

STATE OF MINNESOTA

Office of the State Auditor



Rebecca Otto
State Auditor

HOUSTON COUNTY
CALEDONIA, MINNESOTA

YEAR ENDED DECEMBER 31, 2012

Description of the Office of the State Auditor

The mission of the Office of the State Auditor is to oversee local government finances for Minnesota taxpayers by helping to ensure financial integrity and accountability in local governmental financial activities.

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

The State Auditor performs approximately 160 financial and compliance audits per year and has oversight responsibilities for over 3,300 local units of government throughout the state. The office currently maintains five divisions:

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

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

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

Pension - monitors investment, financial, and actuarial reporting for approximately 730 public pension funds; and

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

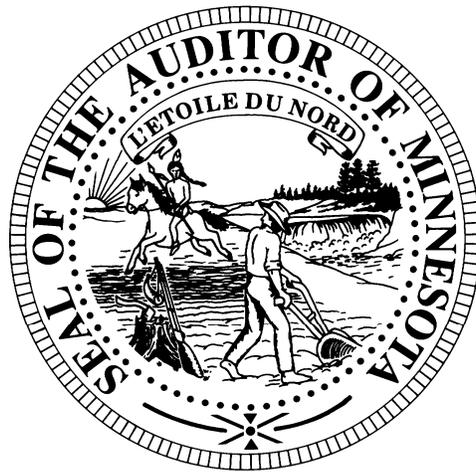
The State Auditor serves on the State Executive Council, State Board of Investment, Land Exchange Board, Public Employees Retirement Association Board, Minnesota Housing Finance Agency, and the Rural Finance Authority Board.

Office of the State Auditor
525 Park Street, Suite 500
Saint Paul, Minnesota 55103
(651) 296-2551
state.auditor@osa.state.mn.us
www.auditor.state.mn.us

This document can be made available in alternative formats upon request. Call 651-296-2551 [voice] or 1-800-627-3529 [relay service] for assistance; or visit the Office of the State Auditor's web site: www.auditor.state.mn.us.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

Year Ended December 31, 2012



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

This page was left blank intentionally.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

TABLE OF CONTENTS

	<u>Exhibit</u>	<u>Page</u>
Introductory Section		
Current Organization Chart		1
Financial Section		
Independent Auditor's Report		2
Management's Discussion and Analysis		5
Basic Financial Statements		
Government-Wide Financial Statements		
Statement of Net Position	1	13
Statement of Activities	2	14
Fund Financial Statements		
Governmental Funds		
Balance Sheet	3	15
Reconciliation of Governmental Funds Balance Sheet to the Government-Wide Statement of Net Position--Governmental Activities	4	17
Statement of Revenues, Expenditures, and Changes in Fund Balance	5	18
Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balance of Governmental Funds to the Government-Wide Statement of Activities--Governmental Activities	6	19
Fiduciary Funds		
Statement of Fiduciary Net Position	7	20
Notes to the Financial Statements		21
Required Supplementary Information		
Budgetary Comparison Schedules		
General Fund	A-1	49
Road and Bridge Special Revenue Fund	A-2	52
Social Services Special Revenue Fund	A-3	53
Schedule of Funding Progress - Other Postemployment Benefits	A-4	54
Notes to the Required Supplementary Information		55

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

TABLE OF CONTENTS

	<u>Exhibit</u>	<u>Page</u>	
Financial Section (Continued)			
Supplementary Information			
Combining and Individual Fund Financial Statements			
Nonmajor Governmental Funds		56	
Combining Balance Sheet	B-1	57	
Combining Statement of Revenues, Expenditures, and Changes in Fund Balance	B-2	58	
Budgetary Comparison Schedule			
Debt Service Fund	B-3	59	
Agency Funds		60	
Combining Statement of Changes in Assets and Liabilities - All Agency Funds	C-1	61	
Other Schedules			
Schedule of Intergovernmental Revenue	D-1	65	
Schedule of Expenditures of Federal Awards	D-2	67	
Notes to the Schedule of Expenditures of Federal Awards		70	
Management and Compliance Section			
Schedule of Findings and Questioned Costs		72	
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>			80
Report on Compliance for Each Major Federal Program and Report on Internal Control Over Compliance		83	

This page was left blank intentionally.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

ORGANIZATION
DECEMBER 31, 2012

			<u>Term Expires</u>
Elected			
Commissioners			
Chair	Jack Miller ⁴	District 1	January 2013
Board Member	Justin Zmyewski ¹	District 2	January 2015
Board Member	Steve Schuldt	District 3	January 2013
Board Member	Teresa Walter ²	District 4	January 2015
Vice Chair	Thomas Bjerke ⁵	District 5	January 2013
Attorney	Jamie Hammell		January 2015
Auditor	Char Meiners		January 2015
County Recorder	Beverly Bauer		January 2015
County Sheriff	Doug Ely		January 2015
District Judge	James Fabian		January 2014
Treasurer	Donna Trehus		January 2015
Appointed			
Assessor	Thomas Dybing		December 2016
County Engineer	Brian Pogodzinski		April 2013
Coroner	Regional Medical Center		Indefinite
Court Administrator	Darlene Larson		Indefinite
Finance Director	Carol Lapham		Indefinite
Human Services Director	Linda Bahr ³		Indefinite
Public Health Nurse	Debra Rock		Indefinite
Veterans Service Officer	Robert Gross		December 2015

¹Chair 2013

²Vice Chair 2013

³Interim Appointment

⁴Replaced with Judy Storlie January 2013

⁵Replaced with Dana Kjome January 2013

This page was left blank intentionally.

This page was left blank intentionally.



REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

SUITE 500
525 PARK STREET
SAINT PAUL, MN 55103-2139

(651) 296-2551 (Voice)
(651) 296-4755 (Fax)
state.auditor@state.mn.us (E-mail)
1-800-627-3529 (Relay Service)

INDEPENDENT AUDITOR'S REPORT

Board of County Commissioners
Houston County

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Houston County as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the County's basic financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the County's preparation and fair presentation of the

financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

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 of Houston County as of December 31, 2012, and the respective changes in financial position thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Required Supplementary Information as listed in the table of contents be presented to supplement the basic financial statements. Such information, although not part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Supplementary Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise Houston County's basic financial statements. The supplementary information as listed in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and

prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated September 27, 2013, on our consideration of Houston 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 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* in considering Houston County’s internal control over financial reporting and compliance.

Report on Schedule of Expenditures of Federal Awards Required by OMB Circular A-133

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the basic financial statements. The accompanying Schedule of Expenditures of Federal Awards (SEFA) 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 is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the SEFA is fairly stated in all material respects in relation to the basic financial statements as a whole.

/s/Rebecca Otto

REBECCA OTTO
STATE AUDITOR

September 27, 2013

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

This page was left blank intentionally.

MANAGEMENT'S DISCUSSION AND ANALYSIS

This page was left blank intentionally.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2012
(Unaudited)**

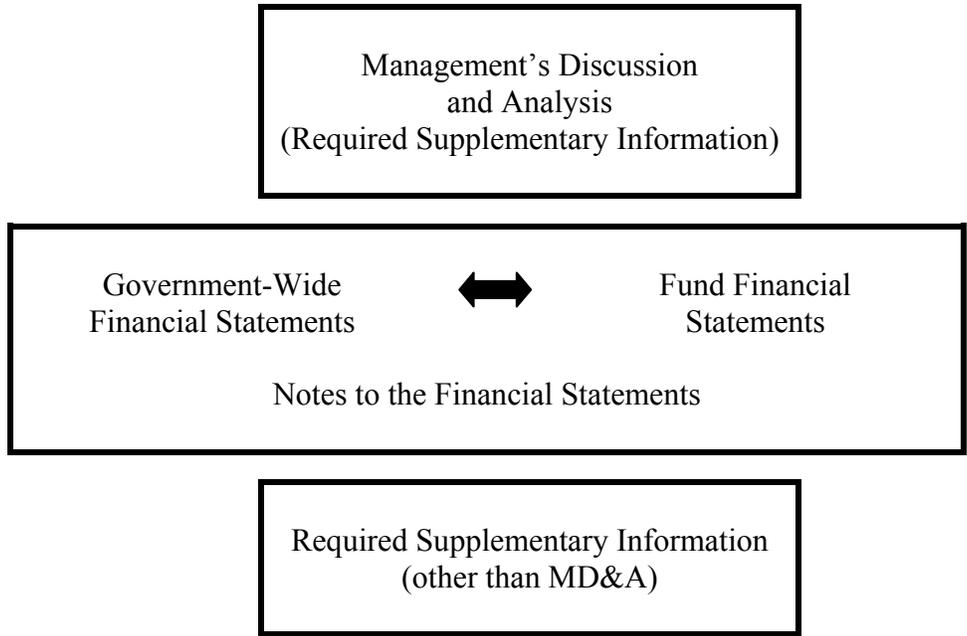
Houston County's discussion and analysis provides an overview of the County's financial activities for the fiscal year ended December 31, 2012. Since this information is designed to focus on current year activities, resulting changes, and currently known facts, it should be read in conjunction with the County's financial statements.

FINANCIAL HIGHLIGHTS

- Governmental activities' total net position are \$78,843,954, of which \$59,258,579 is in net investment in capital assets and \$6,778,561 is restricted to specific purposes.
- Houston County's net position increased by \$3,492,536 for the year ended December 31, 2012.
- The net cost of governmental activities for the current fiscal year was \$8,503,633. The net cost was funded by general revenues, including taxes and grants.
- Governmental funds' fund balances increased by \$2,266,421.

OVERVIEW OF THE FINANCIAL STATEMENTS

This Management's Discussion and Analysis (MD&A) is intended to serve as an introduction to the basic financial statements. Houston County's basic financial statements consist of three parts: government-wide financial statements, fund financial statements, and notes to the financial statements. The MD&A (this section) and certain budgetary comparison schedules are required to accompany the basic financial statements and, therefore, are included as required supplementary information. The following chart demonstrates how the different pieces are interrelated.



There are two government-wide financial statements. The Statement of Net Position and the Statement of Activities (Exhibits 1 and 2) provide information about the activities of the County as a whole and present a longer-term view of the County's finances. Government-wide financial statements start on page 13. For governmental activities, these statements tell how these services were financed in the short term as well as what remains for future spending. Fund financial statements also report the County's operations in more detail than the government-wide statements by providing information about the County's most significant funds. The remaining statements provide financial information about activities for which the County acts solely as an agent for the benefit of those outside of the government.

Government-Wide Financial Statements--The Statement of Net Position and the Statement of Activities

Our analysis of the County as a whole is shown on Exhibits 1 and 2. The Statement of Net Position and the Statement of Activities report information about the County as a whole and about its activities in a way that helps the reader determine whether the County's financial condition has improved or declined as a result of the year's activities. These statements include all assets and liabilities using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the County's net position and changes in them. You can think of the County's net position--the difference between assets and liabilities--as one way to measure the County's financial health or financial position. Over time, increases or decreases in the County's net position are one indicator of whether its financial health is improving or deteriorating. You will need to consider other nonfinancial factors, however, such as changes in the County's property tax base and the condition of County roads, to assess the overall health of the County.

The Statement of Activities presents information showing how the County's net position changed during the year. All changes in net position 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 years. The activities of Houston County are presented as governmental activities because they are principally supported by taxes and intergovernmental revenues. The County's basic services are reported here, including general government, public safety, transportation, sanitation, human services, culture and recreation, conservation of natural resources, and economic development.

Fund Financial Statements

Our analysis of the County's major funds begins on page 15. The fund financial statements provide detailed information about the significant funds--not the County as a whole. Some funds are required to be established by state law. However, the County Board establishes some funds to help it control and manage money for a particular purpose or to show that it is meeting legal responsibilities for using certain taxes, grants, and other money.

The County's basic services are reported in governmental funds, which focus on how money flows into and out of those funds and the balances left at year-end that are available for spending. These funds are reported using an accounting method called modified accrual accounting. This method measures cash and all other financial assets that can be readily converted to cash. The governmental fund statements provide a detailed short-term view of the County's general government operations and the basic services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the County's programs. We describe the relationship (or differences) between governmental activities (reported in the Statement of Net Position and the Statement of Activities) and governmental funds in a reconciliation in a statement following each governmental fund financial statement.

Reporting the County's Fiduciary Responsibilities

The County is the trustee, or fiduciary, over assets that can be used only by other governments, nonprofits, or individuals. All of the County's fiduciary activities are reported in a separate Statement of Fiduciary Net position. We exclude these activities from the County's other financial statements because the County cannot use these assets to finance its operations.

THE COUNTY AS A WHOLE

The County's net position increased from \$75,351,418 to \$78,843,954.

Table 1
Net Position
(in Millions)

	<u>2012</u>	<u>2011</u>
Current and other assets	\$ 24.0	\$ 23.9
Capital assets	<u>77.1</u>	<u>76.7</u>
Total Assets	<u>\$ 101.1</u>	<u>\$ 100.6</u>
Long-term debt outstanding	\$ 18.8	\$ 19.2
Other liabilities	<u>3.5</u>	<u>6.1</u>
Total Liabilities	<u>\$ 22.3</u>	<u>\$ 25.3</u>
Net Position		
Net investment in capital assets	\$ 59.3	\$ 58.0
Restricted	6.7	5.7
Unrestricted	<u>12.8</u>	<u>11.6</u>
Total Net Position	<u>\$ 78.8</u>	<u>\$ 75.3</u>

Net position of the County's governmental activities increased by 4.6 percent (\$78,843,954 compared to \$75,351,418).

Table 2
Changes in Net Position
(in Millions)

	<u>2012</u>	<u>2011</u>
Revenues		
Program revenues		
Fees, fines, charges, and other	\$ 2.5	\$ 2.5
Operating grants and contributions	12.7	10.2
Capital grants and contributions	0.9	0.5
General revenues		
Property taxes	9.6	8.8
Other taxes and payments in lieu of taxes	0.5	0.5
Grants and contributions	1.2	1.8
Other general revenues	<u>0.6</u>	<u>0.7</u>
Total Revenues	<u>\$ 28.0</u>	<u>\$ 25.0</u>

	2011	2011
Program expenses		
General government	\$ 3.9	\$ 3.4
Public safety	3.7	4.5
Transportation	8.8	6.8
Human services	3.9	3.7
Health	1.7	1.7
Sanitation	0.8	0.8
Culture and recreation	0.3	0.3
Conservation of natural resources	0.4	0.3
Economic development	0.3	0.1
Interest	0.7	0.5
	<hr/>	<hr/>
Total Program Expenses	\$ 24.5	\$ 22.1
	<hr/>	<hr/>
Increase (Decrease) in Net Position	\$ 3.5	\$ 2.9

Governmental Activities

The cost of all governmental activities this year was \$24,526,858. However, as shown in the Statement of Activities, the amount that the taxpayers ultimately financed for these activities through County property taxes was only \$9,573,946, because some of the cost was paid by those who directly benefited from the programs (\$2,497,223) or by other governments and organizations that subsidized certain programs with grants and contributions (\$13,526,002). The County paid for the remaining “public benefit” portion of governmental activities with \$11,996,169 in general revenues, primarily property taxes and other revenues, such as interest and general entitlements, resulting in an increase to net position of \$3,492,536.

Table 3 presents the cost of each of the County’s four largest program functions, as well as each function’s net cost (total cost, less revenues generated by the activities). The net cost shows the financial burden that was placed on the County’s taxpayers by each of these functions.

Table 3
Governmental Activities
(in Millions)

	Total Cost of Services		Net Cost of Services	
	2012	2011	2012	2011
Transportation	\$ 8.8	\$ 6.8	\$ (0.2)	\$ (0.7)
Human services	3.9	3.6	1.2	0.9
General government	3.9	3.4	2.9	2.7
Public safety	3.7	4.4	2.8	4.0

FINANCIAL ANALYSIS OF THE COUNTY'S FUNDS

As noted earlier, Houston County uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The focus of the County's funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the County's financing requirements. In particular, unrestricted fund balance may serve as a useful measure of a county's net resources available for spending at the end of the year.

At December 31, 2012, Houston County's governmental funds reported combined ending fund balances of \$14,501,366, an increase of \$2,266,421 in comparison with 2011. The County is reporting an unassigned fund balance of \$3,889,877 in 2012. The remainder of fund balance is nonspendable, restricted, committed, or assigned to indicate that it is not available for new spending because it has already been committed.

The General Fund is the chief operating fund of Houston County. At December 31, 2012, unassigned fund balance was \$3,894,593, while total fund balance was \$4,946,799. As a measure of the General Fund's liquidity, it may be useful to compare both unassigned fund balance and total fund balance to total fund expenditures. Unassigned fund balance represents 35.0 percent of total General Fund expenditures, while total fund balance represents 44.4 percent of the same amount. The 2012 General Fund final budget reflected a \$752,734 deficit which included bond principal and interest payments that were a carryover expenditure of 2011 levy funds. A combination of prior year receipts of grant funding for the ARMER project and County departments collecting fees and reducing expenditures resulted in a fund balance reduction of just \$19,307.

The Road and Bridge Special Revenue Fund's fund balance increased by \$1,813,808 to \$7,282,073 of which \$5,971,177 is assigned. Road and Bridge saw increased revenues in the form of reimbursements from FEMA for the 2008 flood and from MnDot State Aid for past construction expenditures. In addition, both maintenance and construction departments had projects postponed from 2012 to 2013, and the maintenance department underspent funds due to mild winter weather and temporary staff reduction. Also included in the fund balance figure is money levied for two future CR 249 bridge projects.

The Social Services Special Revenue Fund's fund balance increased by \$103,600 to \$1,459,644 of which all is assigned. A significant increase in MA Estate Recoveries along with a salary savings in Human Services' administration staffing account for a significant percentage of the addition to fund balance.

General Fund Budgetary Highlights

Houston County revised its General Fund budget during 2012, increased both expected revenues and appropriations by 0.1 and 1.3 percent, respectively. For the year ended December 31, 2012, expenditures were less than final budget by \$876,034.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At the end of 2012, the County had \$77,100,443 invested in a broad range of capital assets, including land, buildings, highways and streets, and equipment. (See Table 4.) This amount represents a net increase (including additions and deductions) of \$377,823, or 0.4 percent, over last year.

Table 4
Capital Assets at Year-End
(Net of Depreciation, in Millions)

	<u>2012</u>	<u>2011</u>
Land	\$ 3.0	\$ 3.0
Construction in progress	.8	20.2
Buildings and improvements	19.4	2.2
Machinery, vehicles, furniture, and equipment	2.9	3.2
Infrastructure	<u>51.0</u>	<u>48.1</u>
Totals	<u>\$ 77.1</u>	<u>\$ 76.7</u>

Debt

Table 5
Outstanding Debt at Year-End
(in Millions)

	<u>Governmental Activities</u>	
	<u>2012</u>	<u>2011</u>
G. O. bonds	\$ 17.5	\$ 17.7
Capital notes	<u>-</u>	<u>0.3</u>
Totals	<u>\$ 17.5</u>	<u>\$ 18.0</u>

Houston County issued no additional debt in 2012.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

The County's elected and appointed officials considered many factors when setting the fiscal year 2013 budget, tax rates, and fees that will be charged for the government-type activities.

- The unemployment rate in Houston County decreased, moving from 7.2 percent in 2011 to 6.3 percent in 2012 for the annual average. While this compared favorably to the U.S. rate of 8.1 percent, the rate is higher than the Minnesota rate of 5.7 percent.
- County General Fund expenditures for 2013 are budgeted to decrease 1.8 percent over 2012.
- Houston County's population decreased by 5.4 percent from 2002 to 2012, compared to an increase of 6.2 percent in Minnesota as a whole. Citizens age 65+ comprise 19 percent of the County's population.
- The proposed property tax levy has increased 3.52 percent for 2013.
- In June 2013, Houston County incurred a natural disaster due to flooding. The resulting repairs to infrastructure were major to the County. The County was declared a natural disaster by the federal government.
- During 2013, Houston County Officials will be discussing options for repair or replacement of the County Highway facility.

CONTACTING HOUSTON COUNTY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the County's finances and to show the County's accountability for the money it receives. If you have questions about this report, or need additional financial information, contact the County Finance Director, Carol Lapham, Houston County Courthouse, 304 South Marshall Street, Caledonia, Minnesota 55921.

BASIC FINANCIAL STATEMENTS

This page was left blank intentionally.

GOVERNMENT-WIDE FINANCIAL STATEMENTS

This page was left blank intentionally.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT 1

**STATEMENT OF NET POSITION
GOVERNMENTAL ACTIVITIES
DECEMBER 31, 2012**

Assets

Cash and pooled investments	\$	11,359,363
Petty cash and change funds		17,060
Investments		2,885,788
Taxes receivable		
Prior - net		221,272
Accounts receivable - net		192,177
Accrued interest receivable		33,145
Loan receivable		1,313,228
Due from other governments		7,298,703
Inventories		614,399
Prepaid items		4,066
Restricted assets		
Cash and pooled investments		69,011
Accrued interest receivable		154
Capital assets		
Non-depreciable		3,828,173
Depreciable - net of accumulated depreciation		73,272,270
		101,108,809
Total Assets	\$	101,108,809

Liabilities

Accounts payable	\$	336,062
Salaries payable		329,954
Contracts payable		249,387
Due to other governments		95,323
Accrued interest payable		246,383
Unearned revenue		880,942
Customer deposits		17,697
Advance from other governments		1,268,740
Long-term liabilities		
Due within one year		548,087
Due in more than one year		18,292,280
		22,264,855
Total Liabilities	\$	22,264,855

Net Position

Net investment in capital assets	\$	59,258,579
Restricted for		
General government		208,262
Public safety		96,128
Debt service		817,566
Highways and streets		5,379,658
Economic development		276,947
Unrestricted		12,806,814
		78,843,954
Total Net Position	\$	78,843,954

The notes to the financial statements are an integral part of this statement.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT 2

**STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2012**

	Expenses	Program Revenues			Net (Expense) Revenues and Change in Net Position
		Fees, Charges, Fines, and Other	Operating Grants and Contributions	Capital Grants and Contributions	
<u>Functions/Programs</u>					
Primary government					
Governmental activities					
General government	\$ 3,903,207	\$ 395,290	\$ 592,926	\$ -	\$ (2,914,991)
Public safety	3,664,005	94,087	795,285	-	(2,774,633)
Transportation	8,831,768	303,928	8,067,472	691,822	231,454
Sanitation	817,996	410,594	55,950	-	(351,452)
Human services	3,922,931	188,658	2,582,168	-	(1,152,105)
Health	1,671,359	1,053,747	332,568	-	(285,044)
Culture and recreation	339,751	45,888	-	-	(293,863)
Conservation of natural resources	417,097	2,734	20,855	-	(393,508)
Economic development	254,982	2,297	203,670	183,286	134,271
Interest	703,762	-	-	-	(703,762)
Total Governmental Activities	\$ 24,526,858	\$ 2,497,223	\$ 12,650,894	\$ 875,108	\$ (8,503,633)
 General Revenues					
Property taxes					\$ 9,573,946
Mortgage registry and deed tax					14,054
Other taxes					173,452
Payments in lieu of tax					357,271
Grants and contributions not restricted to specific programs					1,245,747
Unrestricted investment earnings					185,470
Miscellaneous					438,852
Gain on sale of capital assets					7,377
Total general revenues					\$ 11,996,169
Change in net position					\$ 3,492,536
Net Position - Beginning					75,351,418
Net Position - Ending					\$ 78,843,954

FUND FINANCIAL STATEMENTS

This page was left blank intentionally.

GOVERNMENTAL FUNDS

This page was left blank intentionally.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT 3

**BALANCE SHEET
GOVERNMENTAL FUNDS
DECEMBER 31, 2012**

	<u>General</u>	<u>Road and Bridge</u>	<u>Social Services</u>	<u>Nonmajor Funds</u>	<u>Total</u>
<u>Assets</u>					
Cash and pooled investments	\$ 3,499,632	\$ 6,094,764	\$ 932,375	\$ 832,592	\$ 11,359,363
Petty cash and change funds	16,960	100	-	-	17,060
Investments	886,267	1,499,521	500,000	-	2,885,788
Taxes receivable					
Prior	127,437	50,099	23,540	20,196	221,272
Accounts receivable	104,262	927	86,988	-	192,177
Loans receivable	1,313,228	-	-	-	1,313,228
Accrued interest receivable	29,580	3,032	527	6	33,145
Due from other funds	842,297	426,210	-	450,198	1,718,705
Due from other governments	266,176	6,643,586	388,941	-	7,298,703
Prepaid expense	4,066	-	-	-	4,066
Inventories	-	614,399	-	-	614,399
Restricted cash and pooled investments	69,011	-	-	-	69,011
Restricted accrued interest receivable	154	-	-	-	154
Total Assets	<u>\$ 7,159,070</u>	<u>\$ 15,332,638</u>	<u>\$ 1,932,371</u>	<u>\$ 1,302,992</u>	<u>\$ 25,727,071</u>

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

**EXHIBIT 3
(Continued)**

**BALANCE SHEET
GOVERNMENTAL FUNDS
DECEMBER 31, 2012**

	<u>General</u>	<u>Road and Bridge</u>	<u>Social Services</u>	<u>Nonmajor Funds</u>	<u>Total</u>
<u>Liabilities and Fund Balances</u>					
Liabilities					
Accounts payable	\$ 92,856	\$ 55,020	\$ 188,186	\$ -	\$ 336,062
Salaries payable	215,955	53,359	60,640	-	329,954
Contracts payable	-	200,825	-	48,562	249,387
Due to other funds	876,408	411,116	-	431,181	1,718,705
Due to other governments	77,089	3,738	14,496	-	95,323
Deferred revenue - unavailable	94,481	6,057,767	166,248	10,399	6,328,895
Deferred revenue - unearned	837,785	-	43,157	-	880,942
Customer deposits	17,697	-	-	-	17,697
Advance from other governments	-	1,268,740	-	-	1,268,740
Total Liabilities	\$ 2,212,271	\$ 8,050,565	\$ 472,727	\$ 490,142	\$ 11,225,705
Fund Balances					
Nonspendable					
Prepaid items	\$ 4,066	\$ -	\$ -	\$ -	\$ 4,066
Long-term loans/notes receivable					
	441,803	-	-	-	441,803
Inventories					
	-	614,399	-	-	614,399
Restricted for					
Debt service	-	-	-	817,566	817,566
Recorder's technology equipment					
	93,909	-	-	-	93,909
Recorder's compliance					
	111,517	-	-	-	111,517
E-911					
	29,548	-	-	-	29,548
Economic development loans					
	276,947	-	-	-	276,947
Conceal and carry					
	53,822	-	-	-	53,822
Sheriff's DUI forfeiture					
	12,758	-	-	-	12,758
Attorney forfeited property					
	2,836	-	-	-	2,836
Road and bridge projects					
	-	496,497	-	-	496,497
Committed					
Airport project	25,000	-	-	-	25,000
Road and bridge projects					
	-	200,000	-	-	200,000
Assigned					
Road and bridge	-	5,971,177	-	-	5,971,177
Human services					
	-	-	1,459,644	-	1,459,644
Unassigned					
	3,894,593	-	-	(4,716)	3,889,877
Total Fund Balances	\$ 4,946,799	\$ 7,282,073	\$ 1,459,644	\$ 812,850	\$ 14,501,366
Total Liabilities and Fund Balances	\$ 7,159,070	\$ 15,332,638	\$ 1,932,371	\$ 1,302,992	\$ 25,727,071

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT 4

**RECONCILIATION OF GOVERNMENTAL FUNDS BALANCE SHEET
TO THE GOVERNMENT-WIDE STATEMENT OF NET POSITION--GOVERNMENTAL ACTIVITIES
DECEMBER 31, 2012**

Fund balances - total governmental funds (Exhibit 3)	\$	14,501,366
Amounts reported for governmental activities in the statement of net position 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.		77,100,443
Other long-term assets are not available to pay for current period expenditures and, therefore, are deferred in the governmental funds.		6,328,895
Long-term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported in the governmental funds.		
Loans payable	\$ (42,000)	
Bonds payable	(17,540,000)	
Bond discount	44,346	
Bond premium	(74,676)	
Accrued interest payable	(246,383)	
Net OPEB obligation	(244,532)	
Compensated absences	(983,505)	
		(19,086,750)
Net Position of Governmental Activities (Exhibit 1)	\$	<u>78,843,954</u>

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT 5

**STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2012**

	<u>General</u>	<u>Road and Bridge</u>	<u>Social Services</u>	<u>Nonmajor Funds</u>	<u>Total</u>
Revenues					
Taxes	\$ 5,312,478	\$ 2,406,019	\$ 1,073,375	\$ 989,120	\$ 9,780,992
Licenses and permits	56,350	3,870	-	-	60,220
Intergovernmental	3,214,630	8,436,077	2,784,688	69,763	14,505,158
Charges for services	1,937,926	317,818	138,429	-	2,394,173
Fines and forfeits	9,299	-	-	-	9,299
Gifts and contributions	2,550	-	-	-	2,550
Investment earnings	154,335	22,313	8,615	207	185,470
Miscellaneous	431,626	12,462	1,915	-	446,003
Total Revenues	\$ 11,119,194	\$ 11,198,559	\$ 4,007,022	\$ 1,059,090	\$ 27,383,865
Expenditures					
Current					
General government	\$ 3,803,281	\$ -	\$ -	\$ -	\$ 3,803,281
Public safety	3,441,029	-	-	32,196	3,473,225
Transportation	-	9,052,376	-	-	9,052,376
Sanitation	790,332	-	-	-	790,332
Human services	-	-	3,903,422	-	3,903,422
Health	1,659,533	-	-	-	1,659,533
Culture and recreation	338,660	-	-	-	338,660
Conservation of natural resources	416,146	-	-	-	416,146
Economic development	464,371	-	-	-	464,371
Intergovernmental	-	216,591	-	-	216,591
Capital outlay	-	-	-	4,143	4,143
Debt service					
Principal	227,210	132,790	-	50,000	410,000
Interest	2,384	1,461	-	597,006	600,851
Administrative (fiscal) charges	-	-	-	7,425	7,425
Total Expenditures	\$ 11,142,946	\$ 9,403,218	\$ 3,903,422	\$ 690,770	\$ 25,140,356
Excess of Revenues Over (Under Expenditures)	\$ (23,752)	\$ 1,795,341	\$ 103,600	\$ 368,320	\$ 2,243,509
Other Financing Sources (Uses)					
Proceeds from sale of capital assets	4,445	2,932	-	-	7,377
Change in Fund Balance	\$ (19,307)	\$ 1,798,273	\$ 103,600	\$ 368,320	\$ 2,250,886
Fund Balance - January 1	4,966,106	5,468,265	1,356,044	444,530	12,234,945
Increase (decrease) in inventories)	-	15,535	-	-	15,535
Fund Balance - December 31	\$ 4,946,799	\$ 7,282,073	\$ 1,459,644	\$ 812,850	\$ 14,501,366

The notes to the financial statements are an integral part of this statement.

Page 18

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT 6

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCE OF GOVERNMENTAL FUNDS
TO THE GOVERNMENT-WIDE STATEMENT OF ACTIVITIES--GOVERNMENTAL ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2012**

Net change in fund balances - total governmental funds (Exhibit 5) \$ 2,250,886

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 revenue between the fund statements and the statement of activities is the increase or decrease in revenue deferred as unavailable.

Deferred revenue - December 31	\$ 6,328,895	
Deferred revenue - January 1	<u>(5,700,743)</u>	628,152

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. Also, in the statement of activities, only the gain or loss on the disposal of assets is reported; whereas, in the governmental funds, the proceeds from the sale increase financial resources. Therefore, the change in net position differs from the change in fund balance by the net book value of the assets sold.

Expenditures for general capital assets and infrastructure	\$ 2,619,879	
Net book value of assets disposed	(39,627)	
Current year depreciation	<u>(2,202,429)</u>	377,823

Issuing long-term debt provides current financial resources to governmental funds, while the repayment of debt consumes current financial resources. Neither transaction, however, has any effect on net position. Also, governmental funds report the net effect of issuance costs, premiums, discounts, and similar items when debt is first issued; whereas, those amounts are deferred and amortized over the life of the debt in the statement of net position.

Principal repayments		
General obligation bonds	\$ 410,000	
Current year amortization of discounts and premiums	<u>2,186</u>	412,186

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 compensated absences	\$ (29,276)	
Change in accrued interest payable	(97,672)	
Change in net OPEB obligation	(65,098)	
Change in inventories	<u>15,535</u>	<u>(176,511)</u>

Change in Net Position of Governmental Activities (Exhibit 2) \$ 3,492,536

This page was left blank intentionally.

FIDUCIARY FUNDS

This page was left blank intentionally.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT 7

**STATEMENT OF FIDUCIARY NET POSITION
FIDUCIARY FUNDS
DECEMBER 31, 2012**

	<u>Agency Funds</u>
<u>Assets</u>	
Cash and pooled investments	<u>\$ 1,281,769</u>
<u>Liabilities</u>	
Accounts payable	\$ 140,007
Due to other governments	<u>1,141,762</u>
Total Liabilities	<u><u>\$ 1,281,769</u></u>

This page was left blank intentionally.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

NOTES TO THE FINANCIAL STATEMENTS
AS OF AND FOR THE YEAR ENDED DECEMBER 31, 2012

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, 2012. The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (statements and interpretations). The more significant accounting policies established in GAAP and used by the County are discussed below.

A. Financial Reporting Entity

Houston County was established February 23, 1854, and is an organized county having the powers, duties, and privileges granted counties by Minn. Stat. ch. 373. As required by accounting principles generally accepted in the United States of America, these financial statements present Houston County (primary government) and its component unit for which the County is financially accountable. 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.

Blended Component Unit

Blended component units are legally separate organizations so intertwined with the County that they are, in substance, the same as the County and, therefore, are reported as if they were part of the County. Houston County has one blended component unit, which is reported as part of the General Fund.

<u>Component Unit</u>	<u>Component Unit Included in Reporting Entity Because</u>	<u>Separate Financial Statements</u>
Houston County Economic Development Authority (EDA) provides for development within the County.	County Commissioners are the members of the EDA Board.	Separate financial statements are not prepared.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

1. Summary of Significant Accounting Policies

A. Financial Reporting Entity (Continued)

Joint Ventures

The County participates in a joint venture described in Note 5.D. The County also participates in jointly-governed organizations described in Note 5.C.

B. Basic Financial Statements

1. Government-Wide Statements

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

The government-wide statement of net position is presented on a consolidated basis by column and 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 position is reported in three parts: (1) net investment in capital assets; (2) restricted net position; and (3) unrestricted net position. The County first utilizes restricted resources to finance qualifying activities.

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

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

1. Summary of Significant Accounting Policies

B. Basic Financial Statements (Continued)

2. Fund Financial Statements

The fund financial statements provide information about the County's funds, including its fiduciary funds and blended component unit. Separate statements for each fund category--governmental and fiduciary--are presented.

The County reports the following major governmental funds:

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

The Road and Bridge Special Revenue Fund accounts for restricted revenues from the federal and state government, as well as committed property tax revenues used for the construction and maintenance of roads, bridges, and other projects affecting County roadways.

The Social Services Special Revenue Fund accounts for restricted revenue sources from the federal, state, and other oversight agencies, as well as committed property tax revenues used for economic assistance and community social services programs.

The County reports the following fund type:

The Debt Service Fund is used to account for all financial resources restricted for payment of principal, interest, and related costs of long-term bonded debt.

The Capital Projects Fund is used to account for financial resources committed for the construction of the Criminal Justice Center.

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.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

1. Summary of Significant Accounting Policies (Continued)

C. Measurement Focus and Basis of Accounting

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

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

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

D. Assets, Liabilities, and Net Position 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, 2012, based on market prices. Pursuant to Minn. Stat. § 385.07, investment earnings on cash and pooled investments are credited to the General Fund. Other funds received investment earnings based on other state statutes, grant agreements, contracts, and bond covenants. Pooled investment earnings for 2012 were \$154,335.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Position 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 either “due to/from other funds” (the current portion of interfund loans) or “advances to/from other funds” (the noncurrent portion of interfund loans). All other outstanding balances between funds are reported as “due to/from other funds.”

Advances between funds, as reported in the fund financial statements, are offset by nonspendable fund balance to indicate they are not available for appropriation and are not expendable available financial resources.

All receivables are shown net of an allowance for uncollectibles.

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 and Prepaid Items

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

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

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

1. Summary of Significant Accounting Policies

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

4. Capital Assets

Capital assets, which include property, plant, equipment, and infrastructure assets (for example, roads, bridges, and similar items), are reported in the government-wide financial statements. Capital assets are defined by the County as assets with an initial, individual cost of more than \$10,000 and an estimated useful life in excess of two years. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair value at the date of donation.

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

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

<u>Assets</u>	<u>Years</u>
Buildings	50
Building improvements	50
Public domain infrastructure	50 - 75
Furniture, equipment, and vehicles	3 - 20

5. Compensated Absences

The liability for compensated absences reported in the financial statements consists of unpaid, accumulated annual vacation and sick leave balances. The liability has been calculated using the vesting method, in which leave amounts for both employees who currently are eligible to receive termination payments and other employees who are expected to become eligible in the future to receive such payments upon termination are included. Compensated absences are accrued when incurred in the government-wide 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.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

1. Summary of Significant Accounting Policies

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

6. Deferred Revenue

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

7. Long-Term Obligations

In the government-wide statement of net position, long-term debt and other long-term obligations are reported as liabilities. 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 another 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. Classification of Net Position

Net position in the government-wide financial statements is classified in the following categories:

Net investment in capital assets - the amount of net position representing capital assets net of accumulated depreciation and reduced by outstanding debt attributed to the acquisition, construction, or improvement of the assets.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Position or Equity

8. Classification of Net Position (Continued)

Restricted net position - the amount of net position for which external restrictions have been imposed by creditors, grantors, contributors, or laws or regulations of other governments and restrictions imposed by law through constitutional provisions or enabling legislation.

Unrestricted net position - the amount of net position that does not meet the definition of restricted or invested in capital assets, net of related debt.

9. Classification of Fund Balances

Fund balance is divided into five classifications based primarily on the extent to which the County is bound to observe constraints imposed upon the use of the resources in the governmental funds. The classifications are as follows:

Nonspendable - amounts that cannot be spent because they are not in spendable form, or legally or contractually required to be maintained intact. The “not in spendable form” criterion includes items that are not expected to be converted to cash.

Restricted - amounts for which constraints have been placed on the use of resources either externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or is imposed by law through constitutional provisions or enabling legislation.

Committed - amounts the County intends to use for the specific purposes imposed by formal action (ordinance or resolution) of the County Board. Those committed amounts cannot be used for any other purpose unless the Board removes or changes the specified use by taking the same type of action (ordinance or resolution) it employed to previously commit those amounts.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

1. Summary of Significant Accounting Policies

D. Assets, Liabilities, and Net Position or Equity

9. Classification of Fund Balances (Continued)

Assigned - amounts the County intends to use for specific purposes but do not meet the criteria to be classified as restricted or committed. In governmental funds other than the General Fund, assigned fund balance represents the remaining amount that is not restricted or committed. In the General Fund, assigned amounts represent intended uses established by the County Board or the County Finance Director who has been delegated that authority by Board resolution.

Unassigned - spendable amounts not contained in the other fund balance classifications for the General Fund. In other governmental funds, the unassigned classification is used only to report a deficit balance resulting from overspending for specific purposes for which amounts had been restricted or committed.

The County applies restricted resources first when expenditures are incurred for purposes for which either restricted or unrestricted (committed, assigned, and unassigned) amounts are available. Similarly, within unrestricted fund balance, committed amounts are reduced first followed by assigned, and then unassigned amounts when expenditures are incurred for purposes for which amounts in any of the unrestricted fund balance classifications could be used.

10. Minimum Fund Balance

Houston County has adopted a minimum fund balance policy to address cash flow or working capital needs for the General Fund and other special revenue funds, which are heavily reliant on property tax revenues to fund current operations. However, property tax revenues are not available for distribution until June. Therefore, the County Board has determined the need to maintain a minimum unassigned fund balance in the General Fund and an unrestricted (committed and assigned) fund balance in the remaining special revenue funds until the tax revenues are distributed. The County Board has determined this amount to be not less than 40 percent and not more than 65 percent of the sum of the most recent budget year's property tax levy.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

1. Summary of Significant Accounting Policies

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

11. 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. Deficit Fund Equity

The Capital Projects Fund had a deficit fund balance of \$4,716 as of December 31, 2012. The deficit can be attributed to the Criminal Justice Center project.

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

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

Government-wide statement of net position	
Governmental activities	
Cash and pooled investments	\$ 11,359,363
Petty cash and change funds	17,060
Investments	2,885,788
Restricted cash	69,011
Statement of fiduciary net position	
Cash and pooled investments	<u>1,281,769</u>
Total Cash and Investments	<u>\$ 15,612,991</u>

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments (Continued)

a. Deposits

The County is authorized by Minn. Stat. §§ 118A.02 and 118A.04 to designate a depository for public funds and to invest in certificates of deposit. The County is required by Minn. Stat. § 118A.03 to protect all County deposits with 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 and revenue obligations rated "AA" or better; irrevocable standby letters of credit issued by the Federal Home Loan Bank; and certificates of deposit. Minnesota statutes require that securities pledged as collateral be held in safekeeping in a restricted account at the Federal Reserve Bank or in an account at a trust department of a commercial bank or other financial institution not owned or controlled by the financial institution furnishing the collateral.

Custodial Credit Risk

Custodial credit risk is the risk that in the event of a financial institution failure, the County's deposits may not be returned to it. The County does not have a deposit policy for custodial credit risk. As of December 31, 2012, the County does not have any deposits exposed to custodial credit risk.

b. Investments

The County may invest in the following types of investments as authorized by Minn. Stat. §§ 118A.04 and 118A.05:

- (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;

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

b. Investments (Continued)

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

Interest Rate Risk

Interest rate risk is the risk that changes in the market interest rates will adversely affect the fair value of an investment. It is the County's policy to minimize interest rate risk by: (1) 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 prior to maturity; and (2) investing operating funds, when most prudent, 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.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

b. Investments

Interest Rate Risk (Continued)

<u>Investment Type</u>	<u>Fair Value</u>	<u>Less Than 1 Year</u>	<u>2 - 3 Years</u>	<u>3 - 13 Years</u>
Federal National Mortgage Association	\$ 170,446	\$ -	\$ -	\$ 170,446
Municipal Bonds	900,732	-	-	900,732
Negotiable certificates of deposit	2,411,727	194,885	505,209	1,711,633
Total Investments	\$ 3,482,905	\$ 194,885	\$ 505,209	\$ 2,782,811

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, as set by the Houston County Investment Policy, to invest only in securities that meet the ratings requirements of state statute.

The County is required to disclose the credit quality ratings of investments in debt securities, external investment pools, money market funds, bond mutual funds, and other pooled investments of fixed income securities. Houston County invests in the following investment pools/mutual funds:

	<u>Credit Rating</u>	<u>Rating Agency</u>	<u>Fair Value</u>
Federal National Mortgage Association	AAA/AA	Standard & Poor's	\$ 170,446
Municipal Bonds	AA3/AAA/Aa2	Moody's w/ Assured Guaranty	900,732

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

1. Deposits and Investments

b. Investments (Continued)

Custodial Credit Risk

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The County's policy is to minimize custodial credit risk by limiting investments with any one broker to no more than ten percent of its Securities Investor Protection Corporation (SIPC) coverage plus any excess coverage if provided. At December 31, 2012, none of Houston County's investments were subject to custodial credit risk.

Concentration of Credit Risk

It is the County's policy to minimize concentration of credit risk, which is the risk of loss attributed to the magnitude of the County's investment in a single issuer, by diversifying the investment portfolio so that the impact of potential losses from any one type of security or issuer will be minimized. This will be based on the applicable opinion units. Investments in any one issuer that represent five percent or more of the County's investments are as follows:

<u>Issuer</u>	<u>Percent of Total Investments</u>	<u>Reported Amount</u>
Municipal Bonds	25.9%	\$ 900,732
American Express Bank	7.2	251,714
Sallie Mae Bank	5.8	201,992
Goldman Sachs Bank	7.5	260,334
GE Capital Bank	11.5	399,661

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets (Continued)

2. Receivables

Receivables as of December 31, 2012, for the County's governmental activities, including the applicable allowances for uncollectible accounts, are as follows:

Accounts receivable, gross	\$	618,133
Less: allowance for uncollectible		(425,956)
Net Accounts Receivable	\$	192,177

The loans receivable balance of \$1,313,228 includes \$966,271, which is not scheduled for collection in the subsequent year.

3. Capital Assets

Capital asset activity for the year ended December 31, 2012, was as follows:

	Beginning Balance	Increase	Decrease	Ending Balance
Capital assets not depreciated				
Land	\$ 1,145,973	\$ -	\$ -	\$ 1,145,973
Land - infrastructure right-of-way	1,603,658	4,319	-	1,607,977
Land improvements	251,088	-	-	251,088
Construction in progress - infrastructure	20,174,495	2,408,768	21,760,128	823,135
Total capital assets not depreciated	\$ 23,175,214	\$ 2,413,087	\$ 21,760,128	\$ 3,828,173
Capital assets depreciated				
Buildings	\$ 1,794,365	\$ 17,151,842	\$ -	\$ 18,946,207
Building improvements	1,557,910	28,348	-	1,586,258
Other improvements	398,941	223,346	-	622,287
Machinery, furniture, and equipment	5,975,407	130,343	125,803	5,979,947
Infrastructure	88,646,899	4,433,041	218,352	92,861,588
Total capital assets depreciated	\$ 98,373,522	\$ 21,966,920	\$ 344,155	\$ 119,996,287

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

3. Detailed Notes on All Funds

A. Assets

3. Capital Assets (Continued)

	Beginning Balance	Increase	Decrease	Ending Balance
Less: accumulated depreciation for				
Buildings	\$ 834,152	\$ 206,106	\$ -	\$ 1,040,258
Building improvements	626,080	31,820	-	657,900
Other improvements	79,967	8,350	-	88,317
Machinery, furniture, and equipment	2,777,087	448,821	111,053	3,114,855
Infrastructure	40,508,830	1,507,332	193,475	41,822,687
 Total accumulated depreciation	 \$ 44,826,116	 \$ 2,202,429	 \$ 304,528	 \$ 46,724,017
Total capital assets depreciated, net	\$ 53,547,406	\$ 19,764,491	\$ 39,627	\$ 73,272,270
 Governmental Activities Capital Assets, Net	 \$ 76,722,620	 \$ 22,177,578	 \$ 21,799,755	 \$ 77,100,443

Depreciation expense was charged to functions/programs as follows:

Governmental Activities	
General government	\$ 99,807
Public safety	275,067
Highways and streets, including depreciation of infrastructure assets	1,794,019
Sanitation	19,253
Culture and recreation	1,091
Economic development	13,192
 Total Depreciation Expense - Governmental Activities	 \$ 2,202,429

B. Interfund Receivables, Payables, and Transfers

The composition of interfund balances as of December 31, 2012, is as follows:

1. Due To/From Other Funds

Receivable Fund	Payable Fund	Amount
General	Road and Bridge	\$ 411,116
Road and Bridge	General	426,210
Debt Service	General	450,198
General	Debt Service	431,181
 Total Due To/From Other Funds		 \$ 1,718,705

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

3. Detailed Notes on All Funds

B. Interfund Receivables, Payables, and Transfers

1. Due To/From Other Funds (Continued)

These balances reflect the interfund goods and services provided and not paid at year-end but expected to be paid in the subsequent year.

C. Liabilities

1. Loans Payable

Houston County received a grant of \$142,000 from the Minnesota Department of Employment and Economic Development. The County used the grant to make an installment loan to fund an economic development project in the County. The County is entitled to the first \$100,000 of principal and interest repayments, and the remaining \$42,000 is to be repaid to the state. Payments on the state loan are deferred until January 2013 when monthly payments of \$1,205, including interest at 6.0 percent, will be made until March 2016. Total payments due from 2013 to 2016, including interest of \$4,265 at December 31, 2012, are \$46,265. The loan payments will be made in the General Fund.

Loans payable requirements at December 31, 2012, were as follows:

<u>Year Ending December 31</u>	<u>State Loan</u>	
	<u>Principal</u>	<u>Interest</u>
2013	\$ 12,300	\$ 2,190
2014	13,033	1,427
2015	13,837	624
2016	2,830	24
Total	<u>\$ 42,000</u>	<u>\$ 4,265</u>

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities (Continued)

2. Bonded Debt

Type of Indebtedness	Final Maturity	Installment Amounts	Interest Rate (%)	Original Issue Amount	Outstanding Balance December 31, 2012
General obligation bonds and notes					
2009B G.O. Capital Improvement Plan Bonds	2019	\$178,793 - \$462,144	2.00- 3.25	\$ 2,865,000	\$ 2,375,000
2009C G.O. Jail Bonds	2030	\$66,717 - \$821,600	3.00 - 4.00	7,250,000	7,250,000
2010A G.O. Capital Improvement Plan Bonds	2022	\$74,534 - \$441,585	1.05 - 3.45	2,695,000	2,695,000
2010B G.O. Jail Bonds	2031	\$214,006 - \$1,396,950	4.00 - 4.25	5,220,000	5,220,000
Total General Obligation Bonds and Notes				<u>\$ 18,030,000</u>	<u>\$ 17,540,000</u>

3. Debt Service Requirements

Debt service requirements at December 31, 2012, were as follows:

Year Ending December 31	General Obligation Bonds	
	Principal	Interest
2013	\$ 485,000	\$ 593,200
2014	490,000	585,774
2015	585,000	576,241
2016	600,000	563,547
2017	615,000	547,761
2018 - 2022	4,325,000	2,387,785
2023 - 2027	5,375,000	1,547,044
2028 - 2031	5,065,000	429,759
Total	<u>\$ 17,540,000</u>	<u>\$ 7,231,111</u>

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

3. Detailed Notes on All Funds

C. Liabilities (Continued)

4. Changes in Long-Term Liabilities

Long-term liability activity for the year ended December 31, 2012, was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Bonds payable					
2009A G.O. Capital Notes	\$ 245,000	\$ -	\$ 245,000	\$ -	\$ -
2009B G.O. Capital Improvement Plan Bonds	2,540,000	-	165,000	2,375,000	160,000
2009C G.O. Jail Bonds	7,250,000	-	-	7,250,000	-
2010A G.O. Capital Improvement Plan Bonds	2,695,000	-	-	2,695,000	325,000
2010B G.O. Jail Bonds	5,220,000	-	-	5,220,000	-
Premium on bonds	83,154	-	8,478	74,676	-
Less: discount on bonds	(50,638)	-	(6,292)	(44,346)	-
Total bonds payable	\$ 17,982,516	\$ -	\$ 412,186	\$ 17,570,330	\$ 485,000
Loans payable	42,000	-	-	42,000	12,300
Compensated absences	954,229	29,276	-	983,505	50,787
Net OPEB obligation	179,434	104,378	39,280	244,532	-
Long-Term Liabilities	\$ 19,158,179	\$ 133,654	\$ 451,466	\$ 18,840,367	\$ 548,087

4. Employee Retirement Systems and Pension Plans

A. Plan Description

All full-time and certain part-time employees of Houston County are covered by defined benefit pension plans administered by the Public Employees Retirement Association of Minnesota (PERA). PERA administers the General Employees Retirement Fund, the Public Employees Police and Fire Fund, and the Local Government Correctional Service Retirement Fund (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.

General 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 and benefits vest after three years of credited service (five years for those first eligible for membership after June 30, 2010).

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

4. Employee Retirement Systems and Pension Plans

A. Plan Description (Continued)

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 as a correctional guard or officer, a joint jailer/dispatcher, or as a supervisor of correctional guards or officers or of joint jailer/dispatchers and are directly responsible for the direct security, custody, and control of the county correctional institution and its inmates, are covered by the Public Employees Correctional Fund. For members first eligible for membership after June 30, 2010, benefits vest on a graduated schedule starting with 50 percent after five years and increasing 10 percent for each year of service until fully vested after ten years. Members eligible for membership before July 1, 2010, are fully vested after three years of service.

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. Defined retirement benefits are based on a member's average yearly salary for the five highest-paid consecutive years of allowable service, age, and years of credit at termination of service.

Two methods are used to compute benefits for General Employees Retirement Fund 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 General Employees Retirement Fund members hired prior to July 1, 1989, 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. Normal retirement age is 55 for Public

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

4. Employee Retirement Systems and Pension Plans

A. Plan Description (Continued)

Employees Police and Fire Fund members and Public Employees Correctional Fund members, and either 65 or 66 (depending on date hired) for General Employees Retirement Fund members. 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.

PERA issues a publicly available financial report that includes financial statements and required supplementary information for the General 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.

B. Funding Policy

Pension benefits are funded from member and employer contributions and income from the investment of fund assets. Rates for employer and employee contributions are set by Minn. Stat. ch. 353. 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. General Employees Retirement Fund Basic Plan members and Coordinated Plan members were required to contribute 9.10 and 6.25 percent, respectively, of their annual covered salary. Public Employees Police and Fire Fund members are required to contribute 9.60 percent. 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 2012:

General Employees Retirement Fund	
Basic Plan members	11.78%
Coordinated Plan members	7.25
Public Employees Police and Fire Fund	14.40
Public Employees Correctional Fund	8.75

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

4. Employee Retirement Systems and Pension Plans

B. Funding Policy (Continued)

The County's contributions for the years ending December 31, 2012, 2011, and 2010, for the General Employees Retirement Fund, the Public Employees Police and Fire Fund, and the Public Employees Correctional Fund were:

	2012	2011	2010
General Employees Retirement Fund	\$ 396,368	\$ 394,134	\$ 386,739
Public Employees Police and Fire Fund	124,363	127,710	123,372
Public Employees Correctional Fund	57,780	51,882	46,190

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

C. Other Postemployment Benefits (OPEB)

Plan Description

The County provides health insurance benefits for certain retired employees under a single-employer self-insured health care plan, financed and administered by the Southeast Service Cooperative and Houston County. Blue Cross and Blue Shield of Minnesota (BCBSM), under contract with the Southeast Service Cooperative, is the Claims Administrator. The County provides benefits for retirees as required by Minn. Stat. § 471.61, subd. 2b. Active employees who retire from the County when eligible to receive a retirement benefit from PERA (or similar plan) and do not participate in any other health benefits program providing similar coverage will be eligible to continue coverage with respect to both themselves and their eligible dependent(s) under the County's health benefits program. Retirees are required to pay 100 percent of the total group rate. Since the premium is a blended rate determined on the entire active and retiree population, the retirees, whose costs are statistically higher than the group average, are receiving an implicit rate "subsidy." As of January 1, 2011, there were four retirees receiving health benefits from the County's health plan.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

4. Employee Retirement Systems and Pension Plans

C. Other Postemployment Benefits (OPEB) (Continued)

Annual OPEB Cost and Net OPEB Obligations

The County's annual OPEB cost is calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that if paid on an ongoing basis, is projected to cover normal costs each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years. The following table shows the components of the County's annual OPEB cost for 2012, the amount actually contributed to the plan, and changes in the County's net OPEB obligation:

ARC	\$ 107,284
Interest on net OPEB obligations	8,075
Adjustment to ARC	<u>(10,981)</u>
Annual OPEB Cost	\$ 104,378
Contribution during the year	<u>(39,280)</u>
Increase in net OPEB obligation	\$ 65,098
Net OPEB - Beginning of Year	<u>179,434</u>
Net OPEB - End of Year	<u>\$ 244,532</u>

The County's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for the year ended December 31, 2012, were as follows:

<u>Fiscal Year Ended</u>	<u>Annual OPEB Cost</u>	<u>Employer Contribution</u>	<u>Percentage Contributed</u>	<u>Net OPEB Obligation</u>
December 31, 2010	\$ 54,101	\$ 21,926	40.5%	\$ 98,754
December 31, 2011	105,693	25,013	23.7	179,434
December 31, 2012	104,378	39,280	37.6	244,532

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

4. Employee Retirement Systems and Pension Plans

C. Other Postemployment Benefits (OPEB) (Continued)

Funded Status

Since the County has not irrevocably deposited into a trust for future health benefits, the actuarial value of assets is \$0.

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded Actuarial Accrued Liability (UAAL) (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
January 1, 2011	-	815,921	815,921	0.0	6,937,733	11.8

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. Examples include assumptions about future employment, mortality, and health care cost trends. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

Actuarial Methods and Assumptions

Projection of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the January 1, 2011, actuarial valuation, the Projected Unit Credit Actuarial Method was used. The actuarial assumptions included a 4.5 percent discount rate (net of expenses), including an inflation assumption of 2.5 percent and an annual health care cost rate of 8.0 percent initially, reduced incrementally to an ultimate rate of six percent after six years. The initial unfunded actuarial accrued liability is being amortized as a level dollar amount over an open 30-year period beginning in 2008.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

5. Summary of Significant Contingencies and Other Items

A. 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 for which the County carries commercial insurance. The County has entered into a joint powers agreement with other Minnesota counties to form the Minnesota Counties Intergovernmental 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 \$460,000 per claim in 2012 and \$470,000 in 2013. 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.

The County has entered into a joint powers agreement with the MCIT to authorize the Board to exercise the common powers of the participating governmental units in connection with certain matters pertaining to the administration and funding of group employee benefits and other financial risk management services. The County may choose to participate in any of the services offered. The County may withdraw from the pool at any time giving a 90-day written notice. There is no contingent liability after withdrawal.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

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

B. Contingent Liabilities

The County has entered into an agreement with the Minnesota Department of Agriculture and a local lending institution to jointly administer the Agricultural Best Management Loan Program to individuals to implement projects that prevent or mitigate nonpoint source water pollution. While the County is not liable for the repayment of the loans in any manner, it does have certain responsibilities under the agreement. The County has met those responsibilities for 2012.

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

C. Jointly-Governed Organizations

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

The Southeast Minnesota Water Resources Board provides regional water quality services to several counties. During the year, the Board received \$4,000 from Houston County.

The Southeast Minnesota Emergency Management Services provides various health services to several counties.

The Workforce Development provides various job training services to several counties. During the year, Houston County paid \$123,541 to the Workforce Development.

The Southeast Minnesota Community Action Council (SEMCAC) provides various social services emergency assistance services to several counties. It also provides housing and redevelopment for Houston County through Bluff Country. During the year, Houston County paid \$84,043 to SEMCAC.

The Southeastern Minnesota Narcotics Task Force provides drug enforcement services to several counties. During the year, Houston County paid \$6,000 to the Task Force.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

5. Summary of Significant Contingencies and Other Items

C. Jointly-Governed Organizations (Continued)

The Southeastern Minnesota Library provides regional library services to counties and cities in southeastern Minnesota. During the year, Houston County paid \$126,690 to the Library.

The Minnesota Counties Computer Cooperative (MCCC) provides computer programming services to several Minnesota counties. During the year, Houston County paid \$94,684 to the MCCC.

The Southeast Minnesota Regional Radio Board provides for the regional administration of enhancements to the Statewide Public Safety Radio and Communications System (ARMER). During 2012, Houston County paid \$1,000 to the Board.

D. Joint Venture

Family Services Collaborative

The Houston County Family Services Collaborative was established in 1995 under the authority of Minn. Stat. §§ 471.59 and 124D.23. The Collaborative includes Houston County, four Houston County school districts, and SEMCAC, each of which appoints members to the Collaborative's governing board. The purpose of the Collaborative is to provide a coordinated approach to support and nurture individuals and families through prevention and intervention so as to ensure success for every child.

Control of the Collaborative is vested in a Board of Directors. Houston County appoints two members to this Board. Houston County acts as fiscal agent for the Collaborative. The Collaborative is financed by state grants and appropriations from participating members. During 2012, Houston County provided no funding. In the event of withdrawal from the Collaborative, the withdrawing party shall give a 30-day notice. The 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 property, real and personal, at the time of termination shall be distributed by the governing board.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

5. Summary of Significant Contingencies and Other Items

D. Joint Venture

Family Services Collaborative (Continued)

Currently, the Collaborative does not prepare complete financial statements; therefore, the Collaborative does not have audited financial statements. Financial information can be obtained by contacting the following:

Loretta Lillegraven
Fiscal Supervisor
Houston County Public Health Nursing Department
Caledonia, Minnesota 55921

E. Subsequent Event

Flood

In early summer of 2013, Houston County incurred a natural disaster due to flooding. The resulting repairs to infrastructure were major to the County. The County was declared a natural disaster by the federal government.

REQUIRED SUPPLEMENTARY INFORMATION

This page was left blank intentionally.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT A-1

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2012**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Revenues				
Taxes	\$ 5,308,444	\$ 5,308,444	\$ 5,312,478	\$ 4,034
Licenses and permits	41,630	41,630	56,350	14,720
Intergovernmental	2,984,638	2,984,638	3,214,630	229,992
Charges for services	2,071,921	2,083,176	1,937,926	(145,250)
Fines and forfeits	6,000	6,000	9,299	3,299
Gifts and contributions	6,000	6,000	2,550	(3,450)
Investment earnings	111,700	111,700	154,335	42,635
Miscellaneous	724,658	724,658	431,626	(293,032)
Total Revenues	\$ 11,254,991	\$ 11,266,246	\$ 11,119,194	\$ (147,052)
Expenditures				
Current				
General government				
Commissioners	\$ 286,303	\$ 286,303	\$ 246,336	\$ 39,967
Courts	60,000	60,000	77,226	(17,226)
County auditor	143,153	152,568	154,878	(2,310)
Motor vehicle/licence bureau	107,416	117,069	116,005	1,064
County treasurer	147,835	154,539	138,931	15,608
County assessor	340,157	359,957	347,651	12,306
Elections	92,277	93,777	95,494	(1,717)
Finance director	129,288	150,902	151,116	(214)
Data processing	282,748	292,988	268,084	24,904
Personnel	190,434	190,434	188,880	1,554
Attorney	382,871	382,871	382,954	(83)
Law library	15,000	15,000	-	15,000
Recorder	219,792	319,575	319,305	270
Surveyor	184,351	185,949	182,447	3,502
Planning and zoning	328,485	328,485	251,749	76,736
Buildings and plant	523,640	523,640	477,478	46,162
Veterans service officer	133,322	133,322	133,354	(32)
Other general government	920,680	920,680	271,393	649,287
Total general government	\$ 4,487,752	\$ 4,668,059	\$ 3,803,281	\$ 864,778

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

**EXHIBIT A-1
(Continued)**

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2012**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Expenditures				
Current (Continued)				
Public safety				
Sheriff	\$ 1,561,234	\$ 1,531,740	\$ 1,526,613	\$ 5,127
Boat and water safety	14,103	14,103	13,148	955
Emergency services	500	500	177,714	(177,214)
Coroner	50,440	50,440	50,440	-
E-911 system	204,135	205,238	132,055	73,183
County jail	1,175,924	1,175,924	1,290,923	(114,999)
Victim assistance	-	-	56,255	(56,255)
Community corrections	194,839	194,839	193,170	1,669
Civil defense	88,343	88,343	711	87,632
Total public safety	\$ 3,289,518	\$ 3,261,127	\$ 3,441,029	\$ (179,902)
Sanitation				
Solid waste	\$ 459,865	\$ 459,865	\$ 455,540	\$ 4,325
Recycling	339,107	339,107	334,792	4,315
Total sanitation	\$ 798,972	\$ 798,972	\$ 790,332	\$ 8,640
Health				
Nursing services	\$ 1,942,699	\$ 1,942,699	\$ 1,645,533	\$ 297,166
Transportation	-	-	12,000	(12,000)
Health center (waivered services)	-	-	2,000	(2,000)
Total health	\$ 1,942,699	\$ 1,942,699	\$ 1,659,533	\$ 283,166
Culture and recreation				
Historical society	\$ 36,700	\$ 36,700	\$ 21,800	\$ 14,900
Parks	31,159	31,159	22,704	8,455
County/regional library	-	-	126,690	(126,690)
Other culture and recreation	-	-	167,466	(167,466)
Total culture and recreation	\$ 67,859	\$ 67,859	\$ 338,660	\$ (270,801)

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

**EXHIBIT A-1
(Continued)**

**BUDGETARY COMPARISON SCHEDULE
GENERAL FUND
FOR THE YEAR ENDED DECEMBER 31, 2012**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Expenditures				
Current (Continued)				
Conservation of natural resources				
County extension	\$ 155,030	\$ 155,030	\$ 159,538	\$ (4,508)
Soil and water conservation	-	-	216,482	(216,482)
Agriculture society/County fair	18,000	18,000	17,975	25
Water planning	22,672	22,672	22,151	521
Total conservation of natural resources	\$ 195,702	\$ 195,702	\$ 416,146	\$ (220,444)
Economic development				
Community development	\$ 88,127	\$ 88,127	\$ 112,223	\$ (24,096)
Airport	995,125	995,125	348,268	646,857
Other economic development	1,310	1,310	3,880	(2,570)
Total economic development	\$ 1,084,562	\$ 1,084,562	\$ 464,371	\$ 620,191
Debt service				
Principal	\$ -	\$ -	\$ 227,210	\$ (227,210)
Interest	-	-	2,384	(2,384)
Total debt service	\$ -	\$ -	\$ 229,594	\$ (229,594)
Total Expenditures	\$ 11,867,064	\$ 12,018,980	\$ 11,142,946	\$ 876,034
Excess of Revenues Over (Under) Expenditures	\$ (612,073)	\$ (752,734)	\$ (23,752)	\$ 728,982
Other Financing Sources (Uses)				
Proceeds from sale of capital assets	-	-	4,445	4,445
Change in Fund Balance	\$ (612,073)	\$ (752,734)	\$ (19,307)	\$ 733,427
Fund Balance - January 1	4,966,106	4,966,106	4,966,106	-
Fund Balance - December 31	\$ 4,354,033	\$ 4,213,372	\$ 4,946,799	\$ 733,427

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT A-2

**BUDGETARY COMPARISON SCHEDULE
ROAD AND BRIDGE SPECIAL REVENUE FUND
FOR THE YEAR ENDED DECEMBER 31, 2012**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Revenues				
Taxes	\$ 2,262,193	\$ 2,262,193	\$ 2,406,019	\$ 143,826
Licenses and permits	1,000	1,000	3,870	2,870
Intergovernmental	7,951,230	7,951,230	8,436,077	484,847
Charges for services	169,000	169,000	317,818	148,818
Investment earnings	17,500	17,500	22,313	4,813
Miscellaneous	12,288	12,288	12,462	174
Total Revenues	\$ 10,413,211	\$ 10,413,211	\$ 11,198,559	\$ 785,348
Expenditures				
Current				
Transportation				
Administration	\$ 251,404	\$ 251,404	\$ 246,293	\$ 5,111
Maintenance	2,349,291	2,315,691	3,308,633	(992,942)
Construction	8,908,288	8,908,288	4,818,696	4,089,592
Equipment maintenance and shop	731,528	765,128	678,754	86,374
Total transportation	\$ 12,240,511	\$ 12,240,511	\$ 9,052,376	\$ 3,188,135
Intergovernmental				
Highway and streets	\$ -	\$ -	\$ 216,591	\$ (216,591)
Debt service				
Principal	\$ -	\$ -	\$ 132,790	\$ (132,790)
Interest	-	-	1,461	(1,461)
Total debt service	\$ -	\$ -	\$ 134,251	\$ (134,251)
Total Expenditures	\$ 12,240,511	\$ 12,240,511	\$ 9,403,218	\$ 2,837,293
Excess of Revenues Over (Under) Expenditures	\$ (1,827,300)	\$ (1,827,300)	\$ 1,795,341	\$ 3,622,641
Other Financing Sources (Uses)				
Proceeds from sale of capital assets	5,000	5,000	2,932	(2,068)
Change in Fund Balance	\$ (1,822,300)	\$ (1,822,300)	\$ 1,798,273	\$ 3,620,573
Fund Balance - January 1	5,468,265	5,468,265	5,468,265	-
Increase (decrease) in inventories	-	-	15,535	15,535
Fund Balance - December 31	\$ 3,645,965	\$ 3,645,965	\$ 7,282,073	\$ 3,636,108

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT A-3

**BUDGETARY COMPARISON SCHEDULE
SOCIAL SERVICES SPECIAL REVENUE FUND
FOR THE YEAR ENDED DECEMBER 31, 2012**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Revenues				
Taxes	\$ 1,088,469	\$ 1,088,469	\$ 1,073,375	\$ (15,094)
Intergovernmental	2,732,780	2,732,780	2,784,688	51,908
Charges for services	159,080	159,080	138,429	(20,651)
Investment earnings	10,000	10,000	8,615	(1,385)
Miscellaneous	274,373	274,373	1,915	(272,458)
Total Revenues	\$ 4,264,702	\$ 4,264,702	\$ 4,007,022	\$ (257,680)
Expenditures				
Current				
Human services				
Income maintenance	\$ 1,314,862	\$ 1,314,862	\$ 1,208,492	\$ 106,370
Social services	2,949,840	2,949,840	2,694,930	254,910
Total Expenditures	\$ 4,264,702	\$ 4,264,702	\$ 3,903,422	\$ 361,280
Change in Fund Balance	\$ -	\$ -	\$ 103,600	\$ 103,600
Fund Balance - January 1	1,356,044	1,356,044	1,356,044	-
Fund Balance - December 31	\$ 1,356,044	\$ 1,356,044	\$ 1,459,644	\$ 103,600

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT A-4

**SCHEDULE OF FUNDING PROGRESS - OTHER POSTEMPLOYMENT BENEFITS
DECEMBER 31, 2012**

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
January 1, 2008	\$ -	\$ 503,862	\$ 503,862	0.0%	\$ 6,203,278	8.1%
January 1, 2011	-	815,921	815,921	0.0	6,937,733	11.8

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION
FOR THE YEAR ENDED DECEMBER 31, 2012

1. Budgetary Information

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

On or before mid-June of each year, all departments and agencies submit requests for appropriations to the County Finance Director so that a budget can be prepared. Before October 31, the proposed budget is presented to the Houston County Board of Commissioners 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. The County's department head may make transfers of appropriations within a department. Transfers of appropriations 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. During the year, the Board made no supplemental budgetary appropriations.

3. Other Postemployment Benefits

Houston County implemented Governmental Accounting Standards Board Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, in 2008. Future reports will provide additional trend analysis to meet the three-actuarial-valuation data requirement as it becomes available. See Note 4.C. in the notes to the financial statements for additional information regarding the County's other postemployment benefits.

This page was left blank intentionally.

SUPPLEMENTARY INFORMATION

This page was left blank intentionally.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

NONMAJOR GOVERNMENTAL FUNDS

The Debt Service Fund is used to account for all financial resources restricted for payment of principal, interest, and related costs of long-term bonded debt.

The Capital Projects Fund is used to account for all financial resources committed for the construction of the Criminal Justice Center.

This page was left blank intentionally.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT B-1

**COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS
DECEMBER 31, 2012**

	<u>Debt Service Fund</u>	<u>Capital Projects Fund</u>	<u>Total Nonmajor Governmental Funds (Exhibit 3)</u>
<u>Assets</u>			
Cash and pooled investments	\$ 788,752	\$ 43,840	\$ 832,592
Taxes receivable			
Prior	20,196	-	20,196
Accrued interest receivable	-	6	6
Due from other funds	450,198	-	450,198
	<u> </u>	<u> </u>	<u> </u>
Total Assets	<u>\$ 1,259,146</u>	<u>\$ 43,846</u>	<u>\$ 1,302,992</u>
 <u>Liabilities and Fund Balances</u>			
Liabilities			
Contracts payable	\$ -	\$ 48,562	\$ 48,562
Due to other funds	431,181	-	431,181
Deferred revenue - unavailable	10,399	-	10,399
	<u> </u>	<u> </u>	<u> </u>
Total Liabilities	<u>\$ 441,580</u>	<u>\$ 48,562</u>	<u>\$ 490,142</u>
 Fund Balances			
Restricted for			
Debt service	\$ 817,566	\$ -	\$ 817,566
Unassigned	-	(4,716)	(4,716)
	<u> </u>	<u> </u>	<u> </u>
Total Fund Balances	<u>\$ 817,566</u>	<u>\$ (4,716)</u>	<u>\$ 812,850</u>
	<u> </u>	<u> </u>	<u> </u>
Total Liabilities and Fund Balances	<u>\$ 1,259,146</u>	<u>\$ 43,846</u>	<u>\$ 1,302,992</u>

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT B-2

**COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE
NONMAJOR GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2012**

	<u>Debt Service Fund</u>	<u>Capital Projects Fund</u>	<u>Total Nonmajor Governmental Funds (Exhibit 5)</u>
Revenues			
Taxes	\$ 989,120	\$ -	\$ 989,120
Intergovernmental	38,431	31,332	69,763
Investment earnings	-	207	207
	<u> </u>	<u> </u>	<u> </u>
Total Revenues	<u>\$ 1,027,551</u>	<u>\$ 31,539</u>	<u>\$ 1,059,090</u>
Expenditures			
Current			
Public safety	\$ -	\$ 32,196	\$ 32,196
Capital outlay			
Public safety	-	4,143	4,143
Debt service			
Principal	50,000	-	50,000
Interest	597,006	-	597,006
Administrative - fiscal charges	7,425	-	7,425
	<u> </u>	<u> </u>	<u> </u>
Total Expenditures	<u>\$ 654,431</u>	<u>\$ 36,339</u>	<u>\$ 690,770</u>
Net Change in Fund Balance	<u>\$ 373,120</u>	<u>\$ (4,800)</u>	<u>\$ 368,320</u>
Fund Balance - January 1	<u>444,446</u>	<u>84</u>	<u>444,530</u>
Fund Balance - December 31	<u><u>\$ 817,566</u></u>	<u><u>\$ (4,716)</u></u>	<u><u>\$ 812,850</u></u>

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT B-3

**BUDGETARY COMPARISON SCHEDULE
DEBT SERVICE FUND
FOR THE YEAR ENDED DECEMBER 31, 2012**

	<u>Budgeted Amounts</u>		<u>Actual Amounts</u>	<u>Variance with Final Budget</u>
	<u>Original</u>	<u>Final</u>		
Revenues				
Taxes	\$ 1,099,290	\$ 1,099,290	\$ 989,120	\$ (110,170)
Intergovernmental	36,292	36,292	38,431	2,139
Total Revenues	\$ 1,135,582	\$ 1,135,582	\$ 1,027,551	\$ (108,031)
Expenditures				
Debt service				
Principal	\$ 509,250	\$ 509,250	\$ 50,000	\$ 459,250
Interest	626,332	626,332	597,006	29,326
Administrative (fiscal) charges	-	-	7,425	(7,425)
Total Expenditures	\$ 1,135,582	\$ 1,135,582	\$ 654,431	\$ 481,151
Change in Fund Balance	\$ -	\$ -	\$ 373,120	\$ 373,120
Fund Balance - January 1	444,446	444,446	444,446	-
Fund Balance - December 31	\$ 444,446	\$ 444,446	\$ 817,566	\$ 373,120

This page was left blank intentionally.

FIDUCIARY FUNDS

This page was left blank intentionally.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

AGENCY FUNDS

Agency funds are used to account for assets held by a governmental unit as an agent for individuals, private organizations, other governmental units, and other funds.

The Crooked Creek Watershed Fund accounts for reimbursements to the Watershed District for operations and the collection of assessments to pay the Watershed District's bonded debt and interest.

The Health Fund is used to account for employees' pre-tax health benefits.

The Revolving Fund accounts for the transfer of County collections to the state (mortgage registry tax, game and fish license sales, motor vehicle license sales, state deed tax sales, and state revenue taxes) and the apportionment of state-aid payments for police and fire departments to cities and towns.

The Soil and Water Conservation Fund accounts for the assets of the Root River Soil and Water Conservation District held by the County.

The School Districts Fund accounts for property taxes collected and remitted by the County to the various school districts in the County.

The Family Collaborative Fund accounts for monies received and expended by the Family Services Collaborative.

The Taxes and Penalties Fund accounts for the collection and distribution of property taxes (current and delinquent).

The Towns and Cities Fund accounts for the taxes and other amounts received by the County for the various towns and cities.

The Historical Bluff Country Fund accounts for the monies received and expended by Historical Bluff Country.

The Victim Services Fund accounts for the funds of Victim Services, a nonprofit agency for which the County is the fiscal agent.

The Region 1 Fund accounts for the funds of Southeast Minnesota Region 1, a joint power board for which the County is the fiscal agent.

This page was left blank intentionally.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT C-1

**COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES
ALL AGENCY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2012**

	Balance January 1	Additions	Deductions	Balance December 31
<u>CROOKED CREEK WATERSHED</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 463	\$ 24,479	\$ 24,405	\$ 537
<u>Liabilities</u>				
Due to other governments	\$ 463	\$ 24,479	\$ 24,405	\$ 537
 <u>HEALTH</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 24,955	\$ 116,046	\$ 112,722	\$ 28,279
<u>Liabilities</u>				
Accounts payable	\$ 24,955	\$ 116,046	\$ 112,722	\$ 28,279
 <u>REVOLVING</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 22,901	\$ 3,709,011	\$ 3,655,709	\$ 76,203
<u>Liabilities</u>				
Due to other governments	\$ 22,901	\$ 3,709,011	\$ 3,655,709	\$ 76,203

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

*EXHIBIT C-1
(Continued)*

**COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES
ALL AGENCY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2012**

	Balance January 1	Additions	Deductions	Balance December 31
<u>SOIL AND WATER CONSERVATION</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 720,944	\$ 363,234	\$ 651,590	\$ 432,588
<u>Liabilities</u>				
Due to other governments	\$ 720,944	\$ 363,234	\$ 651,590	\$ 432,588
 <u>SCHOOL DISTRICTS</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 149,261	\$ 6,042,741	\$ 6,022,476	\$ 169,526
<u>Liabilities</u>				
Due to other governments	\$ 149,261	\$ 6,042,741	\$ 6,022,476	\$ 169,526
 <u>FAMILY COLLABORATIVE</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 201,797	\$ 116,047	\$ 78,557	\$ 239,287
<u>Liabilities</u>				
Due to other governments	\$ 201,797	\$ 116,047	\$ 78,557	\$ 239,287

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

*EXHIBIT C-1
(Continued)*

**COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES
ALL AGENCY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2012**

	Balance January 1	Additions	Deductions	Balance December 31
<u>TAXES AND PENALTIES</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 110,575	\$ 25,724,784	\$ 25,727,188	\$ 108,171
<u>Liabilities</u>				
Accounts payable	\$ 108,587	\$ 140,610	\$ 141,026	\$ 108,171
Due to other funds	-	11,341,575	11,341,575	-
Due to other governments	1,988	14,242,599	14,244,587	-
Total Liabilities	\$ 110,575	\$ 25,724,784	\$ 25,727,188	\$ 108,171
 <u>TOWNS AND CITIES</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 129,015	\$ 7,407,057	\$ 7,335,429	\$ 200,643
<u>Liabilities</u>				
Due to other governments	\$ 129,015	\$ 7,407,057	\$ 7,335,429	\$ 200,643
 <u>HISTORICAL BLUFF COUNTRY</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 162	\$ -	\$ 162	\$ -
<u>Liabilities</u>				
Accounts payable	\$ 162	\$ -	\$ 162	\$ -

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

*EXHIBIT C-1
(Continued)*

**COMBINING STATEMENT OF CHANGES IN ASSETS AND LIABILITIES
ALL AGENCY FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2012**

	Balance January 1	Additions	Deductions	Balance December 31
<u>VICTIM SERVICES</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 6,128	\$ 59,843	\$ 42,993	\$ 22,978
<u>Liabilities</u>				
Due to other governments	\$ 6,128	\$ 59,843	\$ 42,993	\$ 22,978
 <u>REGION 1</u>				
<u>Assets</u>				
Cash and pooled investments	\$ -	\$ 188,056	\$ 184,499	\$ 3,557
Due from other governments	49,408	-	49,408	-
Total Assets	\$ 49,408	\$ 188,056	\$ 233,907	\$ 3,557
<u>Liabilities</u>				
Accounts payable	\$ -	\$ 56,009	\$ 52,452	\$ 3,557
Due to other funds	49,408	-	49,408	-
Due to other governments	-	132,047	132,047	-
Total Liabilities	\$ 49,408	\$ 188,056	\$ 233,907	\$ 3,557
 <u>TOTAL ALL AGENCY FUNDS</u>				
<u>Assets</u>				
Cash and pooled investments	\$ 1,366,201	\$ 43,751,298	\$ 43,835,730	\$ 1,281,769
Due from other governments	49,408	-	49,408	-
	\$ 1,415,609	\$ 43,751,298	\$ 43,885,138	\$ 1,281,769
<u>Liabilities</u>				
Accounts payable	\$ 133,704	\$ 312,665	\$ 306,362	\$ 140,007
Due to other funds	49,408	11,341,575	11,390,983	-
Due to other governments	1,232,497	32,097,058	32,187,793	1,141,762
Total Liabilities	\$ 1,415,609	\$ 43,751,298	\$ 43,885,138	\$ 1,281,769

OTHER SCHEDULES

This page was left blank intentionally.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT D-1

**SCHEDULE OF INTERGOVERNMENTAL REVENUE
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2012**

Shared Revenue

State

Highway users tax	\$	4,040,909
PERA rate reimbursement		23,876
Disparity reduction aid		135,769
Police aid		81,446
County program aid		906,225
Market value credit		179,877
Enhanced 911		92,829
		92,829

Total shared revenue **\$ 5,460,931**

Reimbursement for Services

State

Minnesota Department of Human Services	\$	536,556
		536,556

Payments

Local

Local contributions	\$	12,250
Payments in lieu of taxes		357,271
		357,271

Total Payments **\$ 369,521**

Grants

State

Minnesota Department/Board of		
Public Safety	\$	456,084
Health		86,163
Employment and Economic Development		176,906
Natural Resources		116,115
Human Services		1,083,697
Veterans Affairs		5,098
Corrections		31,834
Transportation		3,452,584
Water and Soil Resources		271,195
Pollution Control Agency		55,950
Peace Officer Standards and Training Board		3,985
		3,985

Total state **\$ 5,739,611**

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

***EXHIBIT D-1
(Continued)***

**SCHEDULE OF INTERGOVERNMENTAL REVENUE
GOVERNMENTAL FUNDS
FOR THE YEAR ENDED DECEMBER 31, 2012**

Grants (Continued)

Federal

Department of	
Agriculture	\$ 182,590
Commerce	51,009
Transportation	852,568
Health and Human Services	1,124,242
Homeland Security	115,888
Environmental Protection Agency	72,242

Total federal **\$ 2,398,539**

Total state and federal grants **\$ 8,138,150**

Total Intergovernmental Revenue **\$ 14,505,158**

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

EXHIBIT D-2

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2012**

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	\$ 101,745
Passed Through Minnesota Department of Human Services State Administrative Matching Grants for Supplemental Nutrition Assistance Program	10.561	<u>86,872</u>
Total U.S. Department of Agriculture		<u>\$ 188,617</u>
U.S. Department of Commerce		
Passed Through Southeastern Minnesota Regional Radio Board Public Safety Interoperable Communications Grant Program	11.555	<u>\$ 51,009</u>
U.S. Department of Transportation		
Passed Through Minnesota Department of Transportation Airport Improvement Program	20.106	\$ 185,861
Highway Planning and Construction Cluster Highway Planning and Construction	20.205	614,606
Passed Through Minnesota Department of Natural Resources Highway Planning and Construction Cluster Recreational Trails Program	20.219	50,000
Passed Through Minnesota Department of Public Safety Highway Safety Cluster State and Community Highway Safety	20.600	3,506
Alcohol Impaired Driving Countermeasures Incentive Grants I	20.601	<u>10,520</u>
Total U.S. Department of Transportation		<u>\$ 864,493</u>
U.S. Environmental Protection Agency		
Passed Through Southeast Minnesota Water Resource Board Nonpoint Source Implementation Grants	66.460	<u>\$ 72,242</u>

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

**EXHIBIT D-2
(Continued)**

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2012**

Federal Grantor Pass-Through Agency Grant Program Title	Federal CFDA Number	Expenditures
U.S. Department of Health and Human Services		
Passed Through the National Association of County and City Health Officials Medical Reserve Corps Small Grant Program	93.008	\$ 5,000
Passed Through Minnesota Department of Health		
Public Health Emergency Preparedness	93.069	7,937
Universal Newborn Hearing Screening	93.251	375
Immunization Cooperative Agreements	93.268	2,100
Centers for Disease Control and Prevention - Investigations and Technical Assistance	93.283	2,210
Temporary Assistance for Needy Families Cluster		
Temporary Assistance for Needy Families	93.558	39,815
(Total Temporary Assistance for Needy Families 93.558 \$177,802)		
Maternal and Child Health Services Block Grant to the States	93.994	23,092
Passed Through Minnesota Department of Human Services		
Promoting Safe and Stable Families	93.556	6,761
Temporary Assistance for Needy Families Cluster		
Temporary Assistance for Needy Families	93.558	137,987
(Total Temporary Assistance for Needy Families 93.558 \$177,802)		
ARRA - Emergency Contingency Fund for Temporary Assistance for Needy Families		
TANF State Programs	93.714	18,566
Child Support Enforcement	93.563	260,291
Refugee and Entrant Assistance - State-Administered Programs	93.566	205
Child Care and Development Block Grant	93.575	7,380
Stephanie Tubbs Jones Child Welfare Services Program	93.645	1,040
Foster Care - Title IV-E	93.658	111,911
Social Services Block Grant	93.667	110,486
Chafee Foster Care Independence Program	93.674	2,226
Children's Health Insurance Program	93.767	29
Medical Assistance Program	93.778	412,600
Total U.S. Department of Health and Human Services		\$ 1,150,011

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

**EXHIBIT D-2
(Continued)**

**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2012**

Federal Grantor Pass-Through Agency Grant Program Title	Federal CFDA Number	Expenditures
U.S. Department of Homeland Security		
Passed Through Minnesota Department of Natural Resources Boating Safety Financial Assistance	97.012	\$ 5,000
Passed Through Minnesota Department of Public Safety Hazard Mitigation Grant	97.039	20,855
Emergency Management Performance Grants	97.042	13,000
Passed Through Southeastern Minnesota Regional Radio Board Interoperable Emergency Communications	97.055	1,094
Homeland Security Grant Program (Total Homeland Security Grant Program 93.067 \$62,894)	97.067	555
Passed Through Southeastern Minnesota Region One Homeland Security and Emergency Management Board Homeland Security Grant Program (Total Homeland Security Grant Program 93.067 \$62,894)	97.067	<u>62,339</u>
Total U.S. Department of Homeland Security		\$ <u>102,843</u>
Total Federal Awards		\$ <u><u>2,429,215</u></u>

This page was left blank intentionally.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

**NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED DECEMBER 31, 2012**

1. Reporting Entity

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

2. Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of Houston County under programs of the federal government for the year ended December 31, 2012. The information in this schedule is presented in accordance with the requirements of Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Because the schedule presents only a selected portion of the operations of Houston County, it is not intended to and does not present the financial position or changes in net position of Houston County.

3. Summary of Significant Accounting Policies

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

4. Clusters

Clusters of programs are groupings of closely related programs that share common compliance requirements. Total expenditures by cluster are:

Highway Planning and Construction Cluster	\$	664,606
Highway Safety Cluster		14,026
Temporary Assistance for Needy Families Cluster		196,368

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

5. Reconciliation to Schedule of Intergovernmental Revenue

Federal grant revenue per Schedule of Intergovernmental Revenue	\$ 2,398,539
Deferred in 2010, recognized as revenue in 2011	
Highway Planning and Construction	(10,073)
Disaster Grants - Public Assistance (Presidentially Declared Disasters)	(284,326)
Temporary Assistance for Needy Families (TANF)	(606)
Medical Assistance Program	(7,966)
Grants received more than 60 days after year-end, deferred in 2011	
State Administrative Matching Grants for Supplemental Nutrition Assistance Program	6,027
Airport Improvement Program	21,998
Disaster Grants - Public Assistance (Presidentially Declared Disasters)	271,281
Child Care and Development Block Grant	666
Foster Care - Title IV-E	7,517
Medical Assistance Program	26,158
	<hr/>
Expenditures per Schedule of Expenditures of Federal Awards	<u>\$ 2,429,215</u>

6. Subrecipients

During 2012, the County passed \$50,000 (CFDA #20.219) to the Houston Money Creek Snowriders Snowmobile Club

7. American Recovery and Reinvestment Act

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

This page was left blank intentionally.

**HOUSTON COUNTY
CALEDONIA, MINNESOTA**

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED DECEMBER 31, 2012**

I. SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued: **Unmodified**

Internal control over financial reporting:

- Material weaknesses identified? **Yes**
- Significant deficiencies identified? **Yes**

Noncompliance material to the financial statements noted? **No**

Federal Awards

Internal control over major programs:

- Material weaknesses identified? **No**
- Significant deficiencies identified? **No**

Type of auditor's report issued on compliance for major programs: **Unmodified**

Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133? **No**

The major programs are:

Highway Planning and Construction Cluster	
Highway Planning and Construction	CFDA #20.205
Recreational Trails Program	CFDA #20.219
Temporary Assistance for Needy Families Cluster	
Temporary Assistance for Needy Families	CFDA #93.558
Emergency Contingency Fund for Temporary Assistance for Needy Families (TANF) State Programs	CFDA #93.714
Medical Assistance Program	CFDA #93.778

The threshold for distinguishing between Types A and B programs was \$300,000.

Houston County qualified as a low-risk auditee? **No**

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

INTERNAL CONTROL

PREVIOUSLY REPORTED ITEMS NOT RESOLVED

06-1 Audit Adjustments

Criteria: A deficiency in internal control over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements of the financial statements on a timely basis. Auditing standards define a material weakness as a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the County's financial statements will not be prevented, or detected and corrected, in a timely basis.

Condition: During our audit, we identified a material adjustment that resulted in significant changes to the County's financial statements. The County provides trial balances which convert the cash basis general ledger to the modified accrual basis necessary for preparing fund level and government-wide financial statements.

Context: The inability to detect significant misstatements in the financial statements increases the likelihood the financial statements would not be fairly presented.

Effect: Audit adjustments were necessary to record additional receivables of \$589,609 and additional payables of \$619,934 in the General Fund and reclassify revenues in the Social Services Special Revenue Fund of \$396,360. Adjustments were also made to the entity wide financial statements to eliminate the interfund items of \$1,718,705, adjust long-term compensated absences of \$954,229, recognize revenues that were recorded as unavailable deferred revenue in the fund level statements of \$6,208,793, and reclassify net position.

Cause: Houston County staff indicated the additional items found by auditors were missed.

Recommendation: We recommend that County staff review internal control procedures over trial balance and financial statement preparation to ensure the County's financial statements are reported in accordance with generally accepted accounting principles.

Client's Response:

Appropriate County personnel have reviewed trial balance and financial statement preparation procedures and will provide adequate preparation and review to ensure accurate financial reporting in a timely manner.

08-2 Segregation of Duties- County Departments

Criteria: A good system of internal control provides for an adequate segregation of duties so that no one individual handles a transaction from its inception to completion.

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

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

Effect: Inadequate segregation of duties could adversely affect the County's ability to detect misstatements in amounts that would be material in relation to the financial statements in a timely period by employees in the normal course of performing their assigned functions.

Cause: Due to available resources, the County would not be able to hire additional qualified accounting staff to segregate duties in every department.

Recommendation: We recommend that the County's elected officials and management be aware of the lack of segregation of duties of the accounting functions and, where possible, implement oversight procedures to ensure that the internal control policies and procedures are being implemented by staff to the extent possible.

Client's Response:

The County's elected officials and management will remain cognizant of the issue of segregating duties due to limited number of personnel and will review and implement policies and procedures as necessary to monitor financial data.

10-1 Information Technology Security Function

Criteria: A good system of internal control provides for an adequate segregation of functions and responsibilities so that no one person has incompatible duties that would permit the perpetration and concealment of material errors or irregularities.

Condition: We noted in our review of user access to the accounting system the current Finance Director performs the information technology security function for the County.

Context: The information technology security function is incompatible with the functions of the current Finance Director because it provides the Director unlimited access to the County's information system to make changes to the accounting records that may or may not be authorized by management or other users.

Effect: The function of information technology security should be segregated from the accounting function to ensure the integrity of the data stored in the County's information system.

Cause: The current Finance Director was the former Information Technology Systems Manager, and the information security duties were not reassigned when the person became the Finance Director.

Recommendation: We recommend that the County segregate the information technology security function from the Finance Director's responsibilities. We further recommend that the information security function be assigned to the Information Technology Department.

Client's Response:

The security function of the accounting system will be performed by the IT Director

ITEMS ARISING THIS YEAR

12-1 Segregation of Duties/Vendor Setup

Criteria: A good system of internal control includes written procedures to monitor new vendors entered into the accounting system. Procedures should include someone independent of the disbursement process reviewing, verifying, and approving new vendors on a timely basis.

Condition: During our review of the disbursements process we noted personnel processing disbursements also are adding and changing vendors. Procedures were established to have personnel independent of the disbursement process reviewing a listing of new or changes to vendors quarterly. Review of this process disclosed the reviews for 2012 were not completed until December 2012.

Context: Segregation of duties between disbursements and vendor setup is limited due to the number of office personnel within the County.

Effect: The risk that errors or irregularities will not be detected in a timely manner increases when internal control procedures that have been established are not followed.

Cause: The vendor listing for the year was not reviewed until the auditors asked for it. The County forgot to review the listing due to involvement with the 2012 election.

Recommendation: We recommend the County re-evaluate the current procedures established for review of new or changes to vendors to determine if there should be any changes in the procedures currently performed. If current procedures are determined to be adequate, the procedures should be performed in a timely manner.

Client's Response:

The County Auditor will perform the vendor review on a quarterly basis and will file the documentation with the Finance Office.

12-2 Timeliness of Preparation of Financial Statements

Criteria: Management is responsible for preparing the County's financial statements in accordance with generally accepted accounting principles (GAAP) and U.S. Office of Management and Budget (OMB) Circular A-133. The financial statement preparation in accordance with GAAP and OMB Circular A-133 requires internal control over both: (1) recording, processing, and summarizing accounting data (that is, 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.

Condition: The information included in the County's financial statements submitted to the auditors required numerous revisions affecting both the financial statements and related notes.

Context: Preparation of information included in the County's financial statements is performed by the County Auditor's Office. In order to meet the County's September 30 single audit deadline, that information needs to be provided to the auditors in a timely fashion.

Effect: Additional audit hours resulted from delays in completing the County's financial statements within a reasonable amount of time. Also, errors were discovered which resulted in adjustments to the financial statements.

Cause: Tasks and information necessary for the County's financial statements were not completed in the time, form, and manner required by the County's audit due to staffing limitations and time constraints.

Recommendation: The County Board of Commissioners and management should take responsibility for the financial statements by reviewing internal controls currently in place over the preparation of the financial statements. Procedures should be implemented to ensure that the necessary financial information be prepared in a manner that allows the auditors an adequate amount of time to complete the audit by the County's required deadline.

Client's Response:

Appropriate County personnel have reviewed trial balance and financial statement preparation procedures and will provide adequate preparation and review to ensure accurate financial reporting in a timely manner.

PREVIOUSLY REPORTED ITEM RESOLVED

Information Technology Policies and Procedures (09-3)

The County did not have documented policies and procedures in place to address the following for its information technology systems: information security, operations development, termination of employees, risk assessments of the systems, and email encryption methods.

Resolution

The County has documented policies and procedures to address the majority of its technology systems.

III. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARD PROGRAMS

None.

IV. OTHER FINDINGS AND RECOMMENDATIONS

A. MANAGEMENT PRACTICES

PREVIOUSLY REPORTED ITEM NOT RESOLVED

01-2 Disaster Recovery Plan

Criteria: The County needs to provide for the continuance of several important applications processed by its computer system, including the preparation of payroll, the calculation of tax assessments and settlements, and the recording of receipts and disbursements. A disaster recovery plan should include, but not be limited to, the following:

- a list of key personnel, including the actual recovery team, who should be available during the recovery process;
- a description of the responsibilities of each member of the recovery team and of all other County employees;
- a plan as to how the County will continue operations until normal operations are re-established; this should include the use of alternative computer facilities and/or the use of manual procedures, a list of master operating schedules, and critical job schedules;
- a list of materials the County needs to continue operations and how they will be obtained;
- hardware configurations and minimum equipment requirements;
- information relative to offsite backup storage facilities;
- a list of vendor contracts;
- identification of the space to be used; and
- a schedule for developing and periodically reviewing and updating the plan.

Condition: While reviewing the Information Technology Department, we noted Houston County has an informal disaster recovery agreement with another county but does not have a formal disaster recovery plan.

Context: A disaster recovery plan would give greater assurance that the County is prepared for a disaster or major computer breakdown.

Effect: In the event that a disaster occurred, the County could experience a delay in reporting of financial services to the public.

Cause: The County is aware of the issue but has not had time to address the completion of a plan.

Recommendation: We recommend the County continue to develop, implement, and test the disaster recovery plan. All County employees should be familiar with the plan.

Client Response:

The County will continue to work on the development and implementation of a formal disaster recovery plan.



REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

SUITE 500
525 PARK STREET
SAINT PAUL, MN 55103-2139

(651) 296-2551 (Voice)
(651) 296-4755 (Fax)
state.auditor@state.mn.us (E-mail)
1-800-627-3529 (Relay Service)

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*

Independent Auditor's Report

Board of County Commissioners
Houston County

We have audited, 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, the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Houston County, Minnesota, as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the County's basic financial statements, and have issued our report thereon dated September 27, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Houston County's internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the County's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the County's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies and, therefore, material weaknesses may exist that were not identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified a deficiency in internal control over financial reporting that we consider to be a material weakness and significant deficiencies.

A deficiency in internal control over financial reporting exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the County's financial statements will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs, as item 06-1 to be a material weakness.

A significant deficiency is a deficiency, or combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs, as items 08-2, 10-1, 12-1, and 12-2 to be significant deficiencies.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Houston County's financial statements are free from 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

The *Minnesota Legal Compliance Audit Guide for Political Subdivisions*, promulgated by the State Auditor pursuant to Minn. Stat. § 6.65, contains seven categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, miscellaneous provisions, and tax increment financing. Our audit considered all of the listed categories, except that we did not test for compliance with the provisions for tax increment financing because the County has no tax increment financing.

In connection with our audit, nothing came to our attention that caused us to believe that Houston County failed to comply with the provisions of the *Minnesota Legal Compliance Audit Guide for Political Subdivisions*. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the County's noncompliance with the above referenced provisions.

Other Matters

Also included in the Schedule of Findings and Questioned Costs is a management practice comment. We believe this recommendation to be of benefit to the County, and we are reporting it for that purpose.

Houston County's responses to the internal control and management practice findings identified in our audit have been included in the Schedule of Findings and Questioned Costs. The County's responses were not subject to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on them.

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control over financial reporting, compliance and the provisions of the *Minnesota Legal Compliance Audit Guide for Political Subdivisions* and the results of that testing, and not to provide an opinion on the effectiveness of the County's internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the County's internal control over financial reporting and compliance. Accordingly, this communication is not suitable for any other purpose.

/s/Rebecca Otto

REBECCA OTTO
STATE AUDITOR

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

September 27, 2013

This page was left blank intentionally.



REBECCA OTTO
STATE AUDITOR

STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

SUITE 500
525 PARK STREET
SAINT PAUL, MN 55103-2139

(651) 296-2551 (Voice)
(651) 296-4755 (Fax)
state.auditor@state.mn.us (E-mail)
1-800-627-3529 (Relay Service)

REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE

Independent Auditor's Report

Board of County Commissioners
Houston County

Report on Compliance for Each Major Federal Program

We have audited Houston County's compliance with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the County's major federal programs for the year ended December 31, 2012. Houston County's major federal programs are identified in the Summary of Auditor's Results section of the accompanying Schedule of Findings and Questioned Costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of Houston County's major federal programs based on our audit of the types of compliance requirements referred to above. 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 Houston 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 on compliance for each major federal program. However, our audit does not provide a legal determination of the County's compliance with those requirements.

Opinion on Each Major Federal Program

In our opinion, Houston County complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2012.

Report on Internal Control Over Compliance

Management of Houston County is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the County's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing our opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the County's internal control over compliance.

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

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

Purpose of This Report

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

/s/Rebecca Otto

REBECCA OTTO
STATE AUDITOR

September 27, 2013

/s/Greg Hierlinger

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR