

STATE OF MINNESOTA

Office of the State Auditor



Rebecca Otto
State Auditor

WATONWAN COUNTY
ST. JAMES, MINNESOTA

YEAR ENDED DECEMBER 31, 2006

Description of the Office of the State Auditor

The mission of the State Auditor's Office 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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**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

Year Ended December 31, 2006



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

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**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

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**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

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**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

**ORGANIZATION
2006**

<u>Office</u>	<u>Name</u>	<u>Term Expires</u>
Commissioners		
1st District	Dwayne Krenz	January 2009
2nd District	Noren Durheim*	January 2007
3rd District	William Berg	January 2009
4th District	Scott Sanders	January 2007
5th District	John Baerg	January 2009
Officers		
Elected		
Attorney	LaMar Piper	January 2007
Auditor	Donald Kuhlman	January 2007
County Recorder	Joy Sing	January 2007
Sheriff	Gary Menssen	January 2007
Treasurer	Carol F. Johnson	January 2007
Appointed		
Assessor	Noreen Curry	January 2009
Court Administrator (State)	Kelly Iverson	Indefinite
Coroner	R. A. Parsons, M.D.	January 2007
Highway Engineer	Roger Risser	May 2007
Probation Officer	Paul Harris	Indefinite
Veterans Service Officer	Deb Grote	Indefinite
Human Services Director	Richard Collins	Indefinite

*2006 Chair

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REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA

OFFICE OF THE STATE AUDITOR

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INDEPENDENT AUDITOR'S REPORT

Board of County Commissioners
Watonwan County

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

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. 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 audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information for Watonwan County as of December 31, 2006, and the respective changes in financial position thereof and the respective budgetary comparisons for the General Fund, Road and Bridge Special Revenue Fund, Human Services Special Revenue Fund, and County Ditch Special Revenue Fund for the year 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 principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming opinions on the financial statements that collectively comprise Watonwan County's basic financial statements. The combining and individual fund financial statements and schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements of Watonwan County. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly presented in all material respects in relation to the basic financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 24, 2007, on our consideration of Watonwan County's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

/s/Rebecca Otto

REBECCA OTTO
STATE AUDITOR

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

September 24, 2007

MANAGEMENT'S DISCUSSION AND ANALYSIS

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**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

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

INTRODUCTION

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

FINANCIAL HIGHLIGHTS

- The assets of Watonwan County exceeded its liabilities at the close of 2006 by \$42,659,316. Of this amount, \$3,679,837 (unrestricted net assets) may be used to meet Watonwan County's ongoing obligations to citizens and creditors.
- Watonwan County's total net assets increased by \$801,535 in 2006.
- At the close of 2006, Watonwan County's governmental funds reported combined ending fund balances of \$8,718,431, \$5,914,275 unreserved, of which approximately \$2,287,992 is available for spending at the County's discretion and is noted as unreserved, undesignated fund balance.
- At the close of 2006, unreserved fund balance for the General Fund was \$3,388,753, or 57 percent, of total General Fund expenditures.
- Watonwan County's total bonds and capital notes payable decreased by \$160,000, or three percent, during 2006. The key factor to this decrease was the payment of \$90,000 of bonds and \$70,000 of capital notes.

OVERVIEW OF THE FINANCIAL STATEMENTS

This Management's Discussion and Analysis is intended to serve as an introduction to Watonwan County's basic financial statements. Watonwan County's basic financial statements comprise three components: (1) County-wide financial statements, (2) fund financial statements, and (3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

County-Wide Financial Statements

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

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

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

The County-wide financial statements list the functions of Watonwan County principally supported by taxes and intergovernmental revenues. The governmental activities of Watonwan County include general government, public safety, highways and streets, sanitation, human services, health, culture and recreation, economic development, and conservation of natural resources. Watonwan County has no business-type activities intended to recover all or a significant portion of their costs through user fees and charges.

The County-wide financial statements can be found on Exhibits 1 and 2.

Fund Financial Statements

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

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

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

Watsonwan County reports five major funds and two nonmajor funds. The major funds are the General Fund, Road and Bridge Special Revenue Fund, Human Services Special Revenue Fund, County Ditch Special Revenue Fund, and Debt Service Fund. The nonmajor funds are the County Library Special Revenue Fund and Solid Waste Special Revenue Fund. Information is presented separately for the major funds and in total for the nonmajor funds in Exhibits 3 and 4.

Fiduciary funds are used to account for assets held by the County as an agent for individuals, private organizations, other governments, or other funds. Watsonwan County's fiduciary funds consist of three agency funds. Agency funds are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations. In addition, the agency funds are not reflected in the County-wide financial statements because those resources are not available to support the County's programs.

Watsonwan County's governmental fund financial statements are on Exhibits 3 to 8, and Watsonwan County's fiduciary funds are on Exhibit 9.

Notes to the Financial Statements

Notes to the financial statements provide additional information that is essential to a full understanding of the data provided.

Other Information

In addition to the basic financial statements and notes, Watsonwan County also provides supplementary information on intergovernmental revenues (Schedule 1).

Watsonwan County adopts an annual appropriated budget for its General Fund, special revenue funds, and the Debt Service Fund. Budgetary comparison statements have been provided for the County's major funds to demonstrate compliance with these budgets.

County-Wide Financial Analysis

Over time, net assets serve as a useful indicator of the County's financial position. Watonwan County's assets exceeded liabilities by \$42,659,316 at the close of 2006. The largest portion of Watonwan County's net assets (83.7 percent) reflects its investment in capital assets (for example, land, buildings, and equipment), less any related debt used to acquire those assets that is still outstanding. However, it should be noted that these assets are not available for future spending.

Governmental Net Assets

	2006	2005
Current and other assets	\$ 11,532,823	\$ 12,311,024
Capital assets	38,764,259	37,382,307
Total Assets	\$ 50,297,082	\$ 49,693,331
Long-term liabilities outstanding	\$ 6,788,488	\$ 6,901,187
Other liabilities	849,278	934,363
Total Liabilities	\$ 7,637,766	\$ 7,835,550
Net Assets		
Invested in capital assets - net of related debt	\$ 35,715,239	\$ 34,950,407
Restricted	3,264,240	4,253,687
Unrestricted	3,679,837	2,653,687
Total Net Assets	\$ 42,659,316	\$ 41,857,781

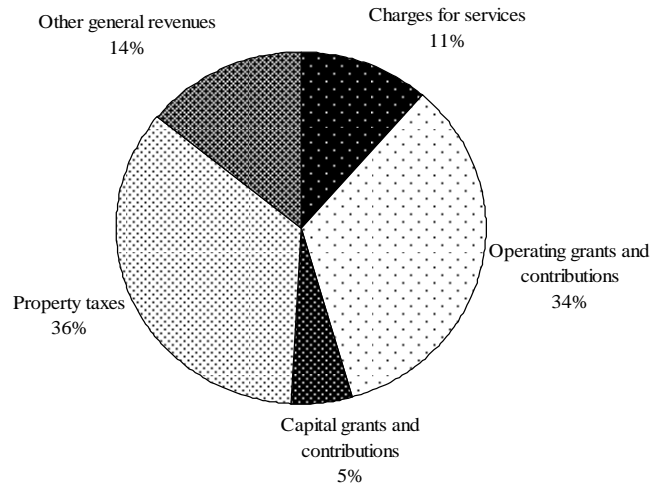
The unrestricted net asset amount of \$3,679,837 as of December 31, 2006, may be used to meet the County's ongoing obligations to citizens and creditors.

Governmental Activities

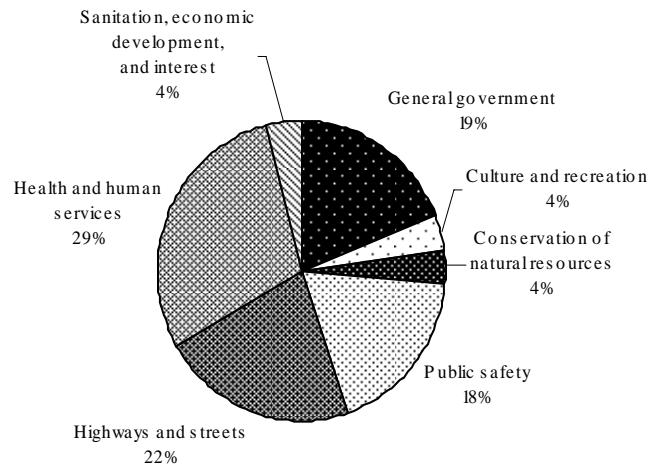
The following table summarizes the changes in net assets for 2006.

	2006	2005
Revenues		
Program revenues		
Charges for services	\$ 1,700,038	\$ 2,004,991
Operating grants and contributions	5,088,557	4,761,761
Capital grants and contributions	797,995	329,156
General revenues		
Property taxes	5,221,875	4,926,186
Other	2,099,545	1,979,710
Total Revenues	<u>\$ 14,908,010</u>	<u>\$ 14,001,804</u>
Expenses		
General government	\$ 2,676,460	\$ 2,526,432
Public safety	2,600,526	1,632,703
Highways and streets	3,086,433	3,024,976
Sanitation	132,179	171,732
Human services	3,741,877	3,709,839
Health	428,952	406,683
Culture and recreation	531,002	564,683
Conservation of natural resources	502,677	717,619
Economic development	146,200	141,815
Interest	260,169	240,982
Total Expenses	<u>\$ 14,106,475</u>	<u>\$ 13,137,464</u>
Increase in Net Assets	\$ 801,535	\$ 864,340
Net Assets - January 1	<u>41,857,781</u>	<u>40,993,441</u>
Net Assets - December 31	<u>\$ 42,659,316</u>	<u>\$ 41,857,781</u>

SOURCES OF COUNTY REVENUES



WHERE COUNTY FUNDS ARE SPENT



(Unaudited)

FINANCIAL ANALYSIS OF THE COUNTY'S FUNDS

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

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

As of the end of the current fiscal year, the County's governmental funds reported combined ending fund balances of \$8,718,431. The majority of this amount (\$5,914,275) constitutes unreserved fund balance. The remainder of fund balance is reserved to indicate this it is not available for new spending because it has already been committed for various reasons.

The General Fund is the chief operating fund of Watonwan County. At the end of the current fiscal year, the unreserved fund balance of the General Fund was \$3,388,753, while the total fund balance was \$3,762,823. As a measure of the General Fund's liquidity, it may be useful to compare unreserved fund balance and total fund balance to annual expenditures. Unreserved fund balance represents 56.6 percent of total General Fund expenditures for 2006, while total fund balance represents 62.9 percent of total General Fund expenditures. In 2006, the total fund balance in the General Fund decreased by \$222,688, with unreserved fund balances increasing by \$414,362 and reserved fund balances decreasing by \$637,050. The primary reasons for the increase in unreserved fund balance were increased interest earnings, dividends from the Minnesota Counties Insurance Trust and ISTS loans from the Minnesota Pollution Control Agency. The primary reason for the decrease in reserved fund balance was the completion of the jail project using proceeds from the bond sale in 2005.

The Road and Bridge Special Revenue Fund's fund balance decreased by \$174,076 in 2006. The main reason for the decrease was increased operation costs due to the price of petroleum and related products.

In 2006, the Human Services Special Revenue Fund's fund balance decreased by \$223,621. This was primarily due to an unforeseen increase in Social Services costs.

General Fund Budgetary Highlights

The largest variances were in miscellaneous revenue which was due to a dividend from workers' compensation and property/casualty insurance and an increase in interest earnings. On the expenditure side, actual expenditures were \$95,309 less than budgeted. This is a result of many small savings and is less than a two percent variance.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

The County's investment in capital assets for its governmental activities as of December 31, 2006, amount to \$38,764,259 (net of accumulated depreciation). This investment in capital assets includes land, buildings, equipment, and infrastructure. The total increase in the County's investment in capital assets for the current fiscal year was 3.7 percent. The major capital asset event in 2006 was additional infrastructure additions (primarily bridges and County State-Aid Highway roads).

Governmental Capital Assets (Net of Depreciation)		
	2006	2005
Land	\$ 695,771	\$ 695,771
Construction in progress	833,903	387,631
Land improvements	36,865	39,321
Buildings and improvements	5,106,320	5,271,643
Machinery, furniture, and equipment	1,942,591	1,907,739
Infrastructure	30,148,809	29,080,202
Total	<u>\$ 38,764,259</u>	<u>\$ 37,382,307</u>

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

Long-Term Debt

At the end of the current fiscal year, the County had total bonded debt and capital notes outstanding of \$5,083,392, which is backed by the full faith and credit of the government. Watonwan County's bonds are not rated.

Governmental Outstanding Debt		
	2006	2005
General obligation bonds and capital notes	<u>\$ 5,083,392</u>	<u>\$ 5,240,606</u>

The County's debt decreased by \$157,214 during the fiscal year, which was due to payments made for bonds and capital notes during the year.

Minnesota statutes limit the amount of debt that a county may levy to two percent of its total market value. As of the end of 2006, Watonwan County is well below the two percent debt limit imposed by state statutes.

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

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS

- Watonwan County's unemployment rate was 4.4 percent as of the end of 2006. This is slightly higher than the state-wide rate of 4.2 percent.
- Both housing and farm land values have continued to increase in 2006.

At the end of 2006, Watonwan County set its 2007 revenue and expenditure budgets. In doing so, it has appropriated \$76,454 from available fund balance to offset the difference between 2007 budgeted revenues and expenditures of \$14,382,005 and \$14,458,459, respectively.

During 2006, Watonwan County's net assets increased by \$801,535. This increase was primarily due to an increase in the County's infrastructure (roads and bridges). Also, a grant from the federal government for \$168,000 was received to purchase elections computer equipment.

REQUESTS FOR INFORMATION

This annual financial report is designed to provide a general overview of the County's finances for all those with an interest in the County's finances. Questions concerning any information provided in this report, or requests for additional financial information, should be addressed to the Watonwan County Auditor, Watonwan County Courthouse, 710 Second Avenue South, P. O. Box 518, St. James, Minnesota 56081.

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BASIC FINANCIAL STATEMENTS

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COUNTY-WIDE FINANCIAL STATEMENTS

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**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

EXHIBIT 1

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

Assets

Cash and pooled investments	\$ 6,868,797
Cash with fiscal agent	2,011,981
Taxes receivable	
Prior	103,478
Special assessments receivable	
Prior	22,268
Noncurrent	849,317
Accounts receivable	204,219
Accrued interest receivable	86,585
Due from other governments	1,193,433
Inventories	158,222
Deferred debt issue costs	34,523
Capital assets	
Non-depreciable	1,529,674
Depreciable - net of accumulated depreciation	37,234,585
	<hr/>
Total Assets	\$ 50,297,082

Liabilities

Accounts payable	\$ 192,468
Salaries payable	151,900
Due to other governments	58,532
Accrued interest payable	100,850
Unearned revenue	46,197
Advance from other governments	299,331
Long-term liabilities	
Due within one year	2,687,983
Due in more than one year	4,100,505
	<hr/>
Total Liabilities	\$ 7,637,766

Net Assets

Invested in capital assets - net of related debt	\$ 35,715,239
Restricted for	
General government	64,149
Public safety	58,251
Highways and streets	554,553
Culture and recreation	155,137
Conservation of natural resources	74,954
Debt service	2,349,134
Economic development	8,062
Unrestricted	3,679,837
	<hr/>
Total Net Assets	\$ 42,659,316

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

EXHIBIT 2

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

			Program Revenues		Net (Expense)
		Fees, Charges, Fines, and Other	Operating Grants and Contributions	Capital Grants and Contributions	Revenue and Change in Net Assets
	Expenses				
Functions/Programs					
Governmental activities					
General government	\$ 2,676,460	\$ 443,813	\$ 202,824	\$ 210,520	\$ (1,819,303)
Public safety	2,600,526	169,022	242,253	-	(2,189,251)
Highways and streets	3,086,433	165,336	2,346,965	587,475	13,343
Sanitation	132,179	139,388	49,079	-	56,288
Human services	3,741,877	355,720	1,813,445	-	(1,572,712)
Health	428,952	17,235	243,737	-	(167,980)
Culture and recreation	531,002	26,026	3,220	-	(501,756)
Conservation of natural resources	502,677	297,372	187,034	-	(18,271)
Economic development	146,200	86,126	-	-	(60,074)
Interest	260,169	-	-	-	(260,169)
Total governmental activities	\$ 14,106,475	\$ 1,700,038	\$ 5,088,557	\$ 797,995	\$ (6,519,885)
General Revenues					
Property taxes					\$ 5,221,875
Mortgage registry and deed tax					8,592
Grants and contributions not restricted to specific programs					1,624,630
Payments in lieu of taxes					15,993
Investment income					326,065
Miscellaneous					124,265
Total general revenues					\$ 7,321,420
Change in net assets					\$ 801,535
Net Assets - January 1					41,857,781
Net Assets - December 31					\$ 42,659,316

FUND FINANCIAL STATEMENTS

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

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

	<u>General</u>	<u>Road and Bridge</u>
<u>Assets</u>		
Cash and pooled investments	\$ 3,669,331	\$ 485,902
Cash with fiscal agent	-	-
Taxes receivable		
Prior	61,024	9,129
Special assessments receivable		
Prior	8,917	-
Noncurrent	699,085	16,628
Accounts receivable	13,208	1,002
Accrued interest receivable	84,225	-
Due from other funds	19,775	21,338
Due from other governments	28,300	527,802
Inventories	-	158,222
Advances to other funds	153,575	-
	<hr/>	<hr/>
Total Assets	<u>\$ 4,737,440</u>	<u>\$ 1,220,023</u>

EXHIBIT 3

Human Services	County Ditch	Debt Service	Other Governmental Funds	Total Governmental Funds
\$ 1,269,475	\$ 256,782	\$ 325,837	\$ 861,470	\$ 6,868,797
-	-	2,011,981	-	2,011,981
22,097	-	4,624	6,604	103,478
-	17	-	13,334	22,268
-	133,604	-	-	849,317
190,009	-	-	-	204,219
-	-	-	2,360	86,585
-	-	-	-	41,113
402,909	17,422	217,000	-	1,193,433
-	-	-	-	158,222
-	-	-	-	153,575
\$ 1,884,490	\$ 407,825	\$ 2,559,442	\$ 883,768	\$ 11,692,988

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

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

	<u>General</u>	<u>Road and Bridge</u>
<u>Liabilities and Fund Balances</u>		
Liabilities		
Accounts payable	\$ 60,135	\$ 27,704
Salaries payable	63,844	25,668
Due to other funds	19,064	-
Due to other governments	30,841	139
Deferred revenue - unavailable	755,160	545,650
Deferred revenue - unearned	45,573	167
Advance from other funds	-	-
Advance from other governments	-	299,331
	<hr/>	<hr/>
Total Liabilities	\$ 974,617	\$ 898,659
	<hr/>	<hr/>
Fund Balances		
Reserved for		
Debt service	\$ -	\$ -
Inventories	-	158,222
Law library	44,125	-
Recorder's equipment	2,475	-
HAVA	3,456	-
E-911	50,252	-
Sheriff's contingency	7,999	-
Highway projects	-	104,746
Future projects	14,093	-
Donations	-	-
ISTS loans	212,534	-
Water plan	31,074	-
HRA special benefits levy	8,062	-
Unreserved		
Designated for cash flows	1,685,342	-
Designated for compensated absences	342,046	58,396
Designated for debt service	-	-
Undesignated	1,361,365	-
Unreserved, reported in nonmajor special revenue funds	<hr/>	<hr/>
	-	-
Total Fund Balances	\$ 3,762,823	\$ 321,364
	<hr/>	<hr/>
Total Liabilities and Fund Balances	\$ 4,737,440	\$ 1,220,023
	<hr/>	<hr/>

EXHIBIT 3
(Continued)

Human Services	County Ditch	Debt Service	Other Governmental Funds	Total Governmental Funds
\$ 86,479	\$ -	\$ -	\$ 18,150	\$ 192,468
55,688	-	-	6,700	151,900
19,775	1,752	-	522	41,113
11,285	16,267	-	-	58,532
373,422	133,621	210,261	13,327	2,031,441
317	-	47	93	46,197
-	153,575	-	-	153,575
-	-	-	-	299,331
\$ 546,966	\$ 305,215	\$ 210,308	\$ 38,792	\$ 2,974,557
\$ -	\$ -	\$ 2,011,981	\$ -	\$ 2,011,981
-	-	-	-	158,222
-	-	-	-	44,125
-	-	-	-	2,475
-	-	-	-	3,456
-	-	-	-	50,252
-	-	-	-	7,999
-	-	-	-	104,746
-	-	-	-	14,093
-	-	-	155,137	155,137
-	-	-	-	212,534
-	-	-	-	31,074
-	-	-	-	8,062
954,534	-	-	-	2,639,876
248,812	-	-	-	649,254
-	-	337,153	-	337,153
134,178	102,610	-	-	1,598,153
-	-	-	689,839	689,839
\$ 1,337,524	\$ 102,610	\$ 2,349,134	\$ 844,976	\$ 8,718,431
\$ 1,884,490	\$ 407,825	\$ 2,559,442	\$ 883,768	\$ 11,692,988

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**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

EXHIBIT 3A

**RECONCILIATION OF THE FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF NET ASSETS
DECEMBER 31, 2006**

Fund balances - total governmental funds (Exhibit 3)		\$ 8,718,431
Amounts reported for governmental activities in the statement of net assets are different because:		
Capital assets, net of accumulated depreciation, used in governmental activities are not financial resources and, therefore, are not reported in the governmental funds.		38,764,259
Other long-term assets are not available to pay for current period expenditures and, therefore, are deferred in the governmental funds.		2,031,441
Long-term liabilities are not due and payable in the current period and, therefore, are not reported in the governmental funds.		
General obligation bonds	\$ (5,055,000)	
Capital notes	(70,000)	
Accrued interest payable	(100,850)	
Deferred debt issue costs	34,523	
Discount on bonds	41,608	
Loans payable	(874,695)	
Compensated absences	(830,401)	
		<u>(6,854,815)</u>
Net assets of governmental activities (Exhibit 1)		<u>\$ 42,659,316</u>

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

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

	<u>General</u>	<u>Road and Bridge</u>
Revenues		
Taxes	\$ 2,712,733	\$ 560,326
Special assessments	122,960	9,872
Licenses and permits	25,323	-
Intergovernmental	1,711,017	3,446,714
Charges for services	656,224	261,889
Fines and forfeits	4,195	-
Gifts and contributions	-	-
Investment earnings	250,117	-
Miscellaneous	211,643	155,384
Total Revenues	\$ 5,694,212	\$ 4,434,185
Expenditures		
Current		
General government	\$ 2,760,427	\$ -
Public safety	1,728,183	-
Highways and streets	-	4,720,097
Sanitation	-	-
Human services	-	-
Health	-	-
Culture and recreation	48,325	-
Conservation of natural resources	458,933	-
Economic development	145,273	-
Capital outlay	788,812	-
Debt service		
Principal	45,702	-
Interest	8,154	-
Administrative charges	-	-
Total Expenditures	\$ 5,983,809	\$ 4,720,097
Excess of Revenues Over (Under) Expenditures	\$ (289,597)	\$ (285,912)
Other Financing Sources (Uses)		
Transfers in	\$ 92,756	\$ 111,533
Transfers out	(121,332)	-
Proceeds from loans	95,485	-
Total Other Financing Sources (Uses)	\$ 66,909	\$ 111,533
Net Change in Fund Balances	\$ (222,688)	\$ (174,379)
Fund Balances - January 1	3,985,511	495,440
Increase (decrease) in reserved for inventories	-	303
Fund Balances - December 31	\$ 3,762,823	\$ 321,364

EXHIBIT 4

Human Services	County Ditch	Debt Service	Other Governmental Funds	Total Governmental Funds
\$ 1,330,955	\$ -	\$ 278,909	\$ 398,293	\$ 5,281,216
-	126,824	-	132,325	391,981
-	-	-	-	25,323
2,308,264	-	55,870	176,171	7,698,036
175,212	-	-	4,283	1,097,608
-	-	-	8,152	12,347
-	-	-	3,220	3,220
-	-	75,948	6,960	333,025
224,369	-	-	7,820	599,216
\$ 4,038,800	\$ 126,824	\$ 410,727	\$ 737,224	\$ 15,441,972
\$ -	\$ -	\$ -	\$ -	\$ 2,760,427
-	-	-	-	1,728,183
-	-	-	-	4,720,097
-	-	-	137,197	137,197
3,744,507	-	-	-	3,744,507
425,158	-	-	-	425,158
-	-	-	497,361	545,686
-	91,658	-	-	550,591
-	-	-	-	145,273
-	-	-	-	788,812
-	-	160,000	-	205,702
-	8,139	241,051	-	257,344
-	-	1,346	-	1,346
\$ 4,169,665	\$ 99,797	\$ 402,397	\$ 634,558	\$ 16,010,323
\$ (130,865)	\$ 27,027	\$ 8,330	\$ 102,666	\$ (568,351)
\$ -	\$ 7,198	\$ -	\$ 2,601	\$ 214,088
(92,756)	-	-	-	(214,088)
-	-	-	-	95,485
\$ (92,756)	\$ 7,198	\$ -	\$ 2,601	\$ 95,485
\$ (223,621)	\$ 34,225	\$ 8,330	\$ 105,267	\$ (472,866)
1,561,145	68,385	2,340,804	739,709	9,190,994
-	-	-	-	303
\$ 1,337,524	\$ 102,610	\$ 2,349,134	\$ 844,976	\$ 8,718,431

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

EXHIBIT 4A

**RECONCILIATION OF THE CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2006**

Net change in fund balances - total governmental funds (Exhibit 4)	\$	(472,866)
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Amounts reported for governmental activities in the statement of activities are different because:

Governmental funds report capital outlay as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.

Capital outlay expenditures	\$ 2,756,315	
Depreciation expense	<u>(1,374,363)</u>	1,381,952

Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.

Decrease in deferred revenue for taxes and special assessments	\$ (27,449)	
Decrease in deferred revenue for grants and allotments	<u>(194,411)</u>	(221,860)

The issuance of long-term debt (such as bonds or loans) provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. Neither transaction, however, has any effect on net assets. Also, governmental funds report the net effect of issuance costs and discounts when debt is issued; these amounts are deferred and amortized over the life of the debt in the statement of activities.

Proceeds of loans issued	\$ (95,485)	
Repayment of debt principal	205,702	
Amortization of discount on debt and issuance costs	<u>(4,929)</u>	105,288

Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds.

Change in inventories	\$ 303	
Change in accrued interest payable	3,450	
Change in compensated absences	<u>5,268</u>	<u>9,021</u>

Change in net assets of governmental activities (Exhibit 2)	\$	<u>801,535</u>
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**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

EXHIBIT 5

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

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Revenues				
Taxes	\$ 2,967,825	\$ 2,655,270	\$ 2,712,733	\$ 57,463
Special assessments	-	-	122,960	122,960
Licenses and permits	10,710	10,710	25,323	14,613
Intergovernmental	1,293,442	1,605,997	1,711,017	105,020
Charges for services	641,137	641,137	656,224	15,087
Fines and forfeits	1,000	1,000	4,195	3,195
Investment earnings	110,000	110,000	250,117	140,117
Miscellaneous	88,028	88,028	211,643	123,615
Total Revenues	\$ 5,112,142	\$ 5,112,142	\$ 5,694,212	\$ 582,070
Expenditures				
Current				
General government				
Commissioners	\$ 181,728	\$ 181,728	\$ 192,182	\$ (10,454)
Courts	20,000	20,000	20,511	(511)
Law library	12,000	12,000	15,985	(3,985)
Victim witness coordinator	42,000	42,000	44,052	(2,052)
Drug court	-	-	17,451	(17,451)
County auditor	207,283	207,283	207,005	278
License bureau	87,322	87,322	86,168	1,154
County treasurer	122,758	122,758	116,123	6,635
County assessor	224,149	224,149	221,753	2,396
Elections	180,050	180,050	188,666	(8,616)
Central services	146,038	146,038	139,604	6,434
Personnel	71,909	71,909	74,762	(2,853)
Information services	79,398	79,398	72,909	6,489
Attorney	221,594	221,594	217,330	4,264
Recorder	162,512	162,512	164,850	(2,338)
Surveyor	4,000	4,000	-	4,000
Buildings and plant	243,825	243,825	242,133	1,692
Transit	273,726	273,726	277,994	(4,268)
Veterans service officer	84,664	84,664	75,679	8,985
Appropriations - general government	4,050	4,050	4,050	-
Other general government	366,912	366,912	381,220	(14,308)
Total general government	\$ 2,735,918	\$ 2,735,918	\$ 2,760,427	\$ (24,509)
Public safety				
Sheriff	\$ 1,117,360	\$ 1,117,360	\$ 1,055,802	\$ 61,558
Emergency services	46,724	46,724	32,444	14,280
Coroner	7,800	7,800	4,518	3,282
County jail	423,898	423,898	456,309	(32,411)
Probation and parole	228,189	228,189	179,110	49,079
Total public safety	\$ 1,823,971	\$ 1,823,971	\$ 1,728,183	\$ 95,788

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

**EXHIBIT 5
(Continued)**

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

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Expenditures				
Current (Continued)				
Culture and recreation				
Historical society	\$ 30,900	\$ 30,900	\$ 30,900	\$ -
Parks	29,500	29,500	17,425	12,075
Total culture and recreation	\$ 60,400	\$ 60,400	\$ 48,325	\$ 12,075
Conservation of natural resources				
Cooperative extension	\$ 73,247	\$ 73,247	\$ 73,835	\$ (588)
Soil and water conservation	46,500	46,500	46,500	-
Agricultural society/County fair	39,800	39,800	35,193	4,607
Water planning	70,740	70,740	60,720	10,020
CWP project	140,000	140,000	48,522	91,478
Environmental services	85,693	85,693	91,128	(5,435)
Septic loan program	-	-	103,035	(103,035)
Total conservation of natural resources	\$ 455,980	\$ 455,980	\$ 458,933	\$ (2,953)
Economic development				
Job training and employment	\$ 88,837	\$ 88,837	\$ 86,340	\$ 2,497
Appropriations - economic development	7,012	7,012	7,012	-
Other	51,500	51,500	51,921	(421)
Total economic development	\$ 147,349	\$ 147,349	\$ 145,273	\$ 2,076
Capital outlay				
General government	\$ 55,500	\$ 55,500	\$ 37,992	\$ 17,508
Public safety	\$ 800,000	\$ 800,000	\$ 750,820	\$ 49,180
Debt service				
Principal	\$ -	\$ -	\$ 45,702	\$ (45,702)
Interest	\$ -	\$ -	\$ 8,154	\$ (8,154)
Total Expenditures	\$ 6,079,118	\$ 6,079,118	\$ 5,983,809	\$ 95,309
Excess of Revenues Over (Under) Expenditures	\$ (966,976)	\$ (966,976)	\$ (289,597)	\$ 677,379

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

***EXHIBIT 5
(Continued)***

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

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Other Financing Sources (Uses)				
Transfers in	\$ 92,000	\$ 92,000	\$ 92,756	\$ 756
Transfers out	(100,000)	(100,000)	(121,332)	(21,332)
Proceeds from loans	-	-	95,485	95,485
Total Other Financing Sources (Uses)	\$ (8,000)	\$ (8,000)	\$ 66,909	\$ 74,909
Net Change in Fund Balance	\$ (974,976)	\$ (974,976)	\$ (222,688)	\$ 752,288
Fund Balance - January 1	3,985,511	3,985,511	3,985,511	-
Fund Balance - December 31	\$ 3,010,535	\$ 3,010,535	\$ 3,762,823	\$ 752,288

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

EXHIBIT 6

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

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Revenues				
Taxes	\$ 629,089	\$ 560,842	\$ 560,326	\$ (516)
Special assessments	-	-	9,872	9,872
Intergovernmental	3,083,380	3,151,627	3,446,714	295,087
Charges for services	234,600	234,600	261,889	27,289
Miscellaneous	391,700	391,700	155,384	(236,316)
Total Revenues	\$ 4,338,769	\$ 4,338,769	\$ 4,434,185	\$ 95,416
Expenditures				
Current				
Highways and streets				
Administration	\$ 380,107	\$ 380,107	\$ 382,769	\$ (2,662)
Maintenance	1,052,360	1,052,360	1,345,289	(292,929)
Construction	1,578,541	1,578,541	1,848,500	(269,959)
Equipment maintenance and shop	953,055	953,055	929,626	23,429
Other	162,616	162,616	213,913	(51,297)
Total Expenditures	\$ 4,126,679	\$ 4,126,679	\$ 4,720,097	\$ (593,418)
Excess of Revenues Over (Under)				
Expenditures	\$ 212,090	\$ 212,090	\$ (285,912)	\$ (498,002)
Other Financing Sources (Uses)				
Transfers in	8,000	8,000	111,533	103,533
Net Change in Fund Balance	\$ 220,090	\$ 220,090	\$ (174,379)	\$ (394,469)
Fund Balance - January 1	495,440	495,440	495,440	-
Increase (decrease) in reserved for inventories	-	-	303	303
Fund Balance - December 31	\$ 715,530	\$ 715,530	\$ 321,364	\$ (394,166)

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

EXHIBIT 7

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

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Revenues				
Taxes	\$ 1,493,804	\$ 1,330,360	\$ 1,330,955	\$ 595
Intergovernmental	2,157,994	2,321,438	2,308,264	(13,174)
Charges for services	122,850	122,850	175,212	52,362
Miscellaneous	271,900	271,900	224,369	(47,531)
Total Revenues	\$ 4,046,548	\$ 4,046,548	\$ 4,038,800	\$ (7,748)
Expenditures				
Current				
Human services				
Income maintenance	\$ 903,662	\$ 903,662	\$ 895,737	\$ 7,925
Social services	2,730,714	2,730,714	2,848,770	(118,056)
Total human services	\$ 3,634,376	\$ 3,634,376	\$ 3,744,507	\$ (110,131)
Health				
Community health services	478,893	478,893	425,158	53,735
Total Expenditures	\$ 4,113,269	\$ 4,113,269	\$ 4,169,665	\$ (56,396)
Excess of Revenues Over (Under) Expenditures	\$ (66,721)	\$ (66,721)	\$ (130,865)	\$ (64,144)
Other Financing Sources (Uses)				
Transfers out	-	-	(92,756)	(92,756)
Net Change in Fund Balance	\$ (66,721)	\$ (66,721)	\$ (223,621)	\$ (156,900)
Fund Balance - January 1	1,561,145	1,561,145	1,561,145	-
Fund Balance - December 31	\$ 1,494,424	\$ 1,494,424	\$ 1,337,524	\$ (156,900)

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

EXHIBIT 8

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

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Revenues				
Special assessments	\$ 102,000	\$ 102,000	\$ 126,824	\$ 24,824
Expenditures				
Current				
Conservation of natural resources				
Other (ditch repairs)	\$ 102,000	\$ 102,000	\$ 91,658	\$ 10,342
Debt service				
Interest	-	-	8,139	(8,139)
Total Expenditures	\$ 102,000	\$ 102,000	\$ 99,797	\$ 2,203
Excess of Revenues Over (Under)				
Expenditures	\$ -	\$ -	\$ 27,027	\$ 27,027
Other Financing Sources (Uses)				
Transfers in	-	-	7,198	7,198
Net Change in Fund Balance	\$ -	\$ -	\$ 34,225	\$ 34,225
Fund Balance - January 1	68,385	68,385	68,385	-
Fund Balance - December 31	\$ 68,385	\$ 68,385	\$ 102,610	\$ 34,225

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

EXHIBIT 9

**STATEMENT OF FIDUCIARY NET ASSETS
AGENCY FUNDS
DECEMBER 31, 2006**

<u>Assets</u>	
Cash and pooled investments	<u><u>\$ 219,169</u></u>
<u>Liabilities</u>	
Due to other governments	<u><u>\$ 219,169</u></u>

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**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

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

1. Summary of Significant Accounting Policies

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

A. Financial Reporting Entity

Watonwan County was established February 25, 1860, and is an organized county having the powers, duties, and privileges granted counties by Minn. Stat. ch. 373. The County is governed by a five-member Board of Commissioners elected from districts within the County. The Board is organized with a chair and vice chair elected at the annual meeting in January of each year.

Joint Ventures

The County participates in joint ventures described in Note 5.B. The County also participates in jointly-governed organizations described in Note 5.C.

B. Basic Financial Statements

1. County-Wide Statements

The County-wide financial statements (the statement of net assets and the statement of activities) display information about the County. These statements include the financial activities of the overall County government, except for fiduciary activities. Eliminations have been made to minimize the double counting of internal activities.

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

1. Summary of Significant Accounting Policies

B. Basic Financial Statements

1. County-Wide Statements (Continued)

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

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

2. Fund Financial Statements

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

The County reports the following major governmental funds:

The General Fund is the County's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

1. Summary of Significant Accounting Policies

B. Basic Financial Statements

2. Fund Financial Statements (Continued)

The Road and Bridge Special Revenue Fund is used to account for revenues and expenditures of the County Highway Department, which is responsible for the construction and maintenance of roads, bridges, and other projects affecting County roadways.

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

The County Ditch Special Revenue Fund is used to account for the operations of the County ditch system. Financing is provided by assessing benefited property owners.

The Debt Service Fund is used to account for the revenues and expenditures related to the County's debt activity.

Additionally, the County reports the following fund types:

Special revenue funds are used to account for the proceeds of specific revenue sources (other than major capital projects) that are legally restricted to expenditures for specified purposes.

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

C. Measurement Focus and Basis of Accounting

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

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

1. Summary of Significant Accounting Policies

C. Measurement Focus and Basis of Accounting (Continued)

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

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

D. Assets, Liabilities, and Net Assets or Equity

1. Deposits and Investments

The cash balances of substantially all funds are pooled and invested by the County Treasurer for the purpose of increasing earnings through investment activities. Pooled and fund investments are reported at their fair value at December 31, 2006, based on market prices. Pursuant to Minn. Stat. § 385.07, investment earnings on cash and pooled investments are credited to the General Fund. Pooled investment earnings for 2006 were \$250,117.

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

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Assets or Equity

1. Deposits and Investments (Continued)

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

- (1) securities which are direct obligations or are guaranteed or insured issues of the United States, its agencies, its instrumentalities, or organizations created by an act of Congress, except mortgage-backed securities defined as “high risk” by Minn. Stat. § 118A.04, subd. 6;
- (2) mutual funds through shares of registered investment companies provided the mutual fund receives certain ratings depending on its investments;
- (3) general obligations of the State of Minnesota and its municipalities, and in certain state agency and local obligations of Minnesota and other states provided such obligations have certain specified bond ratings by a national bond rating service;
- (4) bankers’ acceptances of United States banks;
- (5) commercial paper issued by United States corporations or their Canadian subsidiaries that is rated in the highest quality category by two nationally recognized rating agencies and matures in 270 days or less; and
- (6) with certain restrictions, in repurchase agreements, securities lending agreements, joint powers investment trusts, and guaranteed investment contracts.

Investments of the County are reported at fair value.

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

1. Summary of Significant Accounting Policies

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

2. Receivables and Payables

Activities between funds representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as “advances to/from other funds.” All other outstanding balances between funds are reported as “due to/from other funds.”

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

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

3. Inventories

The Road and Bridge Special Revenue Fund inventory is valued using the weighted average method. Inventories in governmental funds are recorded as expenditures at the time the item is purchased. Inventories at the County-wide level are reported as expenses when consumed.

Inventories, as reported in the fund financial statements, are offset by a fund balance reserve to indicate that they do not constitute available spendable resources.

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

1. Summary of Significant Accounting Policies

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

4. Capital Assets

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

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed.

Capital assets of the County are depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Buildings	25 - 50
Improvements other than buildings	20
Machinery, furniture, and equipment	5 - 20
Infrastructure	50 - 75

5. Compensated Absences

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

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

1. Summary of Significant Accounting Policies

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

6. Deferred Revenue

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

7. Long-Term Obligations

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

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

8. Fund Equity

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

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

1. Summary of Significant Accounting Policies

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

9. Use of Estimates

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

2. Stewardship, Compliance, and Accountability

A. Budgetary Information

Annual budgets are adopted on a basis consistent with generally accepted accounting principles for all major governmental funds and nonmajor special revenue funds. All annual appropriations lapse at year-end.

On or before mid-August of each year, all departments submit requests for appropriations to the County Auditor so that a budget can be prepared. Before October 31, the proposed budget is presented to the County Board for review. The Board holds public hearings, and a final budget must be prepared and adopted no later than December 31.

The appropriated budget is prepared by fund, function, and department. Transfers of appropriations within a department and between departments require approval of the County Board. The legal level of budgetary control--the level at which expenditures may not legally exceed appropriations--is the fund level. The Board made a budget adjustment for the bond sale proceeds as well as some immaterial adjustments.

Encumbrance accounting is employed in governmental funds. Encumbrances outstanding at year-end are reported as reservations of fund balances and do not constitute expenditures or liabilities because the commitments will be re-apportioned and honored during the subsequent year.

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

2. Stewardship, Compliance, and Accountability (Continued)

B. Excess of Expenditures Over Budget

The funds shown below had expenditures in excess of budget for the year ended December 31, 2006.

	<u>Expenditures</u>		<u>Budget</u>		<u>Excess</u>
Road and Bridge Special Revenue Fund	\$ 4,720,097		\$ 4,126,679		\$ 593,418
Human Services Special Revenue Fund	4,169,665		4,113,269		56,396
Debt Service Fund	402,397		288,245		114,152

The excess of expenditures over budget was funded by unanticipated revenues and available fund balance.

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

The County's total cash and investments are as follows:

Governmental funds	
Cash and pooled investments	\$ 6,868,797
Cash with fiscal agent	2,011,981
Fiduciary funds	
Cash and pooled investments	
Agency funds	<u>219,169</u>
Total Cash and Investments	<u>\$ 9,099,947</u>

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments (Continued)

a. Deposits

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

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

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a financial institution failure, the County's deposits may not be returned to it. It is County policy to minimize custodial credit risk of deposits by making deposits with financial institutions as defined by Minn. Stat. § 118A.01, and by obtaining necessary documentation of perfected security interest in pledged collateral from the financial institutions. As of December 31, 2006, \$58,761 of the County's bank balance of \$7,015,988 was exposed to custodial credit risk because one bank pledged a local government security that did not meet statutory requirements for pledged collateral.

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments (Continued)

b. Investments

Interest Rate Risk

Interest rate risk is the risk that changes in the market interest rates will adversely affect the fair value of an investment. It is County policy to minimize exposure to interest rate risk by structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations; thereby avoiding the need to sell securities in the open market, investing operating funds primarily in shorter-term securities, liquid asset funds, money market mutual funds or similar investment pools, and limiting the average maturity in accordance with the County's cash requirements.

Credit Risk

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

Custodial Credit Risk

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities in the possession of an outside party. The County does not have a policy to mitigate custodial credit risk.

At December 31, 2006, none of the County's investments were subject to custodial credit risk.

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

b. Investments (Continued)

Concentration of Credit Risk

The concentration of credit risk is the risk of loss that may be caused by the County's investment in a single issuer. It is the County's policy to minimize concentration of credit risk by diversifying the investment portfolio so that the impact of potential losses from any one type of security or issuer will be minimal. As of December 31, 2006, all of the County's investment, carrying value balance of \$532,000, was invested in the MAGIC Fund.

2. Receivables

Receivables as of December 31, 2006, for the County are as follows:

	<u>Total Receivables</u>	<u>Amounts Not Scheduled for Collection During the Subsequent Year</u>
Taxes - prior	\$ 103,478	\$ -
Special assessments - prior	22,268	-
Special assessments - noncurrent	849,317	630,590
Accounts	204,219	-
Accrued interest	86,585	-
Due from other governments	<u>1,193,433</u>	<u>207,500</u>
Total	<u>\$ 2,459,300</u>	<u>\$ 838,090</u>

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets (Continued)

3. Capital Assets

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

	<u>Beginning Balance</u>	<u>Increase</u>	<u>Decrease</u>	<u>Ending Balance</u>
Capital assets not depreciated				
Land	\$ 695,771	\$ -	\$ -	\$ 695,771
Construction in progress	<u>387,631</u>	<u>821,152</u>	<u>374,880</u>	<u>833,903</u>
Total capital assets not depreciated	<u>\$ 1,083,402</u>	<u>\$ 821,152</u>	<u>\$ 374,880</u>	<u>\$ 1,529,674</u>
Capital assets depreciated				
Buildings	\$ 7,011,387	\$ -	\$ -	\$ 7,011,387
Land improvements	49,128	-	-	49,128
Machinery, furniture, and equipment	4,968,702	463,294	82,420	5,349,576
Infrastructure	<u>38,744,995</u>	<u>1,846,749</u>	<u>-</u>	<u>40,591,744</u>
Total capital assets depreciated	<u>\$ 50,774,212</u>	<u>\$ 2,310,043</u>	<u>\$ 82,420</u>	<u>\$ 53,001,835</u>
Less: accumulated depreciation for				
Buildings	\$ 1,739,744	\$ 165,323	\$ -	\$ 1,905,067
Land improvements	9,807	2,456	-	12,263
Machinery, furniture, and equipment	3,060,963	428,442	82,420	3,406,985
Infrastructure	<u>9,664,793</u>	<u>778,142</u>	<u>-</u>	<u>10,442,935</u>
Total accumulated depreciation	<u>\$ 14,475,307</u>	<u>\$ 1,374,363</u>	<u>\$ 82,420</u>	<u>\$ 15,767,250</u>
Total capital assets depreciated, net	<u>\$ 36,298,905</u>	<u>\$ 935,680</u>	<u>\$ -</u>	<u>\$ 37,234,585</u>
Capital Assets, Net	<u>\$ 37,382,307</u>	<u>\$ 1,756,832</u>	<u>\$ 374,880</u>	<u>\$ 38,764,259</u>

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

3. Capital Assets (Continued)

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

General government	\$ 240,303
Public safety	71,804
Highways and streets, including depreciation of infrastructure assets	1,009,229
Sanitation	846
Human services	<u>52,181</u>
Total Depreciation Expense	<u>\$ 1,374,363</u>

B. Interfund Receivables, Payables, and Transfers

The composition of interfund balances as of December 31, 2006, is as follows:

1. Due To/From Other Funds

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General	Human Services	<u>\$ 19,775</u>
Road and Bridge	General	\$ 19,064
	County Ditch	1,752
	Solid Waste	<u>522</u>
Total Due to Road and Bridge Fund		<u>\$ 21,338</u>
Total Due To/From Other Funds		<u>\$ 41,113</u>

2. Advances To/From Other Funds

<u>Receivable Fund</u>	<u>Payable Fund</u>	<u>Amount</u>
General	County Ditch	<u>\$ 153,575</u>

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

3. Detailed Notes on All Funds

B. Interfund Receivables, Payables, and Transfers (Continued)

3. Interfund Transfers

<u>Transfers Out</u>	<u>Transfers In</u>	<u>Amount</u>	<u>Purpose</u>
General	Road and Bridge	\$ 11,533	Allocated interest
	Road and Bridge	100,000	Operating transfer
	County Ditch	7,198	Allocated interest
	County Library	<u>2,601</u>	Allocated interest
Total Transfers Out of General Fund		\$ 121,332	
Human Services	General	<u>92,756</u>	2006 rent
Total Transfers In/Out		<u>\$ 214,088</u>	

C. Liabilities

1. Long-Term Debt

<u>Types of Indebtedness</u>	<u>Final Maturity</u>	<u>Installment Amount</u>	<u>Interest Rate (%)</u>	<u>Original Issue Amount</u>	<u>Outstanding Balance December 31, 2006</u>
G.O. Capital Improvement Bonds, Series 2000A	2007	\$2,095,000	5.65	\$ 2,500,000	\$ 2,095,000
G.O. Capital Improvement Refunding Bonds, Series 2004A	2021	\$120,000 - \$190,000	2.75 - 4.50	2,115,000	2,115,000
G.O. Capital Improvement Bonds, Series 2005A	2026	\$30,000 - \$60,000	3.50 - 4.40	845,000	845,000
G.O. Capital Notes, Series 2003	2007	\$70,000	3.00	<u>280,000</u>	<u>70,000</u>
Total				<u>\$ 5,740,000</u>	\$ 5,125,000
Less: unamortized discount					<u>(41,608)</u>
Total General Obligation Bonds, Net					<u>\$ 5,083,392</u>

Capital improvement bonds and capital notes are being retired by the Debt Service Fund.

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities (Continued)

Loans Payable

The County entered into loan agreements with the Minnesota Pollution Control Agency for the purpose of funding Clean Water Partnership Projects. The loans are secured by special assessments against benefited properties. Loan payments are reported in the General Fund.

<u>Types of Indebtedness</u>	<u>Final Maturity</u>	<u>Installment Amount</u>	<u>Interest Rate (%)</u>	<u>Original Issue Amount</u>	<u>Outstanding Balance December 31, 2006</u>
Watonwan Watershed Clean Water Partnership Project, SFR0047	2014	\$26,928	2.00	\$ 485,926	\$ 373,355
Watonwan Watershed Continuation Clean Water Partnership Project, SFR0108	2017	\$28,194	2.00	501,340	501,340
Total Loans				<u>\$ 987,266</u>	<u>\$ 874,695</u>

2. Debt Service Requirements

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

<u>Year Ending December 31</u>	<u>General Obligation Bonds</u>		<u>Capital Notes</u>	
	<u>Principal</u>	<u>Interest</u>	<u>Principal</u>	<u>Interest</u>
2007	\$ 2,125,000	\$ 176,656	\$ 70,000	\$ 2,100
2008	150,000	113,205	-	-
2009	155,000	108,630	-	-
2010	165,000	103,470	-	-
2011	165,000	97,788	-	-
2012 - 2016	905,000	392,263	-	-
2017 - 2021	1,115,000	186,199	-	-
2022 - 2026	<u>275,000</u>	<u>31,036</u>	<u>-</u>	<u>-</u>
Total	<u>\$ 5,055,000</u>	<u>\$ 1,209,247</u>	<u>\$ 70,000</u>	<u>\$ 2,100</u>

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities

2. Debt Service Requirements (Continued)

Year Ending December 31	Loans Payable	
	Principal	Interest
2007	\$ 46,620	\$ 7,235
2008	47,558	6,298
2009	48,513	5,342
2010	49,488	4,367
2011	50,483	3,372
2012 - 2014	130,693	3,947
Total	\$ 373,355	\$ 30,561

The debt service requirements for the loan from the Minnesota Pollution Control Agency in the amount of \$501,340 are not known as of December 31, 2006.

Crossover Refunding of Bonds

In 2004, \$2,115,000 General Obligation Capital Improvement Refunding Bonds were sold to refund the following bond issue:

Call Date	Issue	Maturing	Totaling
February 1, 2007	\$2,500,000 G.O. Capital Improvement Bonds, Series 2000A	2008 - 2021	\$ 2,000,000

The proceeds from the refunding bonds were placed with an escrow agent in an irrevocable trust from which U.S. Treasury securities were purchased. The County is responsible for the principal and interest payments on the original issue through 2007. The interest payments on the refunding bonds will be paid by the escrow agent through 2007 from earnings on the escrow account. Principal balances of both bond issues will be shown in the statement of net assets until the call date of the refunded bonds, at which time the 2000 Series bonds will be considered defeased and the liability for those bonds will be removed from the statement of net assets.

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities

2. Debt Service Requirements

Crossover Refunding of Bonds (Continued)

The County crossover refunded the 2000 Capital Improvement Bonds to reduce its total debt service payments in the years 2008 to 2021 by \$160,678 and to obtain an economic gain (difference between the present values of the debt service payments on the old and new debt) of \$111,522.

3. Changes in Long-Term Liabilities

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

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
G.O. Capital Improvement Bonds, Series 2000A	\$ 2,185,000	\$ -	\$ 90,000	\$ 2,095,000	\$ 2,095,000
G.O. Capital Improvement Bonds, Series 2005A	845,000	-	-	845,000	30,000
G. O. Capital Improvement Refunding Bonds, Series 2004A	2,115,000	-	-	2,115,000	-
G.O. Capital Notes, Series 2003	140,000	-	70,000	70,000	70,000
Less: unamortized discount on bonds	(44,394)	-	(2,786)	(41,608)	-
Total bonds payable	\$ 5,240,606	\$ -	\$ 157,214	\$ 5,083,392	\$ 2,195,000
Loans payable	824,912	95,485	45,702	874,695	46,620
Compensated absences	835,669	-	5,268	830,401	446,363
Long-Term Liabilities	<u>\$ 6,901,187</u>	<u>\$ 95,485</u>	<u>\$ 208,184</u>	<u>\$ 6,788,488</u>	<u>\$ 2,687,983</u>

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

3. Detailed Notes on All Funds (Continued)

D. Risk Management

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

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

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

D. Other Postemployment Benefits

Retirees

Watonwan County provides postemployment health care benefits for retirees and elected officials.

- The retirement policy was for employees that exercised a retirement option between July 1, 2003, and June 30, 2004. Individuals are eligible for benefits in the amount equal to the single health insurance premium for two years.

During 2006, there were three employees receiving the premium-coverage benefit. The County finances the plans on a pay-as-you-go basis. For the year ended December 31, 2006, the County recognized \$5,468 of expenditures.

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

3. Detailed Notes on All Funds

E. Other Postemployment Benefits

Retirees (Continued)

- Within 60 days of the effective date of an elected county official's retirement or termination, the County shall contribute an amount equal to the annual premium for single health insurance coverage in effect at the time of termination or retirement for every four complete years of service.

As of December 31, 2006, the County recorded a liability of \$81,540 for the elected official's termination benefits as a part of the compensated absences liability.

4. Pension Plans

A. Defined Benefit Plans

Plan Description

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

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

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.

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

4. Pension Plans

A. Defined Benefit Plans

Plan Description (Continued)

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

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

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

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

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

4. Pension Plans

A. Defined Benefit Plans (Continued)

Funding Policy

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

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

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

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

	<u>Public Employees Retirement Fund</u>	<u>Public Employees Police and Fund</u>	<u>Public Employees Correctional Fund</u>
2006	\$ 252,198	\$ 43,865	\$ 16,710
2005	223,265	39,678	15,322
2004	215,329	38,394	14,177

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

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

4. Pension Plans (Continued)

B. Defined Contribution Plan

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

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

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

The County's contributions for the years ending December 31, 2006, 2005, and 2004, were \$7,499, \$7,176, and \$6,746, respectively, equal to the contractually required contributions for each year as set by state statute.

5. Summary of Significant Contingencies and Other Items

A. Contingent Liabilities

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

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

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

B. Joint Ventures

Red Rock Rural Water System

The Red Rock Rural Water System was established pursuant to Minn. Stat. ch. 116A through a joint powers agreement, pursuant to Minn. Stat. § 471.59, and under the jurisdiction of the Fifth Judicial District. Brown, Cottonwood, Jackson, Lyon, Martin, Murray, Redwood, and Watonwan Counties have agreed to guarantee their shares of debt arising within each respective county. The Red Rock Rural Water System provides water for participating rural water users and cities within the water district.

The governing body is composed of nine members appointed to three-year terms by the District Court. Each county is responsible for levying and collecting the special assessments from the benefited properties within the county. The bond issue and notes payable are shown as long-term debt in the financial statements of the Red Rock Rural Water System. Outstanding bonds at December 31, 2005, (the most current information available) amounted to \$6,490,000, and notes payable were \$263,397. The Water System's net assets increased by \$133,377 in 2005. Complete financial information can be obtained from the Red Rock Rural Water System, Jeffers, Minnesota 56145.

Three Counties for Kids Collaborative

The Three Counties for Kids Collaborative was established in 1996 under the authority of Minn. Stat. § 471.59. The Collaborative includes Brown, Sibley, and Watonwan Counties; the River Bend Education District, and the Sioux Trails Mental Health Center. The purpose of the Collaborative is to join local units of government together to ensure a unified, unduplicated, and family friendly system of intervention and care for families and children.

Control of the Collaborative is vested in a Board of Directors consisting of seven members. Brown County Family Services acts as fiscal agent for the Collaborative. The Collaborative is financed by Local Collaborative Time Study (LCTS) funds. During 2006, Watonwan County made no contributions to the Collaborative. Any withdrawing party remains liable for fiscal obligations incurred prior to the effective date of withdrawal and shall not be entitled to any compensation as long as the Collaborative continues in existence. Should the Collaborative cease to exist, all

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

5. Summary of Significant Contingencies and Other Items

B. Joint Ventures

Three Counties for Kids Collaborative (Continued)

property, real and personal, at the time of the termination shall be distributed by the Three Counties for Kids Collaborative Board of Directors. Complete financial information may be obtained by contacting the Brown County Family Services Department, New Ulm, Minnesota 56073.

Vision for Family and Community Collaborative

The Vision for Family and Community Collaborative was established in 1996 under the authority of Minn. Stat. § 121.8355 (now Minn. Stat. § 124D.23). The Collaborative includes Watonwan County and St. James, Madelia, and Butterfield Independent School Districts. The Joint Powers Board ensures the availability of comprehensive services designed to enhance or strengthen family functioning.

Control of the Collaborative is vested in a Joint Powers Board. The Joint Powers Board is composed of nine members. Watonwan County Human Services acts as fiscal agent for the Collaborative. The Collaborative is financed by LCTS funds. During 2006, Watonwan County made no contributions to the Collaborative. Any withdrawing party remains fiscally liable until the effective date of withdrawal. Should the Collaborative cease to exist, all property, real and personal, held by the Joint Powers Board at the time of the termination shall be distributed by resolution of the Board in accordance with law and in a manner to best accomplish the purpose of the Collaborative.

Rural Minnesota Energy Board

The Rural Minnesota Energy Board was established in 2005 under the authority of Minn. Stat. § 471.59. The Board includes Cottonwood, Faribault, Jackson, Lincoln, Lyon, Martin, Mower, Murray, Nobles, Pipestone, Redwood, Renville, Rock, and Watonwan Counties. The purpose of the Board is to provide policy guidance on issues surrounding energy development in rural Minnesota and to foster the diversification of the economic climate in rural Minnesota. The focus of the Board includes, but is not limited to, renewable energy, wind energy, energy transmission lines, hydrogen energy technology, and bio-diesel and ethanol use.

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

5. Summary of Significant Contingencies and Other Items

B. Joint Ventures

Rural Minnesota Energy Board (Continued)

The governing body is composed of one voting member and one alternate member from each participating county's Board of Commissioners. The Board shall remain in existence as long as two or more counties remain parties to the agreement. Should the Board cease to exist, assets shall be liquidated after payment of liabilities, based upon the ratios set out under the equal and proportionate share articles of the agreement. During 2006, Watonwan County paid \$2,000 to the Board.

C. Jointly-Governed Organizations

The South Central Emergency Medical Services (SEMS) provides various emergency medical services to several counties. During the year, the County made no contributions to the SEMS.

The Minnesota River Board promotes orderly water quality improvement and management of the Minnesota River Watershed. During the year, the County made contributions of \$940 to the Board.

The Greater Blue Earth River Basin Alliance is a joint powers of counties and soil and water districts that combines project and implementation efforts to improve water quality in the Greater Blue Earth River Basin. During the year, the County paid \$5,624 to the Alliance.

The Minnesota Counties Computer Cooperative provides computer programming services for the County. During the year, the County purchased \$105,396 of services.

The South Central Regional IMMTRACK (immunization registry) Joint Powers Board promotes the implementation and maintenance of a regional immunization information system to ensure age-appropriate immunizations through complete and accurate records. During the year, the County paid \$1,432 to the Board.

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

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

D. Agricultural Best Management Loan Program

The County has entered into an agreement with the Minnesota Department of Agriculture and a local lending institution to jointly administer a loan program to individuals to implement projects that prevent or mitigate non-point source water pollution. While the County is not liable for the repayment of the loan in any manner, it does have certain responsibilities under the agreement. The County has met those responsibilities for 2006.

E. Special Benefit Tax Levy

In 1993, the South Central Minnesota Multi-County Housing Authority issued \$20,315,000 of revenue bonds to construct housing units in Watonwan County and four surrounding counties. The Authority has since defaulted on these bonds. In 2000, the counties entered into a settlement agreement where each of the counties will approve a special benefit tax levy on behalf of the Authority from 2001 through 2024 to cover the operating deficits based on each county's proportionate share of housing units constructed. Watonwan County's proportionate share of the operating deficit for 2006 is \$76,774. The proportionate share of the counties may change for years 2007 through 2024 if there are changes in the taxable market value over the 2001 taxable market value.

COMBINING FUND FINANCIAL STATEMENTS AND SCHEDULE

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**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

OTHER GOVERNMENTAL FUNDS

Special Revenue Funds

County Library - to account for the funds of the County library system. Financing comes primarily from an annual tax levy and intergovernmental revenue from the state government.

Solid Waste - to account for the County recycling programs. Financing is provided by a tax levy, user charges, and state grants.

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**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

Statement 1

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

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Revenues				
Taxes	\$ 313,373	\$ 279,407	\$ 278,909	\$ (498)
Intergovernmental	21,404	55,370	55,870	500
Investment earnings	-	-	75,948	75,948
Total Revenues	\$ 334,777	\$ 334,777	\$ 410,727	\$ 75,950
Expenditures				
Debt service				
Principal	\$ 160,000	\$ 160,000	\$ 160,000	\$ -
Interest	128,245	128,245	241,051	(112,806)
Administrative charges	-	-	1,346	(1,346)
Total Expenditures	\$ 288,245	\$ 288,245	\$ 402,397	\$ (114,152)
Net Change in Fund Balance	\$ 46,532	\$ 46,532	\$ 8,330	\$ (38,202)
Fund Balance - January 1	2,340,804	2,340,804	2,340,804	-
Fund Balance - December 31	\$ 2,387,336	\$ 2,387,336	\$ 2,349,134	\$ (38,202)

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

Statement 2

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

	Special Revenue Funds		
	County Library	Solid Waste	Total
<u>Assets</u>			
Cash and pooled investments	\$ 442,394	\$ 419,076	\$ 861,470
Taxes receivable			
Prior	6,431	173	6,604
Special assessments receivable			
Prior	-	13,334	13,334
Accrued interest receivable	2,360	-	2,360
Total Assets	\$ 451,185	\$ 432,583	\$ 883,768
<u>Liabilities and Fund Balances</u>			
Liabilities			
Accounts payable	\$ 1,599	\$ 16,551	\$ 18,150
Salaries payable	6,700	-	6,700
Due to other funds	-	522	522
Deferred revenue - unavailable	3,839	9,488	13,327
Deferred revenue - unearned	91	2	93
Total Liabilities	\$ 12,229	\$ 26,563	\$ 38,792
Fund Balances			
Reserved for donations	\$ 155,137	\$ -	\$ 155,137
Unreserved			
Designated for cash flows	274,492	7,024	281,516
Designated for compensated absences	9,327	-	9,327
Undesignated	-	398,996	398,996
Total Fund Balances	\$ 438,956	\$ 406,020	\$ 844,976
Total Liabilities and Fund Balances	\$ 451,185	\$ 432,583	\$ 883,768

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

Statement 3

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

	Special Revenue Funds		
	County Library	Solid Waste	Total
Revenues			
Taxes	\$ 388,269	\$ 10,024	\$ 398,293
Special assessments	-	132,325	132,325
Intergovernmental	123,892	52,279	176,171
Charges for services	4,283	-	4,283
Fines and forfeits	8,152	-	8,152
Gifts and contributions	3,220	-	3,220
Investment earnings	6,960	-	6,960
Miscellaneous	2,408	5,412	7,820
Total Revenues	\$ 537,184	\$ 200,040	\$ 737,224
Expenditures			
Current			
Sanitation	\$ -	\$ 137,197	\$ 137,197
Culture and recreation	497,361	-	497,361
Total Expenditures	\$ 497,361	\$ 137,197	\$ 634,558
Excess of Revenues Over (Under) Expenditures	\$ 39,823	\$ 62,843	\$ 102,666
Other Financing Sources (Uses)			
Transfers in	2,601	-	2,601
Net Change in Fund Balances	\$ 42,424	\$ 62,843	\$ 105,267
Fund Balances - January 1	396,532	343,177	739,709
Fund Balances - December 31	\$ 438,956	\$ 406,020	\$ 844,976

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

Statement 4

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

	Budgeted Amounts		Actual	Variance with
	Original	Final	Amounts	Final Budget
Revenues				
Taxes	\$ 435,849	\$ 388,165	\$ 388,269	\$ 104
Intergovernmental	76,209	123,893	123,892	(1)
Charges for services	4,600	4,600	4,283	(317)
Fines and forfeits	9,283	9,283	8,152	(1,131)
Gifts and contributions	-	-	3,220	3,220
Investment earnings	-	-	6,960	6,960
Miscellaneous	-	-	2,408	2,408
Total Revenues	\$ 525,941	\$ 525,941	\$ 537,184	\$ 11,243
Expenditures				
Current				
Culture and recreation				
County library	528,083	528,083	497,361	30,722
Excess of Revenues Over (Under)				
Expenditures	\$ (2,142)	\$ (2,142)	\$ 39,823	\$ 41,965
Other Financing Sources (Uses)				
Transfers in	2,142	2,142	2,601	459
Net Change in Fund Balance	\$ -	\$ -	\$ 42,424	\$ 42,424
Fund Balance - January 1	396,532	396,532	396,532	-
Fund Balance - December 31	\$ 396,532	\$ 396,532	\$ 438,956	\$ 42,424

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

Statement 5

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

	Budgeted Amounts		Actual Amounts	Variance with Final Budget
	Original	Final		
Revenues				
Taxes	\$ 11,254	\$ 10,022	\$ 10,024	\$ 2
Special assessments	132,000	132,000	132,325	325
Intergovernmental	51,046	52,278	52,279	1
Miscellaneous	3,150	3,150	5,412	2,262
Total Revenues	\$ 197,450	\$ 197,450	\$ 200,040	\$ 2,590
Expenditures				
Current				
Sanitation				
SCORE	197,450	197,450	137,197	60,253
Net Change in Fund Balance	\$ -	\$ -	\$ 62,843	\$ 62,843
Fund Balance - January 1	343,177	343,177	343,177	-
Fund Balance - December 31	\$ 343,177	\$ 343,177	\$ 406,020	\$ 62,843

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**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

AGENCY FUNDS

Agency - to account for the collection and disbursement of funds for the state or other local governments, including game and fish fees, licenses, fines, police and fire aids, deed taxes, and mortgage registry taxes.

Vision for Family and Community - to account for the funds of a County/multi-school district family service collaborative.

Taxes and Penalties - to account for the collection and disbursement of taxes and penalties.

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**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

Statement 6

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

	Balance January 1	Additions	Deductions	Balance December 31
<u>AGENCY</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 19,757	\$ 2,018,567	\$ 2,025,829	\$ 12,495
<u>Liabilities</u>				
Due to other governments	\$ 19,757	\$ 2,018,567	\$ 2,025,829	\$ 12,495
 <u>VISION FOR FAMILY AND COMMUNITY</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 109,254	\$ 74,010	\$ 110,015	\$ 73,249
<u>Liabilities</u>				
Due to other governments	\$ 109,254	\$ 74,010	\$ 110,015	\$ 73,249
 <u>TAXES AND PENALTIES</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 81,131	\$ 10,003,501	\$ 9,951,207	\$ 133,425
<u>Liabilities</u>				
Due to other governments	\$ 81,131	\$ 10,003,501	\$ 9,951,207	\$ 133,425

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

Statement 6
(Continued)

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

	Balance January 1	Additions	Deductions	Balance December 31
<u>TOTAL ALL AGENCY FUNDS</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 210,142	\$ 12,096,078	\$ 12,087,051	\$ 219,169
<u>Liabilities</u>				
Due to other governments	\$ 210,142	\$ 12,096,078	\$ 12,087,051	\$ 219,169

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

Schedule 1

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

Shared Revenue

State

Highway users tax	\$ 2,877,368
County program aid	953,160
PERA rate reimbursement	19,906
Disparity reduction aid	5,082
Police aid	34,479
Enhanced 911	106,360
Market value credit	634,262

Total Shared Revenue	\$ 4,630,617
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Reimbursement for Services

Minnesota Department of Human Services	\$ 916,468
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Payments

Local

City contribution	\$ 21,904
Payments in lieu of taxes	15,993

Total Payments	\$ 37,897
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Grants

State

Minnesota Department of	
Public Safety	\$ 29,346
Health	65,889
Environmental Assistance	49,079
Natural Resources	6,727
Trial Courts	16,148
Human Services	594,769
Corrections	33,966
Transportation	112,330
Other	4,415
Pollution Control Agency	120,866
Peace Officer Standards and Training Board	3,256
Water and Soil Resources Board	66,168

Total State	\$ 1,102,959
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Federal

Department of	
Agriculture	\$ 83,492
Justice	12,574
Transportation	472,148
Health and Human Services	263,687
Homeland Security	10,194
Election Assistance Commission	168,000

Total Federal	\$ 1,010,095
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Total State and Federal Grants	\$ 2,113,054
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Total Intergovernmental Revenue	\$ 7,698,036
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**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

Schedule 2

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

I. SUMMARY OF AUDITOR'S RESULTS

- A. Our report expresses unqualified opinions on the basic financial statements of Watonwan County.
- B. Deficiencies in internal control were disclosed by the audit of financial statements of Watonwan 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*." None were material weaknesses.
- C. No instances of noncompliance material to the financial statements of Watonwan 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 Watonwan 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	CFDA #20.205
Help America Vote Act	CFDA #90.401
- H. The threshold for distinguishing between Types A and B programs was \$300,000.
- I. Watonwan 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 ITEM NOT RESOLVED

05-1 Transit Department Segregation of Duties and Procedures

Due to the limited number of office personnel within the Watonwan County Transit Office, segregation of the accounting functions necessary to ensure adequate internal control is not possible. The office has only one employee to receive and account for departmental collections. This is not unusual in operations the size of Watonwan County; however, the County's management should constantly be aware of this condition and realize the concentration of duties and responsibilities in a limited number of individuals is not desirable from an accounting point of view.

Since our prior audit, some procedures have been implemented to strengthen internal control over collections. Deposits are remitted on a weekly basis, and checks are stamped immediately upon receipt. However, improvements need to be made to the procedures matching deposits with source documents.

We recommend that the County's management continue to be aware of the lack of segregation of duties within certain accounting functions and continue to implement procedures to ensure adequate controls are in place over cash, receivables, and other items.

Client's Response:

We now have a stamp used on every check when it is received in the Transit Office and then a spreadsheet to record every check.

The stamp:

*For Deposit Only
Watonwan County
dba TMT (Take Me There)
Carol Johnson, County Treasurer*

The receipts are deposited weekly after verifying the dollar amount with the check spreadsheet and the drivers' spreadsheet that they record their fares daily on. The spreadsheets are all kept in a file along with the bank deposit slip.

ITEMS ARISING THIS YEAR

06-1 Preparation of Financial Statements

Watonswan County is required to prepare financial statements in accordance with generally accepted accounting principles (GAAP). The preparation of the financial statements is the responsibility of the County's management. Financial statement preparation in accordance with GAAP requires internal controls over both: (1) recording, processing, and summarizing accounting data (maintaining internal books and records); and (2) preparing and reporting appropriate government-wide and fund financial statements, including the related notes to the financial statements.

As is the case with many small and medium-sized entities, the County has relied on its independent external auditors to assist in the preparation of the basic financial statements, including notes to the financial statements, as part of its external financial reporting process. Accordingly, the County's ability to prepare financial statements in accordance with GAAP is based, at least in part, on its reliance on its external auditors, who cannot by definition be considered part of the government's internal control.

We recommend the County obtain the training and expertise to internally prepare its annual financial statements in accordance with GAAP.

Client's Response:

For the year ending December 31, 2007, the County will prepare the financial statements in accordance with GAAP. Personnel will be trained in order to accomplish this task.

06-2 Audit Adjustments

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements of the financial statements on a timely basis. One control deficiency that typically is considered significant is identification by the auditor of a material misstatement in the financial statements that was not initially identified by the entity's internal controls. During our audit, we proposed the following adjustments that resulted in significant changes to the County's financial statements.

- Allocations were required in the General Fund to reclassify the unallocated departments.

Schedule 2
(Continued)

- Recording additional deferred revenue and receivable amounts was required in the General Fund, Road and Bridge Special Revenue Fund, Human Services Special Revenue Fund, and Debt Service Fund.
- Corrections were made to reclassify various revenues and transfers in the General Fund, Road and Bridge Special Revenue Fund, Human Services Special Revenue Fund, and Debt Service Fund.
- Corrections were made in the Road and Bridge Special Revenue Fund to reclassify construction expenditures and to record the state-aid allotment advance.
- Non-County revenue and expenditures needed to be eliminated in the County Ditch Special Revenue Fund.

The inability to detect a material misstatement 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 detect misstatements in the financial statements. We encourage review of draft financial statements by a qualified individual to identify potential misstatements.

Client's Response:

While preparing the financial statements for the year ending December 31, 2007, staff will address adjustment deficiencies cited by the auditors for the year ended December 31, 2006.

III. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARD PROGRAMS

None.

IV. OTHER FINDINGS AND RECOMMENDATIONS

OTHER ITEM FOR CONSIDERATION

Other Postemployment Benefits (OPEB)

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

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

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

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

If applicable for Watonwan County, GASB Statements 43 and 45 would be implemented for the years ended December 31, 2007, and 2008, respectively.

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OTHER REQUIRED REPORTS

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REBECCA OTTO
STATE AUDITOR

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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Board of County Commissioners
Watonwan County

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Watonwan County as of and for the year ended December 31, 2006, and have issued our report thereon dated September 24, 2007. 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 Watonwan 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 would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the County's ability to initiate, authorize, record,

process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the County's financial statements that is more than inconsequential will not be prevented or detected by the County's internal control over financial reporting. We considered the deficiencies described in the accompanying Schedule of Findings and Questioned Costs as items 05-1, 06-1, and 06-2 to be significant deficiencies in internal control over financial reporting.

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

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe none of the significant deficiencies described above is a material weakness.

Compliance and Other Matters

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

Minnesota Legal Compliance

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

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

The results of our tests indicate that, for the items tested, Watonwan 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 Watonwan County and is reported for that purpose.

Watonwan County's written response to the significant deficiency findings identified in our audit has not been subjected to any auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

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

September 24, 2007

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REBECCA OTTO
STATE AUDITOR

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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
Watonwan County

Compliance

We have audited the compliance of Watonwan 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, 2006. Watonwan 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 each of 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 Watonwan 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, Watonwan 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, 2006.

Internal Control Over Compliance

The management of Watonwan 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, 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 control deficiency in internal control over compliance 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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the County's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the County's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by Watonwan County's internal control.

Our consideration of the internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies 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, each major fund, and the aggregate remaining fund information of Watonwan County as of and for the year ended December 31, 2006, and have issued our report thereon dated September 24, 2007. Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise Watonwan 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 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

September 24, 2007

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**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

Schedule 3

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2006**

Federal Grantor Pass-Through Agency Grant Program Title	Federal CFDA Number	Expenditures
U.S. Department of Agriculture		
Passed Through Minnesota Department of Health Special Supplemental Nutrition Program for Women, Infants, and Children	10.557	\$ 79,463
Passed Through Minnesota Department of Human Services Administrative Matching Grant for Food Stamp Program	10.561	1,638
Passed Through Minnesota Department of Agriculture Farmers Market Nutrition Program	10.572	363
Total U.S. Department of Agriculture		\$ 81,464
U.S. Department of Justice		
Passed Through Minnesota Department of Public Safety Crime Victim Assistance	16.575	\$ 12,574
U.S. Department of Transportation		
Passed Through Minnesota Department of Public Safety State and Community Highway Safety	20.600	\$ 5,351
Passed Through Minnesota Department of Transportation Highway Planning and Construction	20.205	390,513
Public Transportation for Non-Urbanized Areas	20.509	71,770
Total U.S. Department of Transportation		\$ 467,634
U.S. Election Assistance Commission		
Passed Through Minnesota Secretary of State Help America Vote Act	90.401	\$ 168,000
U.S. Department of Health and Human Services		
Passed Through Minnesota Department of Health Center for Disease Control and Prevention	93.283	\$ 28,711
Temporary Assistance for Needy Families	93.558	10,861
Maternal and Child Health Services Block Grant	93.994	18,678
Passed Through Minnesota Department of Human Services Temporary Assistance for Needy Families	93.558	88,996
Child Care Development Block Grant	93.575	3,746
Child Welfare Services	93.645	324
Foster Care - Title IV-E	93.658	11,969
Social Services Block Grant - Title XX	93.667	91,828
Independent Living	93.674	4,144
Community Mental Health Services	93.958	5,773
Total U.S. Department of Health and Human Services		\$ 265,030

**WATONWAN COUNTY
ST. JAMES, MINNESOTA**

Schedule 3
(Continued)

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2006**

Federal Grantor Pass-Through Agency Grant Program Title	Federal CFDA Number	Expenditures
U.S. Department of Homeland Security		
Passed Through Minnesota Department of Public Safety		
Homeland Security Grant Program - Emergency Response	97.004	\$ 999
Emergency Management Performance Grant	97.042	9,195
Total U.S. Department of Homeland Security		\$ 10,194
Total Federal Awards		\$ 1,004,896

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 Watonwan County. The County's reporting entity is defined in Note 1 to the financial statements.
2. The expenditures on this schedule are on the modified accrual basis of accounting. In some instances, expenditures shown are different than reported revenues because they are not available.
3. During the year, the County did not pass any federal money to subrecipients.
4. Pass-through grant numbers were not assigned by the pass-through agencies.