

# STATE OF MINNESOTA

## Office of the State Auditor



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

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MANAGEMENT AND COMPLIANCE REPORT  
PREPARED AS RESULT OF THE AUDIT OF

**LINCOLN COUNTY**  
**IVANHOE, MINNESOTA**

YEAR ENDED DECEMBER 31, 2009

## **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, 2009**



**Management and Compliance Report**

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

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**LINCOLN COUNTY  
IVANHOE, MINNESOTA**

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**LINCOLN COUNTY  
IVANHOE, MINNESOTA**

**Schedule 1**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED DECEMBER 31, 2009**

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

- A. Our report expresses unqualified opinions on the basic financial statements of Lincoln County.
- B. Deficiencies in internal control were disclosed by the audit of financial statements of Lincoln County and are reported in the "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*." One of the significant deficiencies is a material weakness.
- C. No instances of noncompliance material to the financial statements of Lincoln County were disclosed during the audit.
- D. No matters involving internal control over compliance relating to the audit of the major federal award programs were reported in the "Report on Compliance with Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance with OMB Circular A-133."
- E. The Auditor's Report on Compliance for the major federal award programs for Lincoln County expresses an unqualified opinion.
- F. No findings were disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133.
- G. The major programs are:
  - Highway Planning and Construction Cluster
  - Highway Planning and Construction CFDA #20.205
  - Highway Planning and Construction - ARRA CFDA #20.205
- H. The threshold for distinguishing between Types A and B programs was \$300,000.
- I. Lincoln County was not determined to be a low-risk auditee.

**II. 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

One basic objective of internal control is to provide for segregation of incompatible duties. In other words, responsibilities should be separated among employees so that a single employee is not able to authorize a transaction, record the transaction in accounts, and be responsible for custody of the asset resulting from the transaction.

Due to the limited number of personnel within some County offices, segregation of accounting duties necessary to ensure adequate internal accounting control is not always possible. This is not unusual in operations the size of Lincoln County; however, the County's management should constantly be aware of this condition and realize that the concentration of duties and responsibilities in a limited number of individuals is not desirable from an internal control point of view.

Some of the County's departments that collect fees have segregation of duties weaknesses. These departments generally have one staff person who is responsible for billing, collecting, depositing, and recording receipts as well as reconciling bank accounts.

We recommend the County Board segregate accounting duties as much as possible. When it is not feasible to segregate certain duties, Lincoln County management should 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 followed by staff.

Client's Response:

*Lincoln County is aware of the lack of segregation of the accounting functions. We continually strive to implement feasible internal controls.*



06-4 Audit Adjustments

A deficiency in internal control over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements of the financial statements on a timely basis. Statement on Auditing Standards No. 115 defines a material weakness as a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented or detected and corrected on a timely basis. During our audit, we proposed material audit adjustments, which were reviewed and approved by the appropriate staff and are reflected in the financial statements.

The inability to detect material misstatements in the financial statements increases the likelihood that the financial statements would not be fairly presented.

We recommend that the County modify internal controls over financial reporting to prevent or detect and correct misstatements in the financial statements.

Client's Response:

*The County strives to reduce audit adjustments and improve internal controls.*

ITEMS ARISING THIS YEAR

09-1 Employee Password Security

An employee in the County Auditor's Office maintains a listing of other employees' passwords and user names that provide access to the County's information system. Employee passwords are used for authentication to prove identity and to gain access to the information system and they should be kept secret by the employee and not be shared with any other employees. Passwords are used in an information system to protect the integrity of data, prevent unauthorized access of data, and assign responsibilities to those whose job duties are to maintain or make changes to data. When an employee has access to other employees' passwords, this significantly increases the risk of unauthorized access, unauthorized use, and compromises the integrity of the data in the information system.

We recommend that management ensure that employees do not share their passwords with others for safekeeping or any other purpose.

Client's Response:

*The Auditor's Office no longer maintains a listing of other employees' passwords/usernames.*

09-2 Property Tax Amount Levied in 2009 for County Use

For 2009, \$77,300 more was levied for property taxes than the amount approved by the County Board on December 18, 2008. The Board approved \$4,182,367; however, \$4,259,667 was levied on owners' property.

We recommend management make adjustments to its current procedures to ensure the amount levied on owners' property equals the Board-approved total.

Client's Response:

*Additional controls have been implemented to prevent this from happening in the future.*

09-3 Monitoring Internal Controls

County management is responsible for monitoring its internal controls. Monitoring involves assessing the quality of performance over time. Monitoring should occur during normal operations and includes reviews, comparisons, reconciliations, and other actions people take in performing their duties.

An essential element of monitoring controls also includes performing a risk assessment of existing controls over significant functions of the accounting system used to produce financial information for members of the County Board, management, and for external financial reporting. The risk assessment is intended to determine if the internal controls established by management are still effective or if changes are needed to maintain a sound internal control structure. Changes may be necessary due to such things as organizational restructuring, staffing vacancies, updates to information systems, or changes to services being provided.

Our audit procedures detected areas and responsibilities that are performed by County staff with little or no monitoring by management or other staff members. Some areas with minimal or no monitoring include:

- entering budget information into the accounting system;
- processing payroll and transmitting payment information to the bank;
- reviewing receipts issued; and
- reviewing identified receivables.

We recommend that a formal plan be developed that calls for assessing and monitoring the significant internal controls on a regular basis, no less than annually. The monitoring should be documented to show the results of the review, changes required, and who performed the work.

Client's Response:

*The County continues to revise and improve internal controls.*

PREVIOUSLY REPORTED ITEM RESOLVED

**Information System Risk Management (08-1)**

Lincoln County contracts with Computer Professionals Unlimited, Inc. (CPUI), a service organization, to provide: computer hardware for hosting the County's applications; processing of accounting transactions of other data; daily, weekly, and full system backups of applications and processed data; and disaster recovery planning for continued operations. During our site visit to CPUI, we noted that computers were not located in a restricted area away from public view. The computers were in an unlocked cage. Daily backup tapes for information processed Monday through Thursday were kept on site in a locked metal cabinet; however, the cabinet was not designed to protect the tapes from the heat that would be generated in the event of a fire. One fire extinguisher was observed in the office. Weekly and full system backup information was kept at an offsite location.

**Resolution**

CPUI now has a Sentry Safe that protects up to 1700 degrees. If necessary, the safe could be extracted through a nearby window in the event of a fire. In addition, the CPUI office now has two fire extinguishers, and computers are maintained in a locked storage room overnight.

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

None.

**IV. OTHER FINDINGS AND RECOMMENDATIONS**

OTHER ITEM FOR CONSIDERATION

GASB Statement 54

The Governmental Accounting Standards Board (GASB) recently issued Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*. The intention of this standard is to enhance the usefulness of information included in the financial report about fund balance through clearer fund balance classifications that can be more consistently applied, as well as to clarify existing governmental fund type definitions.

Fund Balance Reporting

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

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

Governmental Fund Type Definitions

The definitions of the general fund, special revenue fund type, capital projects fund type, debt service fund type, and permanent fund type are clarified in Statement 54. Interpretations of certain terms within the definition of the special revenue fund type have been provided and, for some governments, those interpretations may affect the activities they choose to report in those funds. The capital projects fund type definition also was clarified for better alignment with the needs of preparers and users. Definitions of other governmental fund types also have been modified for clarity and consistency.

The requirements of GASB Statement 54 are effective for Lincoln County for the year ending December 31, 2011.

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REBECCA OTTO  
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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, 2009, which collectively comprise the County's basic financial statements, and have issued our report thereon dated June 25, 2010. 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 and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified a deficiency in internal control over financial reporting that we consider to be a material weakness and other deficiencies that we consider to be significant deficiencies.

A deficiency in internal control over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the County's financial statements will not be prevented or detected and corrected on a timely basis. We consider the deficiency described in the accompanying Schedule of Findings and Questioned Costs as item 06-4 to be a material weakness.

A significant deficiency is a deficiency, or combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs as items 98-1, 09-1, 09-2, and 09-3 to be significant deficiencies.

### 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 seven categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, miscellaneous provisions, and tax increment financing. 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 Questioned Costs is an other item for consideration. We believe this information to be of benefit to the County, and it is reported for that purpose.



Lincoln County's written responses to the internal control findings identified in our audit have been included in the Schedule of Findings and Questioned Costs. We did not audit the County's responses 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, others within Lincoln County, and federal awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than those specified parties.

*/s/Rebecca Otto*

REBECCA OTTO  
STATE AUDITOR

*/s/Greg Hierlinger*

GREG HIERLINGER, CPA  
DEPUTY STATE AUDITOR

June 25, 2010

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## REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

Board of County Commissioners  
Lincoln County

### Compliance

We have audited the compliance of Lincoln County with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended December 31, 2009. Lincoln County's major federal programs are identified in the Summary of Auditor's Results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal programs is the responsibility of the County's management. Our responsibility is to express an opinion on the County's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Lincoln County's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the County's compliance with those requirements.

In our opinion, Lincoln County complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended December 31, 2009.

### Internal Control Over Compliance

Management of Lincoln County is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the County's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the County's internal control over compliance.

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

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

### Schedule of Expenditures of Federal Awards

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, 2009, which collectively comprise the County's basic financial statements, and have issued our report thereon dated June 25, 2010. Our audit was performed for the purpose of forming opinions on Lincoln County's financial statements that collectively comprise the County's basic financial statements. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

This report is intended solely for the information and use of the Board of County Commissioners, management and others within the County, and federal awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than those specified parties.

*/s/Rebecca Otto*

REBECCA OTTO  
STATE AUDITOR

*/s/Greg Hierlinger*

GREG HIERLINGER, CPA  
DEPUTY STATE AUDITOR

June 25, 2010

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**LINCOLN COUNTY  
IVAHHOE, MINNESOTA**

*Schedule 2*

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED DECEMBER 31, 2009**

Federal Grantor Pass-Through Agency Grant Program Title	Federal CFDA Number	Expenditures
<b>U.S. Department of Commerce</b>		
Passed Through Southwest Minnesota Regional Radio Board Public Safety Interoperable Communications Grant Program	11.555	<u>\$ 34,574</u>
<b>U.S. Department of Justice</b>		
Passed Through Minnesota Department of Safety Law Enforcement Assistance - Narcotics and Dangerous Drugs Training	16.004	<u>\$ 342</u>
<b>U.S. Department of Transportation</b>		
Passed Through Minnesota Department of Transportation Highway Planning and Construction Cluster		
Highway Planning and Construction	20.205	\$ 985,792
Highway Planning and Construction - ARRA	20.205	792,677
Formula Grants for Other Than Urbanized Areas Cluster		
Formula Grants for Other Than Urbanized Areas	20.509	53,755
Formula Grants for Other Than Urbanized Areas - ARRA	20.509	<u>54,766</u>
<b>Total U.S. Department of Transportation</b>		<u><b>\$ 1,886,990</b></u>
<b>U.S. Department of Homeland Security</b>		
Passed Through Minnesota Department of Public Safety		
Emergency Management Performance Grants	97.042	\$ 18,721
Homeland Security Grant Program	97.067	<u>2,999</u>
<b>Total U.S. Department of Homeland Security</b>		<u><b>\$ 21,720</b></u>
<b>Total Federal Awards</b>		<u><u><b>\$ 1,943,626</b></u></u>

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**LINCOLN COUNTY  
IVANHOE, MINNESOTA**

**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED DECEMBER 31, 2009**

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1. Reporting Entity

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

2. Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of Lincoln County under programs of the federal government for the year ended December 31, 2009. The information in this schedule is presented in accordance with the requirements of Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Because the schedule presents only a selected portion of the operations of Lincoln County, it is not intended to and does not present the financial position, changes in net assets, or cash flows of Lincoln County.

3. Summary of Significant Accounting Policies

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

4. Subrecipients

During 2009, the County did not pass any federal money to subrecipients.

5. American Recovery and Reinvestment Act

The American Recovery and Reinvestment Act of 2009 (ARRA) requires recipients to clearly distinguish ARRA funds from non-ARRA funding. In the schedule, ARRA funds are denoted by the addition of ARRA to the program name.