select County employees. Thirteen user names on the system have access to this function. Not all journal entries made to the accounting system are reviewed or approved.

The ability to make journal entries on the accounting system is a powerful function because it allows those employees to make changes to the system. To prevent abuse of this function, access should be limited to those employees whose job duties require them to have this access.

We recommend the County strengthen the controls over the journal entries by reevaluating who has access to the journal entry function and determine whether there is a logical need for those employees to have access to this function. We also recommend a

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

Client's Response:

The County will work toward compliance.

06-7 Accounting Policies and Procedures Manual

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

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

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

Client's Response:

The County has already begun the process of establishing an Accounting Policies and Procedures manual.

II. OTHER FINDINGS AND RECOMMENDATIONS

A. MINNESOTA LEGAL COMPLIANCE

PREVIOUSLY REPORTED ITEMS RESOLVED

Certificates of Deposit (02-2)

The County purchased a \$100,000 certificate of deposit from Capital One Bank through Wachovia Securities. Federal deposit insurance provides protection to depositors up to \$100,000 for each bank. This leaves any earned interest not yet paid to the County uninsured.

Resolution

The County is in compliance with Minn. Stat. § 118A.04.

Depository Pledge Agreement (05-2)

The depository pledge agreement between the County and Bank of the West states that the County is required to give notice of a failure, insolvency, or breach to the bank and wait at least three business days after the notice before the County can collect the collateral from the Custodian so the bank has time to cure the default.

Resolution

The County has a security agreement that is consistent with the default language of Minn. Stat. § 118A.03, subd. 4, and that has the required language included.

Undistributed Collections in Taxes and Penalties Agency Fund (05-3)

At December 31, 2005, undistributed collections in the Taxes and Penalties Agency Fund were \$14,195. The County Auditor could not explain the unreconciled variance as of December 13, 2006. Also, the December settlement was not paid until January 27, 2006, two days after the legal requirement, putting the County in violation of Minn. Stat. § 276.111.

Resolution

The undistributed collections were distributed in 2006, and the County complies with the provisions of Minn. Stat. § 276.111.

B. MANAGEMENT PRACTICES

ITEM ARISING THIS YEAR

06-8 Board Minute Omissions

During our audit, we noted that the Board minutes are not always complete. The County Board minutes from December 20, 2005, note that an insert for the adopted 2006 budget was to be placed in the file with the Board minutes. The County Auditor did not include the detail for the approved budget with the official minutes and is unable to present line-item detail of the County's 2006 budget before it was amended during 2006.

To ensure compliance with Minnesota statutes regarding budgeting, contracting, disbursements, and other areas, a complete and detailed record of County Board meetings should be maintained.

Client's Response:

The Budget was approved December 20, 2005, by the Board of Commissioners, but was inadvertently left out of the minutes. The Budget and Departmental budgets have been added to the December 2005 minutes.

PREVIOUSLY REPORTED ITEM RESOLVED

Improper Accounting (05-4)

Lincoln County serves as fiscal agent for the Solid Waste Task Force, a jointly-governed organization, and the Lake Benton Lake Improvement District, a component unit of the County. The County accounted for these organizations in departments within the General Fund.

Resolution

The County established and uses agency fund accounting to account for these organizations.

C. OTHER ITEM FOR CONSIDERATION

Other Postemployment Benefits (OPEB)

The Governmental Accounting Standards Board (GASB) recently issued Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which establishes financial reporting for OPEB plans; and Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, which governs employer accounting and financial reporting for OPEB. These standards, similar to what GASB Statements 25 and 27 did for government employee pension benefits and plans, provide the accounting and reporting standards for the various other postemployment benefits many local governments offer to their employees. OPEB can include many different benefits offered to retirees such as health, dental, life, and long-term care insurance coverage.

If retirees are included in an insurance plan and pay a rate similar to that paid for younger active employees, this implicit subsidy is considered OPEB. In fact, local governments may be required to continue medical insurance coverage pursuant to Minn. Stat. § 471.61, subd. 2b. This benefit is common when accumulated sick leave is used to pay for retiree medical insurance. Under the new GASB statements, accounting for OPEB is now similar to the accounting used by governments for pension plans.

Some of the issues that the County Board will need to address in order to comply with the statements are:

- determine if employees are provided OPEB;
- if OPEB are being provided, the County Board will have to determine whether it will advance fund the benefits or pay for them on a pay-as-you-go basis;
- if OPEB are being provided, and the County Board determines that the establishment of a trust is desirable in order to fund the OPEB, the County Board will have to wait until legislation is enacted authorizing the creation of an OPEB trust and establishing an applicable investment standard; and
- in order to determine annual costs and liabilities that need to be recognized, the County Board will have to decide whether to hire an actuary.

Schedule 7
(Continued)

If applicable for Lincoln County, GASB Statements 43 and 45 would be implemented for the years ended December 31, 2008 and 2009, respectively.



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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 County Commissioners
Lincoln County

We have audited the financial statements of the governmental activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of Lincoln County as of and for the year ended December 31, 2006, and have issued our report thereon dated March 14, 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 Lincoln County's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the County's internal control over financial reporting.

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

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the County's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the County's financial statements that is more than inconsequential will not be prevented or detected by the County's internal control. We considered the deficiencies described in the accompanying Schedule of Findings and Recommendations as items 98-1, 00-3, 04-2, 05-1, and 06-1 through 06-7 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 Lincoln County's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, of the significant deficiencies described above, we consider items 05-1 and 06-4 to be material weaknesses.

Compliance and Other Matters

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

Minnesota Legal Compliance

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

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

The results of our tests indicate that, for the items tested, Lincoln County complied with the material terms and conditions of applicable legal provisions.

Also included in the Schedule of Findings and Recommendations is a management comment and an other item for consideration. We believe this recommendation and information to be of benefit to Lincoln County and is reported for that purpose.

Lincoln County's written responses to the significant deficiencies and material weakness 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 Board of County Commissioners, management, and others within Lincoln County 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

March 14, 2008

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR