

STATE OF MINNESOTA

Office of the State Auditor



Patricia Anderson
State Auditor

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

FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

Description of the Office of the State Auditor

The Office of the State Auditor serves as a watchdog for Minnesota taxpayers by helping to ensure financial integrity, accountability, and cost-effectiveness in local governments throughout the state.

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 250 financial and compliance audits per year and has oversight responsibilities for over 4,300 local units of government throughout the state. The office currently maintains five divisions:

Audit Practice - conducts financial and legal compliance audits for 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 over 700 public pension funds; and

Tax Increment Financing, Investment and Finance - 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 Employee's Retirement Association Board, Minnesota Housing Finance Agency, and the Rural Finance Authority Board.

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

For the Years Ended December 31, 2005 and 2004



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

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

TABLE OF CONTENTS

	Reference	Page
Introductory Section		
Organization		1
Financial Section		
Independent Auditor’s Report		2
Management’s Discussion and Analysis		4
Basic Financial Statements		
Comparative Statement of Net Assets	Exhibit A	11
Comparative Statement of Revenues, Expenses, and Changes in Net Assets	Exhibit B	13
Comparative Statement of Cash Flows	Exhibit C	14
Notes to the Financial Statements		15
Supplementary Information		
Comparative Statement of Operating Revenues	Schedule 1	29
Management and Compliance Section		
Schedule of Findings and Questioned Costs	Schedule 2	30
Other Required Reports		
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>		33
Report on Compliance with Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance with OMB Circular A-133 and Passenger Facility Charge Programs		35
Schedule of Expenditures of Federal Awards	Schedule 3	38
Schedule of Passenger Facility Charges Collected and Expended	Schedule 4	39

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

**ORGANIZATION
DECEMBER 31, 2005**

	<u>Term Ending</u>
Directors	
Nancy Aronson Norr	July 1, 2007
David Boe	July 1, 2008
Todd Fedora	July 1, 2006
Michael E. Orman	July 1, 2006
Dennis L. Ramberg	July 1, 2006
John M. Eagleton	July 1, 2007
James Laumeyer	July 1, 2007
Executive Director	
Brian Ryks	
Officers	
President	
Dennis L. Ramberg	
Vice President	
James Laumeyer	
Secretary	
Todd Fedora	

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OFFICE OF THE STATE AUDITOR

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PATRICIA ANDERSON
STATE AUDITOR

INDEPENDENT AUDITOR'S REPORT

Mayor and City Council
City of Duluth

Board of Directors
Duluth Airport Authority

We have audited the accompanying basic financial statements of the Duluth Airport Authority, a component unit of the City of Duluth, as of and for the years ended December 31, 2005 and 2004. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Duluth Airport Authority as of December 31, 2005 and 2004, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted primarily 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 audits were made for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying financial information listed as supplementary information in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements. The supplementary information has been subjected to the auditing procedures applied in the audits 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 30, 2006, on our consideration of the Duluth Airport Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

/s/Pat Anderson

PATRICIA ANDERSON
STATE AUDITOR

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

End of Fieldwork: March 30, 2006

MANAGEMENT'S DISCUSSION AND ANALYSIS

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2005
(Unaudited)**

Our Management's Discussion and Analysis (MD&A) of the Duluth Airport Authority's financial performance provides an overview of the Authority's financial activities for the fiscal year ended December 31, 2005. Please read it in conjunction with the financial statements.

FINANCIAL HIGHLIGHTS

- Operating expenses (before depreciation and amortization) increased \$272.7 thousand, or ten percent, compared to fiscal year 2004, due in large part to increased workers' compensation costs and repairs, maintenance, and cleaning costs for an aging infrastructure. Additionally, the increase is attributed to price increases for fuel and utilities.
- Operating revenue decreased \$77.4 thousand, or three percent, due to reduced reimbursement of \$13 thousand by the Transportation Security Agency and a \$64 thousand decline in space rental revenues at the terminal building, \$46 thousand due to the departure of American Eagle Airlines.
- Nonoperating federal and state grant revenues increased \$6 million, or 90 percent, from 2004. Total net assets increased \$10.9 million, or 30 percent, compared to fiscal year 2004.
- Total number of passengers decreased by 11.2 thousand, or four percent, for a total of 305.8 thousand in 2005.
- Total traffic count as recorded by the Federal Aviation Administration (FAA) tower, decreased by over 4.3 thousand, or six percent. Of this figure, approximately 88.6 percent is commercial and general aviation traffic, with the remaining 11.4 percent military traffic.
- Landing fee revenues for 2005 increased by \$3.1 thousand, or one percent, due to a price increase.
- Passenger facility charge revenue decreased \$135.2 thousand in 2005, or 26 percent, compared to 2004.
- Total parking lot gross sales decreased by \$10.8 thousand, or 1.4 percent for 2005.
- Total car rental gross sales decreased by \$71 thousand or two percent.

- The 2005/2006 State Maintenance and Operations Agreement, which became effective July 1, 2005, provided for \$188.9 thousand of state aid, unchanged from the previous year.
- The Transportation Security Administration (TSA) extended its agreement with the Authority effective October 1, 2005, through September 30, 2006, to reimburse the Authority 14 hours per day for contracted law enforcement personnel, or approximately \$7.4 thousand per month.

OVERVIEW OF ANNUAL FINANCIAL REPORT

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

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

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

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

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

SUMMARY OF ORGANIZATION AND BUSINESS

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

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

Operating revenue for the Duluth Airport Authority comes from a variety of sources including: car rental concessions, parking, space and land rentals, Fixed Base Operator concessions, TSA reimbursement for law enforcement, maintenance and operations grant funds from the State of Minnesota, landing fees, airport food and beverage concessions, and Air National Guard joint use funds. The Authority is self-sufficient and is not subsidized by the City of Duluth.

FINANCIAL ANALYSIS

The following comparative condensed financial statements and other selected information serve as the key financial data and indicators for management, monitoring, and planning. Comments regarding year-to-year variances follow:

Condensed Statement of Net Assets (000s)

	FY 2005	FY 2004	FY 2003
Current and restricted assets	\$ 5,663	\$ 3,764	\$ 2,750
Capital assets	25,791	26,470	19,848
Construction in progress	<u>20,606</u>	<u>8,129</u>	<u>9,331</u>
Total Assets	<u>\$ 52,060</u>	<u>\$ 38,363</u>	<u>\$ 31,929</u>
Current liabilities	\$ 4,191	\$ 1,883	\$ 862
Long-term liabilities	<u>670</u>	<u>203</u>	<u>228</u>
Total Liabilities	<u>\$ 4,861</u>	<u>\$ 2,086</u>	<u>\$ 1,090</u>
Net assets			
Invested in capital assets	\$ 45,622	\$ 34,278	\$ 29,160
Restricted passenger facility charge revenue	-	168	-
Unrestricted	<u>1,577</u>	<u>1,831</u>	<u>1,679</u>
Total Net Assets	<u>\$ 47,199</u>	<u>\$ 36,277</u>	<u>\$ 30,839</u>

As can be seen from the table, net assets increased by \$10.9 million to \$47.2 million in 2005, up from \$36.3 million in 2004. The increase in net assets was primarily due to the \$11.3 million increase in invested in capital assets, as well as a decrease of \$168 thousand in restricted net assets.

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

	FY 2005 Actual	FY 2005 Budget	FY 2004 Actual	FY 2003 Actual
Total operating revenues	\$ 2,811	\$ 2,581	\$ 2,888	\$ 2,709
Total operating expenses	<u>(5,275)</u>	<u>(4,738)</u>	<u>(5,015)</u>	<u>(4,647)</u>
Income (Loss)	\$ (2,464)	\$ (2,157)	\$ (2,127)	\$ (1,938)
Nonoperating revenues	575	500	779	500
Other revenues	<u>12,811</u>	<u>11,228</u>	<u>6,786</u>	<u>3,517</u>
Change in Net Assets	<u>\$ 10,922</u>	<u>\$ 9,571</u>	<u>\$ 5,438</u>	<u>\$ 2,079</u>

REVENUES

Operating revenues decreased by \$77.4 thousand, or three percent, in 2005 relative to 2004 due to several factors, the most significant being the departure of American Eagle Airlines on September 1, 2004.

EXPENSES

Duluth Airport Authority expenses increased by \$260 thousand to \$5,275 thousand in 2005, up from \$5,015 thousand in 2004. The increase was due primarily to increases in supplies and utilities expenses. Expenses for supplies increased by \$54.7 thousand primarily due to transition from a Fixed Base Operator at Sky Harbor Airport to operation by the Authority. Expenses for utilities increased by \$100 thousand, from \$386 thousand in 2004 to \$486 thousand in 2005 due to price increases. Expenses for repairs and maintenance increased \$30 thousand, from \$378 thousand in 2004 to \$408 thousand in 2005. Expenses for professional services increased \$48 thousand, from \$91 thousand in 2004 to \$139 thousand in 2005. Employee benefits increased \$89 thousand, due primarily to increased workers' compensation costs. Payroll decreased \$18 thousand, from \$914 thousand in 2004 to \$896 thousand in 2005.

BUDGETARY HIGHLIGHTS

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

The past four years have been the most challenging ever experienced in the aviation industry. The return of passenger travel has been sluggish, and the effects of 9-11 are still felt. Security has taken on an ever-encompassing role with the creation of the TSA and the federalization of security screening personnel.

The airline industry remains in turmoil. The Aircraft Mechanics Fraternal Association struck against Northwest Airlines (NWA) in August 2005, which led to the NWA's A-320 Maintenance Base being shut down. In the fall of 2005, both NWA and Mesabi Airlines filed for bankruptcy. Negative impacts to the region's service are being felt as fewer markets are now being served from Duluth with the loss of a Detroit flight. Additionally, American Eagle Airlines discontinued service in September 2004.

On a positive note, Allegiant Airlines will begin service to Las Vegas from Duluth twice weekly beginning in January 2006.

As far as capital projects, the Authority continued to make improvements and respond to new security directives with the following major projects in 2005:

- Construction of Phase 1 to the Aircraft Rescue and Fire Fighting Facility (ARFF)- \$1.35 million;
- design and construction of Runway 9-27 shoulder and lighting, Phase 2 - \$2.8 million;
- North Perimeter Road, Phase 2 - \$2.6 million;
- north perimeter fencing - \$4.08 million;
- design of passenger terminal upgrades - \$530 thousand; and
- Sky Harbor Airport apron reconstruction - \$420 thousand.

On November 1, 2005, transition of the Fixed Base Operator from North Country Aviation to Monaco Air was completed. The transition has led to more services for corporate, charter, and general aviation users.

The union contract between the Duluth Airport Authority and AFSCME Local 66 was renegotiated in 2005 and is effective through December 31, 2006.

CAPITAL ASSETS

	Capital Assets (000s)			Total Percent (%) Change
	FY 2005	FY 2004	Dollar Change Increase (Decrease)	
Land	\$ 2,228	\$ 2,228	\$ -	-
Runways	37,450	37,238	212	0.57
Buildings	15,737	15,621	116	0.74
Equipment	4,733	4,175	558	13.37
Construction in progress	20,606	8,129	12,477	153.49
Total capital assets	\$ 80,754	\$ 67,391	\$ 13,363	19.83
Less: accumulated depreciation	(35,132)	(33,113)	(2,019)	(6.10)
Net Capital Assets	\$ 45,622	\$ 34,278	\$ 11,344	33.09

At the end of 2005, the Duluth Airport Authority has invested approximately \$81 million in capital assets. The \$13 million increase in capital assets this past year is primarily due to several runway projects, including the construction phase of Runway 9-27, lighting and drainage Phase 2, the north perimeter road construction, apron reconstruction at Sky Harbor Airport, and Phase 1 construction of the ARFF.

The Duluth Airport Authority recently submitted a new Airport Capital Improvement Program (ACIP) through 2016, which includes for 2006:

- \$200 thousand for engineering for general aviation arrivals development,
- \$150 thousand for a terminal building boiler,
- \$100 thousand for Runway 3-21 pavement rehabilitation,
- \$7,352 thousand for Phase 3 construction improvements to Runway 9-27 pavement and shoulders,
- \$1,700 thousand general aviation arrivals site work,
- \$100 thousand seaplane dock reconstruction and ramp rehabilitation for Sky Harbor Airport,
- \$95 thousand for Sky Harbor fuel facility upgrades, and
- \$50 thousand for obstruction removal and lighting at Sky Harbor Airport

DEBT ADMINISTRATION

The Duluth Airport Authority entered into a Lease Acquisition Agreement with North Country Aviation (NCA) on November 1, 2005, where the Authority agrees to pay NCA \$497,378.55. The purpose of the note was to acquire the NCA's Fixed Based Operator lease agreement and to facilitate its transfer to Monaco Air. Such amount shall be payable by the Authority as Airport Facility Revenue Note, Series 2005A. The note is for a term of 13 years, payable each June 1 and December 1, commencing June 1, 2007. Interest is compounded at 8.85 percent per annum.

ECONOMIC AND OTHER FACTORS

When setting the 2005 budget, the Duluth Airport Authority took many factors into consideration: the loss of American Eagle Airlines, the financial turmoil of the commercial aviation sector, lingering effects of 9-11 and its effects on commercial air travel as well as airport security, weather conditions that dictate utility costs and overtime for snow removal crews, energy price increases, and a general review of all rates and services so that revenue will keep pace with expenses. The Duluth Airport Authority has already taken steps to: raise hangar rates, parking rates, and landing fee rates for commercial as well as general aviation aircraft, and also cut costs by utility conservation and reductions in operating supplies, travel, professional services, overtime pay, and contract services. The Authority aggressively seeks new lessees to occupy space as well as economic development opportunities that are a good fit for the aviation sector. An example of this is the Authority's lobbying effort to attain the former Navy Reserve Building on the former Duluth Air Force Base. The Duluth Airport Authority will continue to seek diversifying revenue sources in order to be less reliant on airline revenue sources.

FINANCIAL CONTACT

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

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BASIC FINANCIAL STATEMENTS

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

EXHIBIT A

**COMPARATIVE STATEMENT OF NET ASSETS
DECEMBER 31, 2005 AND 2004**

	2005	2004
Assets		
Current assets		
Cash and cash equivalents	\$ 1,540,208	\$ 1,554,861
Accounts receivable	487,478	196,506
Grants receivable	59,078	88,233
Inventory	54,984	72,077
Prepaid items	59,615	55,818
Assets restricted for construction		
Cash and cash equivalents	759,281	770,691
Accounts receivable	59,657	2,448
Grants receivable	2,642,992	1,023,412
Total current assets	\$ 5,663,293	\$ 3,764,046
Noncurrent assets		
Capital assets		
Nondepreciable	\$ 22,834,242	\$ 10,357,761
Depreciable	57,920,193	57,033,657
Less: allowance for depreciation	(35,131,946)	(33,112,955)
Net capital assets	\$ 45,622,489	\$ 34,278,463
Other assets		
Airport planning costs, net of accumulated amortization of \$420,138 in 2005 and \$356,730 in 2004	\$ 257,384	\$ 320,792
Lease buyout costs, net of accumulated amortization of \$10,352	517,027	-
Total other assets	\$ 774,411	\$ 320,792
Total noncurrent assets	\$ 46,396,900	\$ 34,599,255
Total Assets	\$ 52,060,193	\$ 38,363,301

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

**EXHIBIT A
(Continued)**

**COMPARATIVE STATEMENT OF NET ASSETS
DECEMBER 31, 2005 AND 2004**

	2005	2004
Liabilities		
Current liabilities		
Accounts payable	\$ 100,758	\$ 51,526
Due to City of Duluth	335,636	-
Due to other governments	45,561	44,789
Accrued salaries payable	25,114	19,187
Accrued vacation payable	40,289	39,847
Construction contracts payable	3,137,845	1,482,192
Accrued interest payable	7,274	-
Deferred revenue	468,761	244,965
Advances payable	30,000	-
Total current liabilities	\$ 4,191,238	\$ 1,882,506
Noncurrent liabilities		
Deferred revenue	\$ 172,238	\$ 203,472
Revenue notes payable	497,379	-
Total noncurrent liabilities	\$ 669,617	\$ 203,472
Total Liabilities	\$ 4,860,855	\$ 2,085,978
Net Assets		
Invested in capital assets	\$ 45,622,489	\$ 34,278,463
Restricted passenger facility charge revenue	-	167,848
Unrestricted	1,576,849	1,831,012
Total Net Assets	\$ 47,199,338	\$ 36,277,323

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

EXHIBIT B

**COMPARATIVE STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
YEARS ENDED DECEMBER 31, 2005 AND 2004**

	2005	2004
Operating Revenues		
Charges for services	\$ 2,811,160	\$ 2,888,530
Operating Expenses		
Personal services	\$ 1,269,934	\$ 1,267,658
Supplies	100,571	46,820
Utilities	486,393	386,634
Other services and charges	1,252,703	1,135,767
Depreciation	2,091,247	2,100,949
Amortization	73,759	77,346
Total Operating Expenses	\$ 5,274,607	\$ 5,015,174
Net Operating Income (Loss)	\$ (2,463,447)	\$ (2,126,644)
Nonoperating Revenues (Expenses)		
Earnings on investments	\$ 68,435	\$ 28,118
Passenger facility charge	387,531	522,774
Gain (loss) on disposal of capital assets	(1,732)	111,500
Interest expense	(7,274)	-
Marketing grant	21,217	116,608
Small community air service development grant	106,912	854,442
American Eagle minimum revenue guarantee	-	(854,442)
Total Nonoperating Revenues (Expenses)	\$ 575,089	\$ 779,000
Net Income (Loss) Before Other Revenues	\$ (1,888,358)	\$ (1,347,644)
Other Revenues		
Capital grants		
Federal	\$ 12,582,790	\$ 6,687,803
State	227,583	98,097
Total Other Revenues	\$ 12,810,373	\$ 6,785,900
Change in Net Assets	\$ 10,922,015	\$ 5,438,256
Net Assets - January 1	36,277,323	30,839,067
Net Assets - December 31	\$ 47,199,338	\$ 36,277,323

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

EXHIBIT C

**COMPARATIVE STATEMENT OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2005 AND 2004**

	2005	2004
Cash Flows from Operating Activities		
Cash received from customers	\$ 2,330,292	\$ 2,875,696
Cash paid to suppliers	(1,440,731)	(1,604,328)
Cash paid to employees	(1,263,565)	(1,332,756)
Other cash receipts	203,752	291,379
	\$ (170,252)	\$ 229,991
Cash Flows from Noncapital Financing Activities		
Small community air service development grant	\$ 106,912	\$ 854,442
American Eagle minimum revenue guarantee	-	(854,442)
	\$ 106,912	\$ -
Cash Flows from Capital and Related Financing Activities		
Principal paid on hangar loan	\$ -	\$ (19,470)
Capital grants - federal	11,167,557	6,225,423
Capital grants - state	256,136	26,711
Passenger facility charge	330,322	549,193
Proceeds from sale of capital assets	7,790	111,500
Acquisition or construction of capital assets	(11,792,963)	(6,425,318)
	\$ (31,158)	\$ 468,039
Cash Flows from Investing Activities		
Interest on investments	\$ 68,435	\$ 28,118
	\$ (26,063)	\$ 726,148
Net Increase (Decrease) in Cash and Cash Equivalents		
	\$ (26,063)	\$ 726,148
Cash and Cash Equivalents - January 1	2,325,552	1,599,404
Cash and Cash Equivalents - December 31	\$ 2,299,489	\$ 2,325,552
Reconciliation of Operating Income (Loss) to Net Cash Provided by (Used for) Operating Activities		
Net operating income (loss)	\$ (2,463,447)	\$ (2,126,644)
Adjustments to reconcile net operating income (loss) to net cash provided by (used for) operating activities		
Depreciation	2,091,247	2,100,949
Amortization	73,759	77,346
Marketing grant	17,861	116,608
Changes in assets and liabilities		
Decrease (increase) in receivables	(258,461)	117,005
Decrease (increase) in inventory	17,093	(48)
Decrease (increase) in prepaids	(3,797)	2,006
Increase (decrease) in payables	392,009	(102,163)
Increase (decrease) in deferred revenue	(36,516)	44,932
	\$ (170,252)	\$ 229,991

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

NOTES TO THE FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

1. Summary of Significant Accounting Policies

The accounting policies of the Duluth Airport Authority conform to generally accepted accounting principles.

A. Financial Reporting Entity

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

B. Basis of Presentation

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

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

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

1. Summary of Significant Accounting Policies (Continued)

C. Basis of Accounting

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

D. Budget

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

E. Cash and Cash Equivalents

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

F. Accounts Receivable

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

G. Inventory

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

H. Restricted Assets

Monies restricted for the payment of construction contracts and passenger facility charge revenues are accounted for as restricted assets. When both restricted and unrestricted resources are available for use, it is the Authority's policy to use restricted resources first, then unrestricted resources as they are needed.

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

1. Summary of Significant Accounting Policies (Continued)

I. Capital Assets

Capital assets are stated at cost. The Authority's policy is to capitalize assets with a useful life of one year or more and a minimum cost of \$300.

J. Depreciation

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

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

K. Other Assets

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

L. Deferred Revenue

Amounts received as advance payments for rentals and parking lot commissions are reported as deferred revenue until they are earned. In addition, a rent abatement agreement for land improvements is reported as deferred revenue until earned.

M. Passenger Facility Charges

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

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

1. Summary of Significant Accounting Policies (Continued)

N. Use of Estimates

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

2. Detailed Notes

A. Deposits and Investments

Minn. Stat. §§ 118A.02 and 118A.04 authorize the Authority and the City Council of Duluth to designate a depository of public funds and to invest in certificates of deposit. Minnesota statutes require that all Authority deposits be covered by insurance, surety bond, or collateral.

Minn. Stat. §§ 118A.04 and 118A.05 authorize the types of securities available to the Authority for investment.

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

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

	December 31	
	2005	2004
City pooled cash and investments	\$ 452,177	\$ 196,578
Authority checking accounts	17,963	566,530
Authority savings account	1,829,099	1,562,194
Petty cash funds	250	250
Total	<u>\$ 2,299,489</u>	<u>\$ 2,325,552</u>

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

2. Detailed Notes

A. Deposits and Investments (Continued)

	December 31	
	2005	2004
Detail as shown on Comparative Balance Sheet		
Current assets		
Cash and cash equivalents	\$ 1,540,208	\$ 1,554,861
Assets restricted for construction		
Cash and cash equivalents	759,281	770,691
Total Cash and Cash Equivalents	\$ 2,299,489	\$ 2,325,552

B. Capital Assets

A summary of changes in capital assets at December 31, 2005 and 2004, follows:

	Balance January 1, 2005	Increase	Decrease	Transfers	Balance December 31, 2005
Capital assets not depreciated					
Land	\$ 2,228,456	\$ -	\$ -	\$ -	\$ 2,228,456
Construction in progress	8,129,305	13,463,088	51,235	(935,372)	20,605,786
Total capital assets not depreciated	\$ 10,357,761	\$ 13,463,088	\$ 51,235	\$ (935,372)	\$ 22,834,242
Capital assets depreciated					
Buildings	\$ 15,620,521	\$ 13,118	\$ -	\$ 103,799	\$ 15,737,438
Runways	37,237,850	3,819	-	207,798	37,449,467
Equipment	4,175,286	18,617	84,390	623,775	4,733,288
Total capital assets depreciated	\$ 57,033,657	\$ 35,554	\$ 84,390	\$ 935,372	\$ 57,920,193
Less: accumulated depreciation for					
Buildings	\$ 7,781,222	\$ 433,668	\$ -	\$ -	\$ 8,214,890
Runways	22,099,819	1,435,409	-	-	23,535,228
Equipment	3,231,914	222,170	72,256	-	3,381,828
Total accumulated depreciation	\$ 33,112,955	\$ 2,091,247	\$ 72,256	\$ -	\$ 35,131,946
Total capital assets depreciated, net	\$ 23,920,702	\$ (2,055,693)	\$ 12,134	\$ 935,372	\$ 22,788,247
Capital Assets, Net	\$ 34,278,463	\$ 11,407,395	\$ 63,369	\$ -	\$ 45,622,489

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

2. Detailed Notes

B. Capital Assets (Continued)

	Balance January 1, 2004	Increase	Decrease	Transfers	Balance December 31, 2004
Capital assets not depreciated					
Land	\$ 2,215,327	\$ 13,129	\$ -	\$ -	\$ 2,228,456
Construction in progress	9,330,750	7,556,926	7,251	(8,751,120)	8,129,305
Total capital assets not depreciated	\$ 11,546,077	\$ 7,570,055	\$ 7,251	\$ (8,751,120)	\$ 10,357,761
Capital assets depreciated					
Buildings	\$ 11,618,878	\$ 27,878	\$ 16,656	\$ 3,990,421	\$ 15,620,521
Runways	32,494,716	-	-	4,743,134	37,237,850
Equipment	4,328,531	26,498	197,308	17,565	4,175,286
Total capital assets depreciated	\$ 48,442,125	\$ 54,376	\$ 213,964	\$ 8,751,120	\$ 57,033,657
Less: accumulated depreciation for					
Buildings	\$ 7,357,370	\$ 439,424	\$ 15,572	\$ -	\$ 7,781,222
Runways	20,650,752	1,449,067	-	-	22,099,819
Equipment	3,198,956	212,456	179,498	-	3,231,914
Total accumulated depreciation	\$ 31,207,078	\$ 2,100,947	\$ 195,070	\$ -	\$ 33,112,955
Total capital assets depreciated, net	\$ 17,235,047	\$ (2,046,571)	\$ 18,894	\$ 8,751,120	\$ 23,920,702
Capital Assets, Net	\$ 28,781,124	\$ 5,523,484	\$ 26,145	\$ -	\$ 34,278,463

As of December 31, 2005, the Authority had the following commitments with respect to unfinished construction projects:

<u>Projects</u>	<u>Remaining Construction Commitment</u>
AIP 37	\$ 438,239
AIP 38	840,854
AIP 39	343,507
AIP 40	1,371,220
Air National Guard ARFF Project	98,300
Air National Guard By-pass Project	1,835,712
Transportation Security Administration Safety Project	43,928
Total	\$ 4,971,760

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

2. Detailed Notes

B. Capital Assets (Continued)

As of December 31, 2004, the Authority had the following commitments with respect to unfinished construction projects:

Projects	Remaining Construction Commitment
SP6901-137	\$ 28,237
SP6901-143	107,466
AIP 36	75,761
AIP 37	4,779,887
Air National Guard ARFF Project	101,500
Air National Guard BAK Project	41,252
Total	\$ 5,134,103

C. Vacation and Sick Leave

Full-time employees are granted from 12 to 28 days of vacation time per year depending on their years of service. Maximum amounts of vacation time that can be accumulated range from 18 to 42 days. Unpaid vacation time earned at year-end is recognized as a liability in the financial statements. Sick leave is granted to a maximum of 120 days per illness and is recorded as an expense when paid. Employees are not compensated for unused sick leave. Any liability for earned, unused sick leave is not recognized in the financial statements.

D. Leases

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

Minimum future rents receivable on noncancellable leases are:

2006	\$ 206,469
2007	206,255
2008	205,187
2009	205,187
2010	203,107
After 2010	2,180,984
Total	\$ 3,207,189

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

2. Detailed Notes

D. Leases (Continued)

Contingent rental income from operating leases for 2005 and 2004 was \$875,635 and \$873,402, respectively.

E. Budgets

The Duluth Airport Authority adopts a budget to be approved by the Duluth City Council. A summary of the operating budget for the fiscal years ended December 31, 2005 and 2004, is:

	2005		Variance Favorable (Unfavorable)
	Budget	Actual	
Operating Revenues			
Charges for services	\$ 2,580,817	\$ 2,811,160	\$ 230,343
Operating Expenses			
Personal services	\$ 1,385,700	\$ 1,269,934	\$ 115,766
Supplies	109,300	100,571	8,729
Utilities	389,393	486,393	(97,000)
Other services and charges	833,695	1,252,703	(419,008)
Depreciation	1,950,000	2,091,247	(141,247)
Amortization	70,000	73,759	(3,759)
Total Operating Expenses	\$ 4,738,088	\$ 5,274,607	\$ (536,519)
Net Operating Income (Loss)	\$ (2,157,271)	\$ (2,463,447)	\$ (306,176)
Nonoperating Revenues (Expenses)			
Earnings on investments	\$ 35,000	\$ 68,435	\$ 33,435
Passenger facility charge	465,000	387,531	(77,469)
Gain (loss) on disposal of assets	-	(1,732)	(1,732)
Interest expense	-	(7,274)	(7,274)
Marketing grant	-	21,217	21,217
Small community air service development grant	-	106,912	106,912
Total Nonoperating Revenues (Expenses)	\$ 500,000	\$ 575,089	\$ 75,089
Net Income (Loss) Before Other Revenues	\$ (1,657,271)	\$ (1,888,358)	\$ (231,087)
Other Revenues			
Capital grants - federal	\$ 10,198,900	\$ 12,582,790	\$ 2,383,890
Capital grants - state	1,029,500	227,583	(801,917)
Total Other Revenues	\$ 11,228,400	\$ 12,810,373	\$ 1,581,973
Change in Net Assets	\$ 9,571,129	\$ 10,922,015	\$ 1,350,886

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

2. Detailed Notes

E. Budgets (Continued)

	2004		Variance Favorable (Unfavorable)
	Budget	Actual	
Operating Revenues			
Charges for services	\$ 2,639,952	\$ 2,888,530	\$ 248,578
Operating Expenses			
Personal services	\$ 1,289,500	\$ 1,267,658	\$ 21,842
Supplies	103,920	46,820	57,100
Utilities	373,872	386,634	(12,762)
Other services and charges	781,811	1,135,767	(353,956)
Depreciation	1,700,000	2,100,949	(400,949)
Amortization	120,000	77,346	42,654
Total Operating Expenses	\$ 4,369,103	\$ 5,015,174	\$ (646,071)
Net Operating Income (Loss)	\$ (1,729,151)	\$ (2,126,644)	\$ (397,493)
Nonoperating Revenues (Expenses)			
Earnings on investments	\$ 34,000	\$ 28,118	\$ (5,882)
Passenger facility charge	485,000	522,774	37,774
Gain (loss) on disposal of assets	-	111,500	111,500
Marketing grant	-	116,608	116,608
Small community air service development grant	-	854,442	854,442
American Eagle minimum revenue guarantee	-	(854,442)	(854,442)
Total Nonoperating Revenues (Expenses)	\$ 519,000	\$ 779,000	\$ 260,000
Net Income (Loss) Before Other Revenues	\$ (1,210,151)	\$ (1,347,644)	\$ (137,493)
Other Revenues			
Capital grants - federal	\$ 6,905,520	\$ 6,687,803	\$ (217,717)
Capital grants - state	474,019	98,097	(375,922)
Total Other Revenues	\$ 7,379,539	\$ 6,785,900	\$ (593,639)
Change in Net Assets	\$ 6,169,388	\$ 5,438,256	\$ (731,132)

F. Long-Term Debt

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

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

2. Detailed Notes

F. Long-Term Debt (Continued)

The annual requirements to service the debt follow:

<u>Year Ended December 31</u>	<u>Principal</u>	<u>Interest</u>
2006	\$ -	\$ -
2007	-	60,000
2008	-	75,000
2009	22,170	52,830
2010	33,673	41,327
2011 - 2015	219,952	155,048
2016 - 2019	221,584	40,916
 Total	 <u>\$ 497,379</u>	 <u>\$ 425,121</u>

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

	<u>2005</u>	<u>2004</u>
Balance - January 1	\$ -	\$ 19,470
Additions	497,379	-
Payments	-	(19,470)
 Balance - December 31	 <u>\$ 497,379</u>	 <u>\$ -</u>
 Due Within One Year	 <u>\$ -</u>	 <u>\$ -</u>

3. Risk Management

The Authority is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; employee health and dental; and natural disasters. The Authority participates in the City of Duluth internal service funds to provide its employees health and dental benefits and to insure against its obligation to provide benefits to employees pursuant to the Minnesota Workers' Compensation Act. The Authority purchases commercial insurance for all other risks of loss. There were no significant reductions in insurance coverage from the previous year. There were no settlements in excess of insurance for any of the past three fiscal years.

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

3. Risk Management (Continued)

Employee health and dental benefits are provided through the City of Duluth Group Health Internal Service Fund at premium rates established by the City for all plan participants.

An annual contribution is made to the City of Duluth Self-Insurance Internal Service Fund to provide for payment of workers' compensation claims and costs. Additional amounts may be charged to the Authority for contested claims.

4. Major Customers

Major customers of services provided by the Duluth Airport Authority in 2005 were:

	<u>Operating Revenues</u>	<u>Percentage of Total Operating Revenues</u>
Northwest Airlines	\$ 417,720	14.9%
APCOA, Inc.	647,075	23.0%

Major customers of services provided by the Duluth Airport Authority in 2004 were:

	<u>Operating Revenues</u>	<u>Percentage of Total Operating Revenues</u>
Northwest Airlines	\$ 478,765	16.6%
APCOA, Inc.	656,875	22.7%

5. Pension Plans

A. Plan Description

All full-time and certain part-time employees of the Duluth Airport Authority are covered by defined benefit plans administered by the Public Employees Retirement Association of Minnesota (PERA). The PERA administers the Public Employees Retirement Fund, which is a cost-sharing, multiple-employer retirement plan. The plan is established and administered in accordance with Minn. Stat. chs. 353 and 356.

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

5. Pension Plans

A. Plan Description (Continued)

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.

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. Using 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 Retirement Fund members whose annuity is calculated using Method 1, 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. 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.

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

5. Pension Plans (Continued)

B. 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 Authority 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 5.10 percent, respectively, of their annual covered salary in 2005. Contribution rates in the Coordinated Plan increased in 2006 to 5.5 percent. The Authority is required to contribute the following percentages of annual covered payroll:

In 2005	
Public Employees Retirement Fund	
Basic Plan members	11.78%
Coordinated Plan members	5.53
In 2006	
Public Employees Retirement Fund	
Basic Plan members	11.78%
Coordinated Plan members	6.00

The Authority's contributions for the years ending December 31, 2005, 2004, and 2003, were \$44,088, \$43,166, and \$48,387, respectively, equal to the contractually required contributions for each year as set by state statute.

6. Other Postemployment Benefits

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

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

6. Other Postemployment Benefits (Continued)

The Authority participates in the City of Duluth Group Health Internal Service Fund and pays the required premiums to provide health care benefits and term life insurance for eligible retirees and claimed dependents. Health care premiums are paid by the Authority to the same extent as active employees for the life of the retiree or the surviving spouse. Life insurance premiums are paid by the Authority for the life of the retiree. Premiums paid for eligible retirees and claimed dependents for health care and life insurance in 2005 totaled \$120,683 and \$360, respectively. In 2004, the amounts paid were \$109,692 and \$360.

SUPPLEMENTARY INFORMATION

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

Schedule 1

**COMPARATIVE STATEMENT OF OPERATING REVENUES
YEARS ENDED DECEMBER 31, 2005 AND 2004**

	2005	2004
Operating Revenues		
Charges for services		
Tower building		
Space rental and services	\$ 203,661	\$ 197,635
Terminal building		
Loading bridges rent	\$ 32,647	\$ 39,738
Space rental	343,126	407,162
Utility sales	35,620	35,053
Car rental commissions	358,520	365,956
Other commissions	4,784	6,902
Percentage of lessees' sales	21,450	19,299
Other income	24,387	44,254
Total terminal building	\$ 820,534	\$ 918,364
Parking lot		
Parking lot commissions	\$ 647,075	\$ 656,875
Land, field, and runways		
Airport use contract - Minnesota Air National Guard	\$ 50,000	\$ 50,000
Transportation Security Administration charges	97,814	110,559
State aid for maintenance and operation	132,795	192,879
Rental income	256,829	239,404
Fuel flowage fees	34,868	26,268
Landing fees	361,547	358,433
Percentage of lessees' sales	7,011	8,719
Utility sales	11,336	13,028
Total land, field, and runways	\$ 952,200	\$ 999,290
Hangar		
Space rental	\$ 47,502	\$ 51,988
Utility sales	30,759	31,371
Total hangar	\$ 78,261	\$ 83,359
Sky Harbor		
State aid for maintenance and operation	\$ 20,585	\$ 14,134
Rental income	22,225	16,507
Fuel sales	61,012	314
Percentage of lessees' sales	60	1,602
Other income	5,547	450
Total Sky Harbor	\$ 109,429	\$ 33,007
Total Operating Revenues	\$ 2,811,160	\$ 2,888,530

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

Schedule 2

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED DECEMBER 31, 2005

I. SUMMARY OF AUDITOR'S RESULTS

- A. Our report expresses an unqualified opinion on the basic financial statements of the Duluth Airport Authority.
- B. No matters involving internal control over financial reporting were 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*."
- C. No instances of noncompliance material to the financial statements of the Duluth Airport Authority were disclosed during the audit.
- D. No matters involving internal control over compliance relating to the audit of the major federal award program 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 and Passenger Facility Charge Programs."
- E. The Auditor's Report on Compliance for the major federal award program for the Duluth Airport Authority 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 program is:
 - Airport Improvement Program
 - CFDA #20.106
- H. The threshold for distinguishing between Types A and B programs was \$380,691.
- I. The Duluth Airport Authority was not determined to be a low-risk auditee.

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

None.

III. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARD PROGRAMS

None.

IV. FINDINGS – PASSENGER FACILITY CHARGE (PFC) REGULATIONS

None.

V. 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 Pension Plans*, which governs employer accounting and financial reporting for OPEB. These standards, like 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 the Authority 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 Authority 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 Authority Board determines that the establishment of a trust is desirable in order to fund the OPEB, the 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 Authority Board will have to decide whether to hire an actuary.

If applicable for the Duluth Airport Authority, GASB Statements 43 and 45 would be implemented for the years ended December 31, 2006 and 2007, respectively.

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OTHER REQUIRED REPORTS

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PATRICIA ANDERSON
STATE AUDITOR

**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***

Mayor and City Council
City of Duluth

Board of Directors
Duluth Airport Authority

We have audited the financial statements of the Duluth Airport Authority as of and for the year ended December 31, 2005, and have issued our report thereon dated March 30, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Duluth Airport Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

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

Minnesota Legal Compliance

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, the Duluth Airport Authority complied with the material terms and conditions of applicable legal provisions.

This report is intended solely for the information and use of the Board of Directors, management, 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/Pat Anderson

PATRICIA ANDERSON
STATE AUDITOR

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

End of Fieldwork: March 30, 2006



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PATRICIA ANDERSON
STATE AUDITOR

**REPORT ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR PROGRAM AND INTERNAL
CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB
CIRCULAR A-133 AND PASSENGER FACILITY CHARGE PROGRAMS**

Mayor and City Council
City of Duluth

Board of Directors
Duluth Airport Authority

Compliance

We have audited the compliance of the Duluth Airport Authority 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 its major federal program for the year ended December 31, 2005. The Duluth Airport Authority's major federal program is identified in the Summary of Auditor's Results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal program is the responsibility of the Authority's management. Our responsibility is to express an opinion on the Authority's compliance based on our audit.

We have also audited the Duluth Airport Authority's compliance with requirements applicable to its passenger facility charge (PFC) funds collected and expended for the year ended December 31, 2005. Compliance with the requirements of laws and regulations applicable to PFC funds is the responsibility of the Authority's management. Our responsibility is to express an opinion on the Authority'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*; and *Passenger Facility Charge Audit Guide for Public Agencies*, issued by the Federal Aviation

Administration (FAA). Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program or PFC program occurred. An audit includes examining, on a test basis, evidence about the Duluth Airport Authority's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Authority's compliance with those requirements.

In our opinion, the Duluth Airport Authority complied, in all material respects, with the requirements referred to above that are applicable to its major federal program and its PFC program for the year ended December 31, 2005.

Internal Control Over Compliance

The management of the Duluth Airport Authority is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal and PFC programs. In planning and performing our audit, we considered the Authority's internal control over compliance with requirements that could have a direct and material effect on a major federal program and on a PFC program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on the internal control over compliance in accordance with OMB Circular A-133 and the FAA's *Passenger Facility Charge Audit Guide for Public Agencies*.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program or PFC program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

Schedule of Expenditures of Federal Awards and Passenger Facility Charges Collected and Expended

We have audited the financial statements of the Duluth Airport Authority as of and for the year ended December 31, 2005, and have issued our report thereon dated March 30, 2006. Our audit was performed for the purpose of forming an opinion on the Duluth Airport Authority's basic financial statements. The accompanying Schedule of Expenditures of Federal Awards and Schedule of Passenger Facility Charges Collected and Expended are presented for purposes of additional analysis as required by OMB Circular A-133 and the FAA's *Passenger Facility Charge Audit Guide for Public Agencies* and are 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 Directors, management, 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/Pat Anderson

/s/Greg Hierlinger

PATRICIA ANDERSON
STATE AUDITOR

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

End of Fieldwork: March 30, 2006

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**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

Schedule 3

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2005**

Federal Grantor Pass-Through Agency Grant Program Title	Federal CFDA Number	Pass-Through Grant Number	Expenditures
Federal Aviation Administration			
Passed Through Minnesota Department of Transportation - Aeronautics			
AIP-3-27-0025-03	20.106	6901-134	\$ 3,437
AIP-3-27-0024-36	20.106	6901-141	56,492
AIP-3-27-0024-37	20.106	6901-142	4,018,814
AIP-3-27-0024-38	20.106	6901-144	2,678,527
AIP-3-27-0024-39	20.106	6901-147	1,982,426
AIP-3-27-0024-40	20.106	6901-149	984,866
Total CFDA No. 20.106			<u>\$ 9,724,562</u>
Department of Defense - National Guard Bureau			
Direct			
Military Construction Cooperative Agreement	12.401	W912LM-04-2-1051	\$ 41,122
Military Construction Cooperative Agreement	12.401	DAHA21-02-2-2101	1,084,621
Military Construction Cooperative Agreement	12.401	W912LM-05-2-1051	1,374,908
Military Construction Cooperative Agreement	12.401	W912LM-05-2-2101	342,858
Total CFDA No. 12.401			<u>\$ 2,843,509</u>
Department of Transportation			
Direct			
Small Community Air Service Development Pilot Program	20.93	DOT Order 2003-9-14	<u>\$ 106,912</u>
Department of Homeland Security			
Direct			
Port Security Research and Development Grant	97.06	HSTS04-05-A-DEP348	<u>\$ 14,719</u>
Total Expenditures of Federal Awards			<u>\$ 12,689,702</u>

Notes to Schedule of Expenditures of Federal Awards

1. The Schedule of Expenditures of Federal Awards presents the activity of federal award programs expended by the Duluth Airport Authority. The Authority's reporting entity is defined in Note 1 to the basic financial statements.
2. The expenditures on this schedule are on the accrual basis of accounting.
3. During 2005, the Duluth Airport Authority did not pass any federal money to subrecipients.

**DULUTH AIRPORT AUTHORITY
DULUTH, MINNESOTA**

Schedule 4

**SCHEDULE OF PASSENGER FACILITY CHARGES COLLECTED AND EXPENDED
FOR THE YEAR AND EACH QUARTER WITHIN THE YEAR ENDED DECEMBER 31, 2005**

<u>Application</u>	<u>1st Quarter</u>	<u>2nd Quarter</u>	<u>3rd Quarter</u>	<u>4th Quarter</u>	<u>Total</u>
Sixth Application*					
Balance - January 1					\$ 564,285
Collections***	\$ 3,014	\$ -	\$ -	\$ -	3,014
Expenses	(396,774)	-	-	-	(396,774)
Interest	56	-	-	-	56
Transfer of over-collection to seventh application	-	(170,581)	-	-	(170,581)
Balance - December 31					<u>\$ -</u>
Seventh Application**					
Balance - January 1					\$ -
Collections***	\$ -	\$ 99,014	\$ 148,029	\$ 80,264	327,307
Expended prior to effective date April 1, 2005					(673,011)
Expenses	-	(45,469)	(85,396)	(274,344)	(405,209)
Transfer of over-collection from sixth application	-	170,581	-	-	170,581
Balance - December 31					<u>\$ (580,332)</u>

*Federal Aviation Administration Record of Decision passenger facility charge effective date for Application Six is April 1, 2003.

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

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