

STATE OF MINNESOTA

Office of the State Auditor



Patricia Anderson
State Auditor

**LAKE COUNTY HOUSING AND
REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

FOR THE YEAR ENDED DECEMBER 31, 2004

Description of the Office of the State Auditor

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

Through financial, compliance, and special audits, the State Auditor oversees and ensures that local government funds are used for the purposes intended by law and that local governments hold themselves to the highest standards of financial accountability.

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

Audit Practice - conducts financial and legal compliance audits for local governments;

Government Information - collects and analyzes financial information for cities, towns, counties, and special districts;

Legal/Special Investigations - provides legal analysis and counsel to the Office and responds to outside inquiries about Minnesota local government law; as well as investigates allegations of misfeasance, malfeasance, and nonfeasance in local government;

Pension - monitors investment, financial, and actuarial reporting for over 700 public pension funds; and

Tax Increment Financing, Investment and Finance - promotes compliance and accountability in local governments' use of tax increment financing through financial and compliance audits.

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

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**LAKE COUNTY HOUSING AND
REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

For the Year Ended December 31, 2004



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

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**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

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**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

ORGANIZATION
DECEMBER 31, 2004

<u>Commissioners</u>	<u>Term Expires</u>
Scott Johnson	May 30, 2010
Paul Bergman	May 30, 2007
Jon Anderson	May 30, 2006
Gordon Klein	May 30, 2009

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STATE OF MINNESOTA

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PATRICIA ANDERSON
STATE AUDITOR

INDEPENDENT AUDITOR'S REPORT

Board of County Commissioners
Lake County Housing and
Redevelopment Authority

We have audited the accompanying financial statements of the governmental activities, the business-type activities, and each major fund of the Lake County Housing and Redevelopment Authority, a component unit of Lake County, as of and for the year ended December 31, 2004, which collectively comprise the Authority's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Lake County Housing and Redevelopment Authority's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the 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 financial position of the governmental activities, the business-type activities, and each major fund of the Lake County Housing and Redevelopment Authority as of December 31, 2004, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Lake County Housing and Redevelopment Authority has adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements--Management's Discussion and Analysis--for State and Local Governments*, as

amended. The Lake County Housing and Redevelopment Authority has not presented a Management's Discussion and Analysis that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be part of, the basic financial statements.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 10, 2005, on our consideration of the Lake County Housing and Redevelopment Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

/s/Pat Anderson

PATRICIA ANDERSON
STATE AUDITOR

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

End of Fieldwork: August 10, 2005

BASIC FINANCIAL STATEMENTS

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GOVERNMENT-WIDE FINANCIAL STATEMENTS

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**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

EXHIBIT 1

**STATEMENT OF NET ASSETS
DECEMBER 31, 2004**

	<u>Governmental Activities</u>	<u>Business-Type Activities</u>	<u>Total</u>
<u>Assets</u>			
Cash	\$ 28,593	\$ 40,325	\$ 68,918
Taxes receivable	10,413	-	10,413
Accounts receivable	119,771	-	119,771
Accrued interest receivable	75	-	75
Due from other governments	68,632	-	68,632
Due from Lake County	2,538	-	2,538
Internal balances	14,380	(14,380)	-
Loans receivable	83,000	-	83,000
Restricted assets			
Debt service	-	69,198	69,198
Customer deposits	-	9,619	9,619
Capital assets			
Non-depreciable	208,629	-	208,629
Depreciable - net of accumulated depreciation	1,003,340	1,522,868	2,526,208
Total Assets	\$ 1,539,371	\$ 1,627,630	\$ 3,167,001
<u>Liabilities</u>			
Accounts payable	\$ 20,655	\$ 4,599	\$ 25,254
Due to Lake County	566,538	-	566,538
Accrued interest payable	9,173	2,650	11,823
Deferred revenue	-	25	25
Liabilities payable from restricted assets			
Customer deposits payable	-	9,619	9,619
Long-term liabilities			
Due within one year	140,000	30,100	170,100
Due in more than one year	300,000	998,862	1,298,862
Total Liabilities	\$ 1,036,366	\$ 1,045,855	\$ 2,082,221
<u>Net Assets</u>			
Investment in capital assets, net of related debt	\$ 771,969	\$ 493,906	\$ 1,265,875
Restricted for debt service	-	69,198	69,198
Unrestricted	(268,964)	18,671	(250,293)
Total Net Assets	\$ 503,005	\$ 581,775	\$ 1,084,780

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

EXHIBIT 2

**STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2004**

	Expenses	Program Revenues Charges for Services	Net (Expense) Revenue and Changes in Net Assets		
			Governmental Activities	Business-Type Activities	Total
<u>Functions/Programs</u>					
Governmental activities					
Urban and economic development	\$ 531,190	\$ 2,537	\$ (528,653)	\$ -	\$ (528,653)
Business-type activities					
Senior housing	169,383	139,253	-	(30,130)	(30,130)
Total	\$ 700,573	\$ 141,790	\$ (528,653)	\$ (30,130)	\$ (558,783)
General Revenues					
Tax increments			\$ 237,474	\$ -	\$ 237,474
Intergovernmental			160,255	-	160,255
Investment earnings			1,373	-	1,373
Miscellaneous			76,648	1,733	78,381
Total general revenues			\$ 475,750	\$ 1,733	\$ 477,483
Change in net assets			\$ (52,903)	\$ (28,397)	\$ (81,300)
Net Assets - Beginning			555,908	610,172	1,166,080
Net Assets - Ending			\$ 503,005	\$ 581,775	\$ 1,084,780

FUND FINANCIAL STATEMENTS

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GOVERNMENTAL FUND

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**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

EXHIBIT 3

**BALANCE SHEET
GENERAL FUND
DECEMBER 31, 2004**

Assets

Cash	\$	25,136
Undistributed cash with Lake County		3,457
Taxes receivable		10,413
Accounts receivable		119,771
Accrued interest receivable		75
Due from other governments		68,632
Due from Lake County		2,538
Due from other funds		14,380
Loans receivable		83,000
		<hr/>
Total Assets	\$	327,402

Liabilities and Fund Balance

Liabilities

Accounts payable	\$	20,655
Due to Lake County		566,538
Deferred revenue		167,959
		<hr/>
Total Liabilities	\$	755,152

Fund Balance

Reserved for loans receivable	\$	83,000
Unreserved - undesignated		(510,750)
		<hr/>
Total Fund Balance	\$	(427,750)

Total Liabilities and Fund Balance	\$	327,402
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**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

EXHIBIT 4

**RECONCILIATION OF GOVERNMENTAL FUND BALANCE SHEET TO
THE GOVERNMENT-WIDE STATEMENT OF NET ASSETS--GOVERNMENTAL ACTIVITIES
DECEMBER 31, 2004**

Fund balances - governmental fund (Exhibit 3)	\$ (427,750)
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.	1,211,969
Other long-term assets are not available to pay for current period expenditures and, therefore, are deferred in the governmental funds.	167,959
Long-term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported in the governmental funds.	
General Obligation Jail Lease Revenue Bonds	(440,000)
Accrued interest payable	<u>(9,173)</u>
Net assets of governmental activities (Exhibit 1)	<u>\$ 503,005</u>

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

EXHIBIT 5

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2004**

Revenues	
Tax increments	\$ 243,970
Intergovernmental	160,255
Investment earnings	1,373
Miscellaneous	
Rental income	10,266
Other	35,939
	\$ 451,803
Total Revenues	
Expenditures	
Current	
Urban and economic development	
Meetings	\$ 4,197
Rent	10,982
Legal	40,343
Consulting	4,432
Accounting and auditing	19,234
Tax increment distributions	393,042
Property maintenance and development	4,024
Other	711
Debt service	
Principal retirement	135,000
Interest	25,255
	\$ 637,220
Total Expenditures	
Excess of Revenues Over (Under) Expenditures	\$ (185,417)
Fund Balance - January 1, as restated (Note 2)	(242,333)
Fund Balance - December 31	\$ (427,750)

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

EXHIBIT 6

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES, AND
CHANGES IN FUND BALANCE OF THE GOVERNMENTAL FUND TO THE
GOVERNMENT-WIDE STATEMENT OF ACTIVITIES--GOVERNMENTAL ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2004**

Net change in fund balances - governmental fund (Exhibit 5)	\$	(185,417)
Amounts reported for governmental activities in the statement of activities are different because:		
In the funds, under the modified accrual basis, receivables not available for expenditure are deferred. In the statement of activities, those revenues are recognized when earned. The adjustment to revenues between the fund statements and the statement of activities is the increase (decrease) in revenues deferred as unavailable.		
Deferred revenue - December 31	\$ 167,959	
Deferred revenue - January 1	<u>(141,475)</u>	26,484
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.		
Current year depreciation		(31,670)
Repayment of debt principal is an expenditure in the governmental fund, but the repayment reduces long-term debt at the government-wide level.		
Principal repayments		135,000
Some expenses reported in the statement of activities do not require the use of current financial resources, and therefore, are not reported as expenditures in governmental funds.		
Change in accrued interest payable		<u>2,700</u>
Change in net assets of governmental activities (Exhibit 2)	\$	<u>(52,903)</u>

PROPRIETARY FUND

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**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

EXHIBIT 7

**STATEMENT OF NET ASSETS
SILVERPOINTE ENTERPRISE FUND
DECEMBER 31, 2004**

Assets

Current assets	
Cash and cash equivalents	\$ <u>40,325</u>
Restricted assets	
Cash and cash equivalents	
Debt service	\$ 69,198
Customer deposits	9,619
Total restricted assets	\$ <u>78,817</u>
Noncurrent assets	
Capital assets	
Depreciable capital assets - net of accumulated depreciation	\$ <u>1,522,868</u>
Total Assets	\$ <u>1,642,010</u>

Liabilities

Current liabilities	
Accounts payable	\$ 4,599
Interest payable	2,650
Due to other funds	14,380
Deferred revenue	25
General obligation bonds payable - current	30,100
Total current liabilities	\$ <u>51,754</u>
Current liabilities payable from restricted assets	
Customer deposits payable	9,619
Noncurrent liabilities	
General obligation bonds payable - long-term	998,862
Total Liabilities	\$ <u>1,060,235</u>
Net Assets	
Invested in capital assets - net of related debt	\$ 493,906
Restricted for debt service	69,198
Unrestricted	18,671
Total Net Assets	\$ <u>581,775</u>

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

EXHIBIT 8

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
SILVERPOINTE ENTERPRISE FUND
FOR THE YEAR ENDED DECEMBER 31, 2004**

Operating Revenues	
Rental	\$ 134,833
Parking	4,420
Miscellaneous	1,733
	<hr/>
Total Operating Revenues	\$ 140,986
Operating Expenses	
Other services and charges	
Human resources	\$ 15,286
Management fees	9,815
Professional fees	2,650
Real estate taxes	5,791
Travel	522
Telephone	2,345
Utilities	16,894
Advertising	12,632
Insurance	4,400
Repairs and maintenance	8,100
Sanitation	1,422
Miscellaneous	179
Supplies	1,308
Depreciation expense	47,490
	<hr/>
Total Operating Expenses	\$ 128,834
Operating Income (Loss)	\$ 12,152
Nonoperating Revenues (Expenses)	
Interest expense	<hr/> (40,549)
Change in Net Assets	\$ (28,397)
Net Assets - January 1	<hr/> 610,172
Net Assets - December 31	<hr/> \$ 581,775

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

EXHIBIT 9

**STATEMENT OF CASH FLOWS
SILVERPOINTE ENTERPRISE FUND
YEAR ENDED DECEMBER 31, 2004**

Cash Flows from Operating Activities	
Cash received from customers	\$ 140,364
Cash paid to suppliers	<u>(76,327)</u>
Net cash provided by (used for) operating activities	<u>\$ 64,037</u>
Cash Flows from Capital and Related Financing Activities	
Principal paid on long-term debt	\$ (27,819)
Interest paid on long-term debt	<u>(41,399)</u>
Net cash provided by (used in) capital and related financing activities	<u>\$ (69,218)</u>
Net Increase (Decrease) in Cash	\$ (5,181)
Cash and Cash Equivalents - January 1, 2004	<u>45,506</u>
Cash and Cash Equivalents - December 31, 2004	<u><u>\$ 40,325</u></u>
Reconciliation of Operating Income (Loss) to Net Cash Provided by (Used for) Operating Activities	
Net operating income (loss)	\$ 12,152
Adjustments to reconcile net operating income (loss) to net cash provided by (used for) operating activities	
Depreciation expense	47,490
Increase (decrease) in accounts payable	5,017
Increase (decrease) in deferred revenue	<u>(622)</u>
Net Cash Provided by (Used for) Operating Activities	<u><u>\$ 64,037</u></u>
Noncash Investing, Capital, and Financing Activities	
Increase in cash held for security deposits	\$ (278)

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**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

**NOTES TO THE FINANCIAL STATEMENTS
AS OF AND FOR THE YEAR ENDED DECEMBER 31, 2004**

1. Summary of Significant Accounting Policies

The Authority's financial statements are prepared in accordance with generally accepted accounting principles (GAAP) for the year ended December 31, 2004. 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 (FASB) issued through November 30, 1989, (when applicable) that do not conflict with or contradict GASB pronouncements. Although the Authority has the option to apply FASB pronouncements issued after that date to its business-type activities and enterprise funds, the Authority has chosen not to do so. The Authority has not presented in the financial statements a Management's Discussion and Analysis that GASB has determined is necessary to supplement, although not required to be part of, the basic financial statements. The more significant accounting policies established in GAAP and used by the Authority are discussed below.

A. Financial Reporting Entity

The Lake County Housing and Redevelopment Authority was established June 13, 1984, and became active in 1986, having all the powers and duties of a county housing and redevelopment authority under the provisions of Minn. Stat. §§ 469.001-469.047. The Authority is governed by a five-member Board, appointed by the Lake County Board of Commissioners. The Board is organized with a chair, vice chair, and a secretary-treasurer, elected annually. At December 31, 2004, there are four Board members and one vacancy.

Component Unit

The Lake County Housing and Redevelopment Authority is considered to be a component unit of Lake County and is included in Lake County's annual financial report.

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

1. Summary of Significant Accounting Policies (Continued)

B. Basic Financial Statements

1. Government-Wide Statements

The government-wide financial statements (the statement of net assets and the statement of activities) display information about the government. These statements include the financial activities of the overall Authority government. Eliminations have been made to minimize the double counting of internal activities. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges to external parties for support.

In the government-wide statement of net assets, both the governmental and business-type activities columns: (a) are presented on a consolidated basis by column; and (b) are reported on a full accrual, economic resource basis, which recognizes all long-term assets and receivables as well as long-term debt and obligations.

The Authority'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 statement of activities demonstrates the degree to which the direct expenses of each function of the Authority's governmental activities and business-type activities are offset by program revenues. Direct expenses are those clearly identifiable with a specific function or activity. Program revenues include: (1) fees, fines, and charges paid by the recipients of goods, services, or privileges provided by a given function or activity; and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or activity. Revenues that are 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 Authority's funds. Separate statements for each fund--governmental and proprietary--are presented.

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

1. Summary of Significant Accounting Policies

B. Basic Financial Statements

2. Fund Financial Statements (Continued)

Proprietary fund operating revenues, such as charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as subsidies and investment earnings, result from nonexchange transactions or incidental activities.

The Authority reports the following major governmental fund:

- The General Fund is the Authority's primary operating fund. It accounts for all financial resources of the general government not accounted for in other funds.

The Authority reports the following major enterprise fund:

- The Silverpointe Enterprise Fund is used to account for the operations of a 25-unit senior housing facility in Silver Bay, Minnesota. The facility is owned by the Authority and was built to provide quality and affordable housing for senior citizens in Lake County. Silverpointe is operated similar to a business enterprise. The intent of the Authority is that the cost of providing housing services to the general public, on a continuing basis, is financed or recovered primarily through user charges.

C. Measurement Focus and Basis of Accounting

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

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, 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. The Lake County Housing and Redevelopment Authority considers all revenues to be available if they are collected within 90 days after the end of the current period. Property and other taxes, licenses, and interest are all considered to be susceptible to accrual.

Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, and claims and judgments, which are recognized as expenditures to the extent that they have matured. Proceeds of general 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 Authority's policy to use restricted resources first, then unrestricted resources as they are needed.

D. Budget

The Authority does not prepare budgets for the General Fund operations. Expenditures are made in accordance with the tax increment financing plans for the Tax Increment Financing Districts. An estimated operating budget is prepared by the management company for the Silverpointe Enterprise Fund. The budget is prepared on an accrual basis. The budget is approved and can be adjusted by the Board.

E. Assets, Liabilities, and Net Assets or Equity

1. Cash and Cash Equivalents

The Authority's cash and cash equivalents consist of savings and checking accounts, cash on hand, and certificates of deposit, and do not include restricted accounts.

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

1. Summary of Significant Accounting Policies

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

2. Receivables and Payables

All outstanding balances between funds are reported as “due to/from other funds.” Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as “internal balances.”

Property taxes, including property taxes captured as tax increments, 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 on May 15 and the second half payment due October 15. The Authority approved an annual levy for operating purposes. Property taxes, including tax increment, are collected by Lake County.

Unpaid taxes at December 31 become liens on the respective property and are classified in the financial statements as taxes receivable.

3. Restricted Assets

Certain funds of the Authority are classified as restricted assets on the statement of net assets because the restriction is either imposed by law through constitutional provisions or enabling legislation or imposed externally by creditors, grantors, contributors, or laws or regulations of other governments. Therefore, their use is limited by applicable laws and regulations.

4. Capital Assets

Capital assets, which include land, buildings and structures, and equipment, are reported in the applicable governmental or business-type activities column in the government-wide financial statements. Capital assets are defined by the government as assets with an initial, individual cost of more than \$1,000 and have an expected life of at least five years. Such assets are recorded at historical cost.

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.

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

1. Summary of Significant Accounting Policies

E. Assets, Liabilities, and Net Assets or Equity

4. Capital Assets (Continued)

Buildings and structures, and equipment of the Authority is depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Buildings and structures	25 - 40
Equipment	7

5. Deferred Revenue

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

6. Long-Term Obligations

In the government-wide financial statements, and proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities, or proprietary fund type statement of net assets.

7. Fund Equity

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose.

8. 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.

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

2. Prior Period Restatement

An adjustment was made to the Authority's General Fund prior year fund balance to account for a change in revenue recognition for receivables. Prior year receivables that were not collected within the Authority's period of availability should be shown as deferred revenue.

Fund Balance - December 31, 2003, as reported	\$	(126,328)
Restatement		<u>(116,005)</u>
Fund Balance - December 31, 2003, as restated	\$	<u>(242,333)</u>

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

The Authority's total cash and cash equivalents are reported as follows:

Unrestricted		
Cash and cash equivalents	\$	65,004
Cash in transit		3,914
Restricted assets		
Cash		
Debt service		69,198
Customer deposits		<u>9,619</u>
Total Cash	\$	<u>147,735</u>

Minn. Stat. §§ 118A.02 and 118A.04 authorize the Authority to deposit its cash and to invest in certificates of deposit in financial institutions. At December 31, 2004, the carrying amount of the Authority's deposits totaled \$140,364. The bank balance deposit amount was \$140,267. Minnesota statutes require that all County deposits be covered by insurance, surety bond, or collateral.

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments (Continued)

Following is a summary of the deposits covered by insurance or collateral at December 31, 2004.

	<u>Bank Balance</u>
Covered Deposits	
Insured, or collateralized with securities held by the Authority or its agent in the Authority's name	<u>\$ 140,267</u>

Included as cash on Exhibit 1 is \$3,457 held by the Lake County Treasurer for the Authority.

Three levels of custodial credit risk for securities are defined by generally accepted accounting principles:

- (1) securities that are insured or registered, or for which the securities are held by the County or its agent in the County's name;
- (2) securities that are uninsured and unregistered and are held by the counterparty's trust department or agent in the County's name; and
- (3) securities that are uninsured and unregistered and are held by the counterparty, or by its trust department or agent, but not in the County's name.

At December 31, 2004, the Authority did not own any investments that required classification regarding custodial credit risk.

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets (Continued)

2. Receivables

Receivables as of December 31, 2004, for the Authority's governmental activities are as follows:

	Total Receivables	Amounts Not Scheduled for Collection During the Subsequent Year
Governmental Activities		
Taxes	\$ 10,413	\$ -
Accounts receivable	119,771	-
Accrued interest	75	-
Due from other governments	68,632	-
Due from Lake County	2,538	-
Loans receivable	83,000	55,000
Total Governmental Activities	\$ 284,429	\$ 55,000

There were no receivables for the Silverpointe Enterprise Fund at December 31, 2004.

3. Loan Receivable

The Authority has an \$83,000 loan receivable from North Shore Business Enterprise Center, Inc., an unrelated non-profit organization. The loan is without interest. Annual principal payments are scheduled of \$28,000 due on September 1, 2005, \$28,000 due on September 1, 2006, and the final payment of \$27,000 due on September 1, 2007.

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets (Continued)

4. Capital Assets

Capital asset activity for the year ended December 31, 2004, was as follows:

Governmental Activities

	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets, not Depreciated				
Land	\$ 208,629	\$ -	\$ -	\$ 208,629
Capital assets depreciated				
Buildings and structures	\$ 1,250,973	\$ -	\$ -	\$ 1,250,973
Less: accumulated depreciation for				
Buildings and structures	215,963	31,670	-	247,633
Total capital assets, depreciated, net	\$ 1,035,010	\$ (31,670)	\$ -	\$ 1,003,340
Governmental Activities Capital Assets, Net	\$ 1,243,639	\$ (31,670)	\$ -	\$ 1,211,969

Business-Type Activities

	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets depreciated				
Buildings and structures	\$ 1,879,117	\$ -	\$ -	\$ 1,879,117
Equipment	3,911	-	-	3,911
Total capital assets Depreciated	\$ 1,883,028	\$ -	\$ -	\$ 1,883,028
Less: accumulated depreciation for				
Buildings and structures	\$ 309,271	\$ 46,978	\$ -	\$ 356,249
Equipment	3,399	512	-	3,911
Total accumulated Depreciation	\$ 312,670	\$ 47,490	\$ -	\$ 360,160
Business-Type Activities Capital Assets, Net	\$ 1,570,358	\$ (47,490)	\$ -	\$ 1,522,868

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

4. Capital Assets (Continued)

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

Governmental Activities	
Urban and economic development	\$ 31,670
Business-Type Activities	
Senior housing	\$ 47,490

B. Interfund Receivables, Payables, and Transfers

The composition of interfund balances as of December 31, 2004, is as follows:

Due To/From Other Funds

Receivable Fund	Payable Fund	Amount
General Fund	Silverpointe Enterprise Fund	\$ 14,380

C. Liabilities

1. Long-Term Debt

Governmental Activities

Types of Indebtedness	Final Maturity	Installment Amounts	Interest Rates (%)	Original Issue Amount	Outstanding Balance December 31, 2004
1996 General Obligation Jail Lease Revenue Bonds	2007	\$95,000- \$155,000	4.00 to 5.10	\$ 1,245,000	\$ 440,000

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities

1. Long-Term Debt (Continued)

Business-Type Activities

Types of Indebtedness	Final Maturity	Installment Amounts	Interest Rates (%)	Original Issue Amount	Outstanding Balance December 31, 2004
1996 General Obligation Senior Housing Bonds	2027	Varies	3.92	\$ 1,160,642	\$ 1,028,962

2. Debt Service Requirements

Debt service requirements at December 31, 2004, were as follows:

Governmental Activities

Year Ending December 31	Revenue Bonds	
	Principal	Interest
2005	\$ 140,000	\$ 18,585
2006	145,000	11,530
2007	155,000	3,953
Total	<u>\$ 440,000</u>	<u>\$ 34,068</u>

Business-Type Activities

Year Ending December 31	Revenue Bonds	
	Principal	Interest
2005	\$ 30,100	\$ 39,076
2006	30,589	38,609
2007	31,810	37,388
2008	33,079	36,119
2009	34,400	34,798
2010-2014	193,723	152,267
2015-2019	235,594	110,396
2020-2024	286,514	59,476
2025-2027	153,153	7,317
Total	<u>\$ 1,028,962</u>	<u>\$ 515,446</u>

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities (Continued)

3. Changes in Long-Term Liabilities

Governmental Activities

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Bonds payable					
General Obligation Jail					
Lease Revenue Bonds	\$ 575,000	\$ -	\$ 135,000	\$ 440,000	\$ 140,000

Business-Type Activities

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
Bonds payable					
General Obligation					
Senior Housing Bonds	\$ 1,056,781	\$ -	\$ 27,819	\$ 1,028,962	\$ 30,100

4. Summary of Significant Contingencies and Other Items

A. Tax Increment Financing Districts

The Authority administers the following tax increment financing districts established pursuant to Minn. Stat. §§ 469.174-469.1791.

District Number 2	Blue Water/Superior Shores Project
District Number 3	Cove Point Project
District Number 4	Incubator Building Project

The bonds outstanding for District Nos. 2 and 3 are general obligation bonds issued by Lake County and are included in the Lake County financial statements. The bonds do not constitute a debt of the Authority. The County collects and pays the debt service payments pursuant to the amended Tax Increment Pledge Agreement, and the Authority recognizes the tax increment revenues and operating transfers to Lake County in its financial statements.

LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA

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

B. Risk Management

The Authority 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. To manage these risks, the Authority has joined the Minnesota Counties Insurance Trust (MCIT). The Authority retains risk for the deductible portions of the insurance policies. The amounts of these deductibles are considered immaterial to the financial statements. 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.

C. Related-Party Transactions - Lake County

The Lake County Housing and Redevelopment Authority is a discretely presented component unit of Lake County. During 1996, the Authority issued \$1,245,000 in General Obligation Jail Lease Revenue Bonds, which have \$440,000 outstanding at December 31, 2004. The bonds were issued to finance the jail portion of the County Law Enforcement Center. The jail is owned by the Authority and is leased to Lake County. The County makes lease payments in the amounts necessary to make the bond principal and interest payments each year. When all of the bonds have been paid off, the title to the jail will pass to the County. Because the debt is essentially an obligation of the County, it is shown as County debt in the Lake County financial statements. It is also shown as debt in the separately issued financial statements of the Lake County Housing and Redevelopment Authority because the Authority issued the bonds.

D. Tax Increment Assistance

The Lake County Housing and Redevelopment Authority is committed to provide tax increment assistance pursuant to the Northshore Business Enterprise Center development agreement. The assistance is provided in the form of an annual tax rebate to the developer. The annual tax rebate is contingent upon payment of annual property taxes by the developer. The assistance for the project is limited in amount based on both the scope of the project and the life of the tax increment district. The tax increment assistance does not result in debt proceeds and does not meet the definition of debt.

**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

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

E. Conduit Debt Obligation

The Lake County Housing and Redevelopment Authority has issued the Health Care Facilities Revenue Bonds, Series 2000, originally issued for \$5,000,000 in May 2000 and refinanced in October 2003 for \$4,108,000, to provide financial assistance to First Plan of Minnesota to construct two medical clinics. The bonds are secured by the property financed through a loan agreement and are payable solely from the revenues of First Plan of Minnesota. Neither the Authority nor the state is obligated in any manner for repayment of the bonds. Accordingly, the bonds are not reported as a liability in the accompanying financial statements.

F. Financial Condition

The Authority's expenses, including required payments to Lake County pursuant to bond obligations, exceed current tax increment financing and other revenues. This continuing condition has resulted in a deficit balance of unrestricted net assets. Under current agreements and regulations, it appears the financial condition of the Authority will continue to deteriorate. The Authority's Board is looking into ways to improve its financial condition, including working with other similarly situated parties and the Minnesota Legislature to amend tax increment laws. The Authority is also in discussion with Lake County regarding its current obligations and the availability of alternative revenue sources.

The ability of the Authority to continue as a going concern is dependent on its ability to generate additional revenues and/or limit its current debt obligations to provide sufficient net cash flow to fund its daily and long-term obligations. The financial statements do not include any adjustments that might be necessary if the Authority is unable to continue as a going concern.

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**LAKE COUNTY HOUSING AND REDEVELOPMENT AUTHORITY
TWO HARBORS, MINNESOTA**

**SCHEDULE OF FINDINGS AND RECOMMENDATIONS
FOR THE YEAR ENDED DECEMBER 31, 2004**

I. FINANCIAL STATEMENT AUDIT--INTERNAL CONTROLS

PREVIOUSLY REPORTED ITEM NOT RESOLVED

98-1 Segregation of Duties

The Lake County Housing and Redevelopment Authority has no employees, and operations are handled by the contracted attorney and Board members. These operations are reported to the Board by the contracted accounting firm. The Authority does not have segregation of accounting functions necessary to ensure adequate internal accounting control. This is not unusual in operations the size of the Authority.

We recommend that management be aware of this condition.

Client's Response:

The HRA will continue to be aware of the problems of carrying on operations as a very small entity.

II. MANAGEMENT PRACTICES

PREVIOUSLY REPORTED ITEMS NOT RESOLVED

98-2 Development Agreement Billings

The Authority has a development agreement that includes a tax increment financing guarantee on the Cove Point project. The agreement guarantees a minimum amount of tax increments to be collected on the project. Any deficiency of tax increments collected under the guarantee will be paid to the Authority by the Developer. The tax increments collected on the property have not met the guarantee in any year since 1997. The deficient amounts for the years 1998 to 2004 have not been billed to the Developer by the Authority and, at December 31, 2004, total \$118,851.

We recommend that the Authority review the development agreement to ascertain that billings are being prepared and collected on a timely basis.

Client's Response:

The HRA intends to complete Cove Point billing in 2005 and avoid projects which require that the LCHRA pay consulting fees for other entities. If these are considered essential to our purpose, we can include a 10% surcharge if accounts are not paid in 60 days, and require duplicate bills from consultants so the LCHRA can easily bill them every 30 days. At one time, the HRA could afford to bank roll these projects. Now that is not possible.

03-1 Financial Condition

The Authority's financial statements are prepared based on the assumption that the Authority will continue as a going concern in the future. As a result of the Authority's current financial condition, it is questionable how long the Authority will continue to be a going concern because of its inability to meet its obligations as they become due without assistance.

The General Fund's fund balance has steadily decreased from a positive \$829,048 at December 31, 1997, to a negative \$427,750 at December 31, 2004. This is a result of tax increment revenues decreasing from \$501,092 in 1998 to \$243,970 in 2004. Class rate changes and the fiscal disparity tax have decreased the amount of tax increments collected. Future tax increment collections will likely not be sufficient to fund future debt service.

We recommend the Authority develop a formal plan that would outline how the Authority intends to improve its current financial condition. The Authority may wish to consider liquidating certain assets, restructuring existing debt, reducing expenditures, and obtaining other sources of revenue.

Client's Response:

The LCHRA understands that only grave measures can assure our continued existence. Plans in process in 2005:

- 1. Bill and collect funds owed to the HRA*
- 2. Expand marketing efforts at Silverpointe to include non-seniors*

Plans for 2006:

- 1. Reduce monthly expenses: Cut down accounting fees, meeting costs, attorney fees, and reduce frequency of meetings.*
- 2. Improve our relationship with the County Board*
- 3. Try to restructure Debt, find other sources of revenue, and sell property.*

PREVIOUSLY REPORTED ITEM RESOLVED

Investment Policy (96-2)

The Authority does not have a formal investment policy to provide guidance in the investment decision-making process.

Resolution

The Authority has done little or no investing the past few years due to minimal funds. If and when funds become available to invest, the Authority will use the Lake County Investment Policy as a guideline.

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PATRICIA ANDERSON
STATE AUDITOR

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

Board of County Commissioners
Lake County Housing and
Redevelopment Authority

We have audited the financial statements of the Lake County Housing and Redevelopment Authority as of and for the year ended December 31, 2004, and have issued our report thereon dated August 10, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Lake County Housing and Redevelopment Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted a matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Authority's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. A reportable condition is described in the accompanying Schedule of Findings and Recommendations as item 98-1.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by

employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we do not believe the reportable condition indicated above is a material weakness.

Compliance and Other Matters

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

Minnesota Legal Compliance

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

The *Minnesota Legal Compliance Audit Guide for Local Government* contains five categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, and claims and disbursements. Our study included all of the listed categories, except that we did not test for compliance in contracting and bidding, because the Lake County Housing and Redevelopment Authority did not enter into any applicable contracts.

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

This report is intended solely for the information and use of the Board and management and is not intended to be, and should not be, used by anyone other than those specified parties.

/s/Pat Anderson

PATRICIA ANDERSON
STATE AUDITOR

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

End of Fieldwork: August 10, 2005