

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA

FINANCIAL STATEMENTS

DECEMBER 31, 2012

## CONTENTS

	<u>PAGE</u>
Official Directory	
Independent Auditors' Report	1 - 3
Management Discussion and Analysis	4 - 9
Basic Financial Statements	
Statement of Net Assets – Modified Cash Basis	10
Statement of Activities – Modified Cash Basis	11
Balance Sheet – Modified Cash Basis – Governmental Funds	12
Statement of Revenues, Expenditures and Changes in Fund Balance – Modified Cash Basis – Governmental Funds	13
Reconciliation of Changes in Fund Balance of Governmental Funds to the Statement of Activities	14
Budgetary Comparison – Modified Cash Basis	15
Notes to Basic Financial Statements	16 - 26
Supplementary Information	
Schedule of Changes in Fund Balances – Modified Cash Basis	27 - 29
Schedule of Direct Expenditures by Classification – Modified Cash Basis – Governmental Funds	30
Auditors' Report on Legal Compliance	31
Report on Compliance and 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>	32 – 33
Schedule of Findings and Responses	34

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
DECEMBER 31, 2012

BOARD OF MANAGERS

2012

<u>Name</u>	<u>Office</u>
Dale M. Nelson	President
Gene Tiedemann	Vice President
Lee Coe	Treasurer
Orville Knott	Secretary
Les Torgerson	Manager
LeRoy Ose	Manager
Albert Mandt	Manager

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*Certified Public Accountants*

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INDEPENDENT AUDITORS' REPORT

Board of Directors  
Red Lake Watershed District  
Thief River Falls, Minnesota

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities and each major fund of the Red Lake Watershed District, as of and for the year ended December 31, 2012, and the related notes to the financial statements, which collectively comprise the District's basic financial statements-modified cash basis 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 the modified cash basis of accounting described in Note 1; this includes determining that the modified cash basis of accounting is an acceptable basis for the preparation of the financial statements in the circumstances. Management is also responsible for 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 from 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 entity'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 entity'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 and each major fund of the Red Lake Watershed District, as of December 31, 2012, and the respective changes in financial position and budgetary comparison information thereof for the year then ended in accordance with the basis of accounting described in Note 1.

### Basis of Accounting

We draw attention to Note 1 of the financial statements, which describes the basis of accounting. The financial statements are prepared on the modified cash basis of accounting, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to that matter.

### Other Matters

#### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 4 - 9 be presented to supplement the basic financial statements. Such information, although not a 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.

#### *Other Information*

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Red Lake Watershed District's basic financial statements. The schedule of changes in fund balances – modified cash basis and schedule of direct expenditures by classification – modified cash basis are presented for purposes of additional analysis and are not a required part of the basic financial statements. The supplementary information on pages 27 – 30 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 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 supplementary information listed above 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 March 7, 2013 on our consideration of the Red Lake Watershed District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering District's internal control over financial reporting and compliance.

DREES, RISKEY & VALLAGER. LTD.

Certified Public Accountants

March 7, 2013  
Crookston, Minnesota

## MANAGEMENT DISCUSSION AND ANALYSIS

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

As management of the Red Lake Watershed District, we offer readers of the Red Lake Watershed District's financial statements this narrative overview and analysis of the financial activities of the District for the fiscal year ended December 31, 2012. We encourage readers to consider the information presented here in conjunction with the District's basic financial statements following this section.

### **Financial Highlights**

- The assets of Red Lake Watershed District exceeded its liabilities at the close of the recent fiscal year by \$13,903,423 (Net assets). Of this amount, \$2,072,501 (unrestricted net assets) may be used to meet the government's ongoing designations and fiscal policies.
- The District's total net assets increased by \$1,583,562.
- As of the close of the current fiscal year, Red Lake Watershed District's governmental funds reported combined ending fund balance was \$2,072,501. This total amount is designated or reserved through legal restrictions and board member authorization.
- At the end of the current fiscal year the general fund balance of \$328,201 of which all was unassigned.

### **Overview of the Financial Statements**

The discussion and analysis are intended to serve as an introduction to the Red Lake Watershed District's basic financial statements. The District's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

**Basis of Accounting.** The District has elected to present its financial statements on a modified cash basis of accounting. The modified cash basis of accounting is a basis of accounting other than generally accepted accounting principles. Basis of accounting is a reference to when financial events are recorded, such as the timing for recognizing revenues, expenses, and their related assets and liabilities. Under the District's modified cash basis of accounting, revenues, and expenses and related assets and liabilities are recorded when they result from cash transactions, except for the recording of depreciation expense on the capital assets in the government-wide financial statements.

As a result of the use of the modified cash basis of accounting, certain assets and their related revenues (such as accounts and taxes receivable and related revenue not collected yet) and certain liabilities and their related expenses (such as accounts payable and expenses for goods or services received but not paid yet) are not recorded in these financial statements. Therefore when reviewing the financial information and discussion within this annual report, the reader should keep in mind the limitations resulting from the use of the modified cash basis of accounting.

**Government-Wide Financial Statements.** The government-wide financial statements are designed to display information about the Red Lake Watershed District taken as a whole.

Over time, increased or decreased in net assets – modified cash basis may serve as a useful indicator of whether the financial position of the Red Lake Watershed District is improving or deteriorating.

The government-wide financial statements can be found on pages 9 and 10 of this report.

**Fund Financial Statements.** The fund financial statements focus on the individual parts of the District. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. Red Lake Watershed District, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All the funds of Red Lake Watershed District are governmental funds.

All governmental funds utilize a “current financial resources” measurement focus. Only current financial assets and liabilities are generally included on their balance sheets. Their operating statements present sources and uses of available spendable financial resources during a given period. These funds use fund balance as their measure of available spendable financial resources at the end of the period.

Red Lake Watershed District maintains three individual major governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the General Fund, Special Revenue Fund, and the Administrative Construction/Capital Projects Fund, which are considered to be major funds.

Red Lake Watershed District adopts an annual appropriated budget for its General Fund for Statutory/Management purposes.

The basic government fund financial statements can be found on pages 9 through 13 of this report.

**Notes to the financial statements.** The notes provided additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found on pages 14 through 24 of this report.

### **Financial Analysis of the Watershed District**

As noted earlier, net assets – modified cash basis may serve over time as a useful indicator of a government’s financial position. In the case of the Red Lake Watershed District, assets exceeded liabilities by \$13,903,423 by the close of the most recent fiscal year, which is an increase of \$1,583,562 over the prior year; more than a 17% increase over the prior year.

A portion of Red Lake Watershed District’s net assets (\$11,830,922 or 85%) reflects its investment in capital assets less any related debt to acquire those assets that are still outstanding. Red Lake Watershed District uses these capital assets to provide services to citizens; consequently, these are not available for future spending. Although Red Lake Watershed District’s investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

**RED LAKE WATERSHED DISTRICT'S NET ASSETS – MODIFIED CASH BASIS**

	<u>2012</u>	<u>2011</u>
<b>ASSETS</b>		
Total current assets	\$ 2,072,501	\$ 4,269,442
Net capital assets	<u>11,830,922</u>	<u>8,050,419</u>
<b>TOTAL ASSETS</b>	<u><u>\$ 13,903,423</u></u>	<u><u>\$ 12,319,861</u></u>
<b>NET ASSETS</b>	<u><u>\$ 13,903,423</u></u>	<u><u>\$ 12,319,861</u></u>

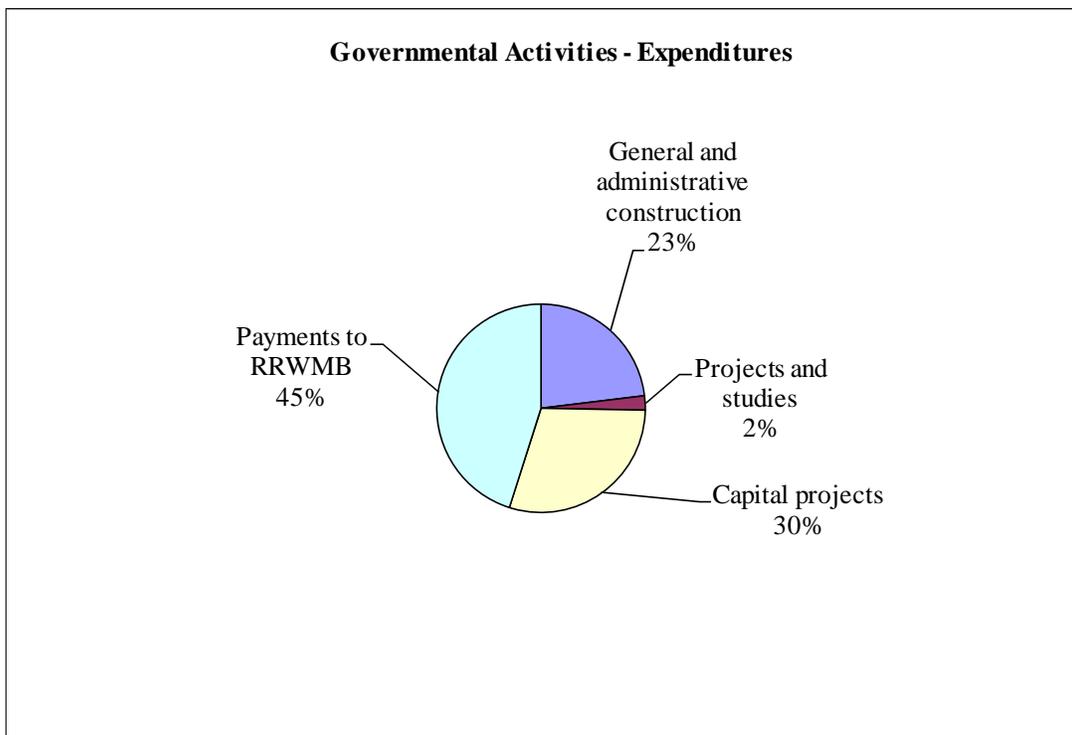
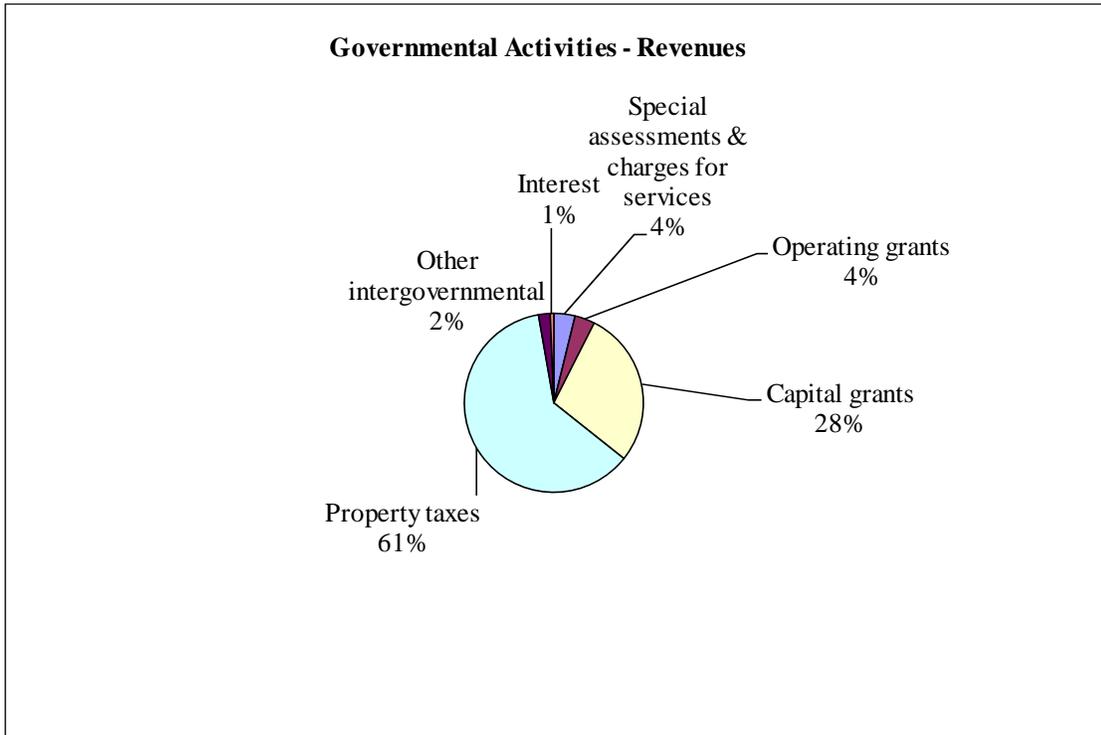
At the end of 2012 and 2011, the Red Lake Watershed District is able to report positive balances in net assets.

**RED LAKE WATERSHED DISTRICT'S CHANGE IN NET ASSETS  
 – MODIFIED CASH BASIS**

Governmental activities resulted in an increase of Red Lake Watershed District's net assets from the fiscal year 2011 to the fiscal year 2012 in the amount of \$1,583,562. The details of the increase are as follows:

	<u>2012</u>	<u>2011</u>
<b>REVENUES</b>		
Special assessments and charges		
for services	\$ 179,910	\$ 405,228
Operating grants	170,898	16,000
Capital grants	1,327,042	1,881,331
General revenues:		
Property taxes	2,893,105	2,481,415
Other intergovernmental	98,384	275,507
Interest	31,144	37,650
<b>TOTAL REVENUES</b>	<u><u>4,700,483</u></u>	<u><u>5,097,131</u></u>
<b>EXPENSES</b>		
General and administration		
construction	719,459	181,175
Ongoing projects and studies	68,447	457,792
Capital projects	923,608	1,359,641
Payments to RRWMB	1,405,407	1,289,116
<b>TOTAL EXPENSES</b>	<u><u>3,116,921</u></u>	<u><u>3,287,724</u></u>
<b>CHANGE IN NET ASSETS</b>	<u><u>\$ 1,583,562</u></u>	<u><u>\$ 1,809,407</u></u>

Below are specific graphs which provide comparisons of the governmental activities revenues and expenditures for the year ended December 31, 2012:



**Financial Analysis of the Government's Funds**

At the end of the current fiscal year, Red Lake Watershed District's governmental funds reported combined ending fund balances of \$4,477,656. The total fund balance can be attributed to 1) General Fund, \$378,057; 2) Capital Projects Fund, \$4,099,599; as well as Special Revenue Fund with a deficit fund balance of -\$2,355,299.

The general fund increased by \$33,496 in 2012, which was due to higher net increases in general revenues over expenses than was originally expected in the budget. The general fund cash balance remained relatively unchanged, however. The board voted to annually allocate the remaining revenue over expenses in the general fund budget to the capital projects fund until all monies borrowed for the new building are paid. The remaining balance of the new watershed district building is reflected on page 20, interfund balances.

**Budgetary Highlights**

**General Fund.** The General Fund exceeded budgeted revenues and had expenditures below the budgeted amounts for the year ended December 31, 2012.

**Capital Asset and Debt Administration**

**Capital assets.** Red Lake Watershed District's investment in capital assets for its governmental activities as of December 31, 2012, amounts to \$11,830,922 (net of accumulated depreciation). This investment in capital assets consists of building, equipment, and infrastructure assets necessary for the District to carryout watershed and conservation management within its service area.

**Red Lake Watershed District's Capital Assets  
 (Net of Depreciation)**

	2012		2011	
	Cost	Accumulated Depreciation	Cost-Less Accumulated Depreciation	Cost-Less Accumulated Depreciation
Building and improvements	\$ 762,888	\$ 171,179	\$ 591,709	\$ 623,400
Infrastructure improvements	7,813,655	1,146,351	6,667,304	5,331,041
Engineering equipment	426,203	305,622	120,581	137,253
Office equipment	128,304	70,918	57,386	46,811
Land & permanent easements	1,767,061	-	1,767,061	1,567,050
Construction in progress	2,626,881	-	2,626,881	344,864
	<u>\$ 13,524,992</u>	<u>\$ 1,694,070</u>	<u>\$ 11,830,922</u>	<u>\$ 8,050,419</u>

**Other Items of Interest.** Construction was completed on RLWD Project No. 171, RLWD Ditch No. 14. Bid opening for the construction of the project was conducted in the spring 2012 and construction continued throughout the summer with the final payment hearing for the contractor was held in December 2012. Funding for this project was paid for by the Special Revenue Fund (benefitted landowners).

Construction was mainly completed in 2012, with a retainer maintained until the completion and final inspection in the spring of 2012, for the Thief River Falls Flood Damage Project (TRF FDR), RLWD Project 171A. Funding for the TRF FDR Project has been paid in part by a Minnesota Flood Damage Reduction Grant, matched by the Red Lake Watershed District using Capital Projects Funds, and a Water Management District that will be paid from Special Revenue Fund.

Construction on one of the retention ponds for Clearbrook Stormwater Retention Pond Project, RLWD Proj. No. 160, was completed in the summer of 2012. It is anticipated that engineering for a second retention pond may be completed in 2013. This project is funded in part from the City of Clearbrook and Clearwater County SWCD, with a majority of the expenditures being paid from the RLWD Capital Projects Fund.

Marshall County Ditch #20 Grade Stabilization/State Ditch No. #83, RLWD Project No. 14D, was completed in 2012. This project reduced sediment loads presently coming from CD #20 and settling into State Ditch #83. A portion of the project was funded through a grant received from the Board of Water and Soil Resources Clean Water Competitive Grant, Marshall County Ditch Authority, with remaining funds being paid from the Special Revenue Fund.

The RLWD also completed construction on a Clean Water Competitive Grant approved project from the Board of Water and Soil Resources (BWSR). This project is referred to as Grand Marais Cut Channel Stabilization Project, RLWD Project 60FF, and is intended to reduce sediment loads in the Red River of the North. The final engineer's report was completed, informational meetings held, and bid opening completed early in 2012. The remaining expenditures not allocated from BWSR will be deducted from the Capital Projects Fund.

Water Quality grants from the State of Minnesota, Minnesota Pollution Control Agency, for Surface Water Assessment Grants, Watershed Assessment Projects (watershed based TMDL), and others are ongoing. Expenses over and above the grants are expended from the Capital Projects Fund.

State of Minnesota flow through grant with Federal Emergency Management Agency (FEMA) for flood plan analysis along on the Red Lake River in Polk, Red Lake, and Pennington Counties has been extended to April 30, 2015. This will allow time for FEMA to determine how past modeling within the city of Crookston and East Grand Forks will match present datum.

More details of the 2012 construction, maintenance, and ongoing water quality programs of Red Lake Watershed District are included in the 2012 Annual Report or by contacting the Red Lake Watershed District.

**Requests for information.** This financial report is designed to provide a general overview of Red Lake Watershed District's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Red Lake Watershed District, 1000 Pennington Avenue South, Thief River Falls, Minnesota 56701.

BASIC FINANCIAL STATEMENTS

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
STATEMENT OF NET ASSETS - MODIFIED CASH BASIS  
DECEMBER 31, 2012

## ASSETS

Current Assets:

Petty cash	\$ 100
Pooled cash and investments	<u>2,072,401</u>
Total Current Assets	<u>2,072,501</u>

Capital Assets:

Property and equipment	13,524,992
Less: accumulated depreciation	<u>(1,694,070)</u>
Net Capital Assets	<u>11,830,922</u>

TOTAL ASSETS	<u>13,903,423</u>
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## NET ASSETS

Investment in capital assets, net of related debt	11,830,922
Unrestricted	<u>2,072,501</u>

TOTAL NET ASSETS	<u>\$ 13,903,423</u>
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RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
STATEMENT OF ACTIVITIES - MODIFIED CASH BASIS  
FOR THE YEAR ENDED DECEMBER 31, 2012

FUNCTION/PROGRAMS	Expenses			Program Revenues			Net (Expenses) Revenues and Changes in Net Assets
	Direct	Allocated Salaries & Overhead	Total	Special Assessments and Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities
General and administrative construction	\$ (719,459)	\$ 543,161	\$ (176,298)	\$ 5,194	\$ -	\$ -	\$ (171,104)
Ongoing projects and studies	(3,038,880)	(129,648)	(3,168,528)	145,163	124,333	846,194	(2,052,838)
Capital projects	2,046,825	(413,513)	1,633,312	29,553	(130,558)	480,848	2,013,155
Payments to RRWMB	(1,405,407)	-	(1,405,407)	-	-	-	(1,405,407)
Allocated interest	(23,243)	-	(23,243)	-	-	-	(23,243)
<b>Total Governmental Activities</b>	<b>\$ (3,140,164)</b>	<b>\$ -</b>	<b>\$ (3,140,164)</b>	<b>\$ 179,910</b>	<b>\$ (6,225)</b>	<b>\$ 1,327,042</b>	<b>(1,639,437)</b>
General Revenues:							
Tax levies							2,893,105
Intergovernmental, (not restricted to specific programs)							
State MV and disparity reduction credits							275,507
Allocated interest							54,387
<b>Total General Revenue</b>							<b>3,222,999</b>
Changes in Net Assets							1,583,562
Net Assets - Beginning							12,319,861
Net Assets - Ending							<b>\$ 13,903,423</b>

See accompanying notes to the basic financial statements.

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
BALANCE SHEET - MODIFIED CASH BASIS  
GOVERNMENTAL FUNDS  
DECEMBER 31, 2012

	<u>General</u>	<u>Special Revenue Fund</u>	<u>Capital Project Fund</u>	<u>Total</u>
<b>ASSETS</b>				
Petty cash	\$ 100	\$ -	\$ -	\$ 100
Pooled cash and investments	377,957	-	1,694,444	2,072,401
Due from other funds	<u>-</u>	<u>-</u>	<u>2,405,155</u>	<u>2,405,155</u>
<b>TOTAL ASSETS</b>	<u><u>378,057</u></u>	<u><u>-</u></u>	<u><u>4,099,599</u></u>	<u><u>4,477,656</u></u>
<b>LIABILITIES</b>				
Due to other funds	<u>49,856</u>	<u>2,355,299</u>	<u>-</u>	<u>2,405,155</u>
<b>TOTAL LIABILITIES</b>	<u>49,856</u>	<u>2,355,299</u>	<u>-</u>	<u>2,405,155</u>
<b>FUND BALANCE</b>				
Spendable:				
Committed for Capital Project	-	-	4,099,599	4,099,599
Unassigned	<u>328,201</u>	<u>(2,355,299)</u>	<u>-</u>	<u>(2,027,098)</u>
<b>TOTAL FUND BALANCES</b>	<u>328,201</u>	<u>(2,355,299)</u>	<u>4,099,599</u>	<u>2,072,501</u>
<b>TOTAL LIABILITIES AND FUND BALANCE</b>	<u><u>\$ 378,057</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 4,099,599</u></u>	<u><u>\$ 4,477,656</u></u>

Amounts reported from governmental activities in the Statement of Net Assets are different because:

Total fund balance per Balance Sheet, from above \$ 2,072,501

When capital assets (land, building, equipment and infrastructure) that are to be used in governmental activities are purchased or constructed, the costs of those assets are reported as expenditures in governmental funds. However, the statements of net assets includes those capital assets among the assets of the District as a whole.

Cost of capital assets	13,524,992
Accumulated depreciation	<u>(1,694,070)</u>

Total Net Assets \$ 13,903,423

See accompanying notes to the basic financial statements.

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES  
MODIFIED CASH BASIS - GOVERNMENTAL FUNDS  
FOR THE YEAR ENDED DECEMBER 31, 2012

	<u>General</u>	<u>Special Revenue Fund</u>	<u>Capital Project Fund</u>	<u>Total</u>
<b>REVENUES</b>				
Tax levies	\$ 180,675	\$ -	\$ 2,712,430	\$ 2,893,105
Intergovernmental				
Federal	-	84,799	107,428	192,227
State	1,806	770,110	427,163	1,199,079
Local	-	37,570	91,206	128,776
Special assessments	-	132,418	-	132,418
Miscellaneous	3,388	90,793	29,553	123,734
Allocated interest	6,425	2,132	45,830	54,387
Total Revenues	<u>192,294</u>	<u>1,117,822</u>	<u>3,413,610</u>	<u>4,723,726</u>
<b>EXPENDITURES</b>				
General and administrative construction	155,182	-	-	155,182
Ongoing projects and studies	-	3,151,856	-	3,151,856
Capital projects	-	-	2,184,979	2,184,979
Payments to RRWMB	-	-	1,405,407	1,405,407
Allocated interest	3,616	15,788	3,839	23,243
Total Expenditures	<u>158,798</u>	<u>3,167,644</u>	<u>3,594,225</u>	<u>6,920,667</u>
Revenues Over (Under) Expenditures	33,496	(2,049,822)	(180,615)	(2,196,941)
<b>OTHER FINANCING SOURCES (USES)</b>				
Transfers in	546,830	237	446,705	993,772
Transfers out	(546,830)	-	(446,942)	(993,772)
Net Other Sources (Uses)	<u>-</u>	<u>237</u>	<u>(237)</u>	<u>-</u>
Revenues & Other Sources Over (Under) Expenditures & Other Uses	33,496	(2,049,585)	(180,852)	(2,196,941)
Fund Balance (Deficit), January 1	<u>294,705</u>	<u>(305,714)</u>	<u>4,280,451</u>	<u>4,269,442</u>
Fund Balance (Deficit), December 31	<u>\$ 328,201</u>	<u>\$ (2,355,299)</u>	<u>\$ 4,099,599</u>	<u>\$ 2,072,501</u>

See accompanying notes to the basic financial statements.

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
RECONCILIATION OF CHANGE IN FUND BALANCES OF GOVERNMENTAL FUNDS  
TO THE STATEMENT OF ACTIVITIES  
FOR THE YEAR ENDED DECEMBER 31, 2012

Net Change in Fund Balances - Total Governmental Funds	\$ (2,196,941)
<p>Governmental funds report capital outlay as expenditures, while governmental activities report depreciation expense allocating those expenditures over the life of the asset:</p>	
Capital additions	4,116,938
Depreciation expense	<u>(336,435)</u>
Change in Net Assets - Governmental Activities	<u>\$ 1,583,562</u>

See accompanying notes to the basic financial statements.

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
BUDGETARY COMPARISON - MODIFIED CASH BASIS  
GOVERNMENTAL FUNDS  
FOR THE YEAR ENDED DECEMBER 31, 2012

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>	<u>Final Budget to Actual Variance</u>
<b>REVENUES</b>				
Tax levies	\$ 180,475	\$ 180,475	\$ 180,675	\$ 200
Intergovernmental				
State	-	-	1,806	1,806
Miscellaneous	-	-	3,388	3,388
Allocated interest	-	-	2,809	2,809
Total Revenues	<u>180,475</u>	<u>180,475</u>	<u>188,678</u>	<u>8,203</u>
<b>EXPENDITURES</b>				
General and administrative	<u>180,475</u>	<u>180,475</u>	<u>155,182</u>	<u>25,293</u>
Revenues Over (Under) Expenditures	-	-	33,496	33,496
<b>OTHER FINANCING SOURCES (USES)</b>				
Transfers in	-	-	546,830	546,830
Transfers out	<u>237</u>	<u>-</u>	<u>(546,830)</u>	<u>(546,830)</u>
Net Other Sources (Uses)	<u>237</u>	<u>-</u>	<u>-</u>	<u>-</u>
Revenues & Other Sources Over (Under) Expenditures & Other Uses	237	-	33,496	33,496
Fund Balance (Deficit), January 1	<u>294,705</u>	<u>294,705</u>	<u>294,705</u>	<u>-</u>
Fund Balance (Deficit), December 31	<u>\$ 294,942</u>	<u>\$ 294,705</u>	<u>\$ 328,201</u>	<u>\$ 33,496</u>

See accompanying notes to the basic financial statements.

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
NOTES TO BASIC FINANCIAL STATEMENTS  
FOR THE YEAR ENDED DECEMBER 31, 2012

The Red Lake Watershed District, (the "District") was established under the Minnesota Watershed Act as an agency of the State of Minnesota. The purpose of the District is to carry out conservation of the natural resources of the State of Minnesota through land utilization, flood control, and other needs upon sound scientific principles for the protection of the public health and welfare and the provident use of natural resources. The District serves an area in Northwestern Minnesota and includes all of Red Lake County and parts of the following counties: Beltrami, Clearwater, Itasca, Koochiching, Mahnomen, Marshall, Pennington, Polk and Roseau. The District is governed by the Board of Managers, which is composed of seven members appointed by the county boards in accordance with Minnesota Statutes.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

As discussed in Note 1.C, these financial statements are presented on a modified cash basis of accounting. This modified basis of accounting differs from accounting principles generally accepted in the United States of America (GAAP). Generally accepted accounting principles include all relevant Governmental Accounting Standards (GASB) pronouncements. In the government-wide financial statements, Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board (APB) opinions issued on or after November 30, 1989, have been applied, to the extent applicable to the modified cash basis of accounting, unless those pronouncements conflict with or contradict GASB pronouncements.

A. Reporting Entity

The financial statements of the District include all organizations, funds and account groups over which the District's Board exercises significant influence over and, or is financially accountable or organizations for which the nature and significance of their relationship with the District is such that exclusion would cause the Red Lake Watershed District's financial statements to be misleading. Currently, the District does not have any component units.

B. Basis of Presentation

*Government-Wide Financial Statement*

The Statement of Net Assets and Statement of Activities display information about the reporting government taken as a whole. They include all funds of the reporting entity except any fiduciary funds. The statements would distinguish between governmental and business-type activities (if any). Governmental activities are typically financed through taxes, intergovernmental revenues and other non-exchange revenues, because of this all of the District's activities are reported as governmental activities.

*Fund Financial Statements*

Fund financial statements of the District are organized into funds, each of which is considered to be a separate accounting entity. Each fund is accounted for by providing a separate set of self-balancing accounts that constitute its assets, liabilities, fund equity, revenues and expenditures. Funds are typically organized into two major categories: governmental and proprietary. The District currently has no proprietary or fiduciary funds.

An emphasis is placed on major funds within the governmental categories. A fund is considered major if it is the primary operating fund of the District or meets the following criteria:

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
NOTES TO BASIC FINANCIAL STATEMENTS

1. Total assets, liabilities, revenues or expenditures of that individual governmental fund are at least 10 percent of the corresponding total for all funds of that type, AND
2. Total assets, liabilities, revenues or expenditures of the individual governmental fund are at least 5% of the corresponding total for all governmental funds combined.

*Governmental Funds*

General Fund

The general fund is the primary operating fund of the District and always classified as a major fund. It is used to account for all activities except those legally or administratively required to be accounted for in other funds.

Special Revenue Fund

The special revenue fund is used to account for the proceeds of specific revenue sources (other than capital projects) where the expenditures are legally restricted for purposes specified in the grant or project agreements. The reporting entity includes the special revenue fund as a major fund.

Capital Projects Fund

The capital projects fund is used to account for the financial resources to be used for the acquisition or construction of capital projects. The reporting entity includes the capital projects fund as a major fund.

C. Measurement Focus and Basis of Accounting

Measurement focus is a term used to describe the recognition of revenues and expenditures within the various financial statements. Basis of accounting refers to “when” transactions are recorded regardless of the measurement focus applied.

*Measurement Focus*

In government-wide Statement of Net Assets and the Statement of Activities, governmental activities are presented using the economic resources measurement focus, within the limitations of the modified cash basis of accounting, as defined below.

In the fund financial statements, the “current financial resources” measurement focus or the “economic resources” measurement focus, as applied to the modified cash basis of accounting is used as appropriate:

All governmental funds utilize a “current financial resources” measurement focus. Only current financial assets and liabilities are generally included on their balance sheets. Their operating statements present sources and uses of available spendable financial resources during a given period. These funds use fund balance as their measure of available spendable financial resources at the end of the period.

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
NOTES TO BASIC FINANCIAL STATEMENTS

When fund balance resources are available for use, it is the government's policy to use restricted, committed, assigned, and unassigned resources as they are needed in that order.

*Basis of Accounting*

In the government-wide Statement of Net Assets and Statement of Activities governmental activities are presented using a modified basis of accounting. This basis recognizes assets, liabilities, net assets, revenues and expenditures when they result from cash transactions with a provision for depreciation in government-wide statements. This basis is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

As a result of the use of modified cash basis of accounting, certain assets and their related revenues (such as accounts receivable and revenue for billed or unbilled services provided in current year) and certain liabilities and their related expense (such as accounts payables, unpaid good or services received in the current year and accrued expenses) are not recorded in these financial statements.

If the District utilized the basis of accounting recognized as generally accepted, the fund financial statements for governmental funds would use the modified accrual basis of accounting and the government-wide financials would be presented on the accrual basis of accounting.

D. Budgets

The budget is prepared using the same method of accounting as the financial statements. The annual adopted budget is not legally binding on the District, with the exception of the budget for the general fund, which is limited by state statute at \$250,000 and set by the Board for 2012 at \$180,475. All appropriations lapse at year-end.

E. Revenues

In the Statement of Activities, modified cash basis revenues that are derived directly from each activity or from parties outside the District's taxpayers are reported as program revenues. The District has the following program revenues; direct project cost reimbursements and project special assessments, rental income and operating and capital grants specific to projects. All other governmental revenues and general tax levies are classified as general revenue.

F. Property Taxes

The District levies property taxes on property owners within the District, which becomes an enforceable lien as of January 1. Taxes are levied in September and are payable to counties on May 15 and October 15 (November 15 for farm property) of the following year. The District levies the tax, while the respective counties collect and remit the tax collections to the District. Property taxes are recognized when received from the counties under the cash basis of accounting.

The District also levies special assessments through the counties against property owners who obtain direct benefits from projects or property owners who request, through the petition process, to have a project undertaken. The special assessment collections are recorded in a manner similar to that for property taxes.

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
NOTES TO BASIC FINANCIAL STATEMENTS

G. Cash and Investments

Cash balances from all funds are pooled and invested to the extent available in authorized investments authorized by Minnesota statutes. Earnings from such investments are allocated to the respective funds on the basis of average cash balance participation by each fund. Funds with deficit averages are charged with the investment earnings lost in financing the deficits.

H. Capital Assets

The District’s modified cash basis of accounting reports capital assets resulting from cash transactions and reports depreciation where appropriate.

All capital assets are valued at historical cost or if donated recorded at its estimated fair value. Infrastructure assets acquired prior to January 1, 2004 are not capitalized, but subsequent acquisitions are recorded at cost.

In the government-wide financial statements, capital assets arising from cash transactions are accounted for as an expense in the Statement of Net Assets, with accumulated depreciation reflected in the Statement of Net Assets. Depreciation is provided over the assets’ estimated useful lives using the straight-line method of depreciation. Capitalization thresholds of \$500 for equipment and building improvements and \$10,000 for infrastructure are used to report capital assets. Estimated useful lives being used are summarized below:

Building & improvements	19 - 40 years
Equipment, furniture and fixtures	5 – 15 years

In governmental fund financial statements, capital assets arising from cash transactions acquired for use in governmental fund operations are accounted for as capital outlay expenditures of the governmental fund upon acquisition.

I. Long-Term Debt

All long-term debt arising from cash transactions to be repaid from governmental fund resources is reported as a liability only in the government-wide statements.

Long-term debt arising from cash basis transactions of governmental funds is not reported as liabilities in the fund financial statements. The debt proceeds are reported as other financing sources and the payment of principal and interest reported as expenditures.

J. Compensated Absences

Full-time employees employed for six months with the District accrue 80 hours per year of vacation for the first five years of employment. During the next five years of employment, an employee accrues 120 hours per year and after ten years of employment, an employee accrues 160 hours per

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
NOTES TO BASIC FINANCIAL STATEMENTS

year of vacation. Qualifying part-time employees are entitled to vacation based on the percentage of hours worked per pay period. The maximum accumulation of vacation leave is 200 hours. Unused vacation leave is paid only upon termination of employment.

Full-time employees employed with the District accrue eight hours of sick leave per month. Part-time employees who have worked 60 percent of the time for a period of nine months shall be entitled to sick leave based on the percentage of hours worked per pay period. The maximum accumulation of sick leave is 336 hours and does not vest upon termination of employment. No vested or accumulated liability has been recorded for accumulated compensated absences.

K. Equity

In the government-wide financial statements equity is classified as “net assets” and displayed in three components:

1. Investment in Capital Assets, Net of Related Debt – consists of capital assets including restricted capital assets, net of accumulated depreciation and reduced by any outstanding debt issued that is attributable to the acquisition, construction, or improvements of those assets.
2. Restricted Net Assets – Consists of net assets with constraints placed on the use either by (1) external groups such as creditors, grantors, contributors, or laws and regulations of other governments; or (2) law through constitutional provisions or enabling legislation.
3. Unrestricted Net Assets – All other net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

L. Net Assets/Fund Balance

The difference between assets and liabilities is “Net Assets” on the government wide financial statements and “Fund Balance” on the governmental fund financial statements.

In the governmental fund financial statements, fund balances are classified as nonspendable, restricted, committed, assigned or unassigned.

Nonspendable fund balance represents a portion of fund balance that includes amounts that cannot be spent because they are either (a) not in spendable form or (b) legally or contractually required to be maintained intact.

Restricted fund balance represents a portion of fund balance that reflects constraints placed on the use of resources (other than nonspendable items) that are either: (a) externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments; or (b) imposed by law through constitutional provisions or enabling legislation.

Committed fund balance includes amounts that can only be used for specific purposes pursuant to constraints imposed by formal action of the government’s highest level of decision making authority which is the Board of Managers through a resolution.

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
NOTES TO BASIC FINANCIAL STATEMENTS

Assigned fund balance represents amounts constrained by the government's intent to be used for specific purposes, but neither restricted nor committed.

Unassigned fund balance represents residual classification for the general fund. This classification represents fund balance not assigned to other funds and not restricted, committed, or assigned to specific purposes within the general fund. The general fund should be the only fund that reports a positive unassigned fund balance amount. In other governmental funds, if expenditures incurred for specific purposes exceeded the amounts restricted, committed, or assigned to those purposes, it would be necessary to report a negative unassigned fund balance.

The first priority is to utilizing the restricted before unrestricted fund balance when both are available. Committed funds will be considered spent first when an expenditure is incurred for purposes for which amounts in any of those unrestricted fund balance classification could be used like assigned or unassigned.

M. Interfund Balances

In the process of aggregating the fund information for the government-wide Statement of Net Assets and Statement of Activities, some amounts reported as interfund activity and balances in the fund financial statements have been eliminated or reclassified.

N. Estimates

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

O. Subsequent Events

Red Lake Watershed District has evaluated subsequent events through March 7, 2013, the date which the financial statements were available to be issued.

NOTE 2. CASH AND INVESTMENTS

In accordance with applicable Minnesota Statutes, the District maintains deposits at depository banks authorized by the District's Board.

Minnesota Statutes require that all deposits be protected by federal deposit insurance, corporate surety bond, or collateral. The market value of collateral pledged must equal 110% of the deposits not covered by federal deposit insurance or corporate surety bonds.

At December 31, 2012, all deposits were protected by federal deposit insurance, corporate surety bond, or collateral as required by Minnesota Statute.

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
NOTES TO BASIC FINANCIAL STATEMENTS

Interest Rate Risk

The District does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk

The District may invest idle funds as authorized by Minnesota statutes, as follows: direct obligations or obligations guaranteed by the United States or its agencies; shares of investment companies registered under the Federal Investment Company Act of 1940 and receives the highest credit rating, is rated in one of the two highest rating categories by a statistical rating agency, and all of the investments have a final maturity of thirteen months or less; general obligations rated "A" or better; revenue obligations rated "AA" or better, general obligations of the Minnesota Housing Finance Agency rated "A" or better; bankers' acceptances of United States' banks eligible for purchase by the Federal Reserve System; commercial paper issued by United States' corporations or their Canadian subsidiaries, of the highest quality category by at least two nationally recognized rating agencies, and maturing in 270 days or less; Guaranteed Investment Contracts guaranteed by a United States commercial bank, domestic branch of a foreign bank, or a United States insurance company, and with a credit quality in one of the top two highest categories; repurchase or reverse purchase agreements and securities lending agreements with financial institutions qualified as a "depository" by the government entity, with banks that are members of the Federal Reserve System with capitalization exceeding \$10,000,000, a primary reporting dealer in U.S. government securities to the Federal Reserve Bank of New York, or certain Minnesota securities broker-dealers. The District has no investment policy that would further limit its investment choices.

NOTE 3. INTERFUND BALANCES

The following reconciles interfund receivables and payables as of December 31, 2012:

<u>Advances from/Advances to</u>	<u>Receivables</u>	<u>Payables</u>
Capital Projects Fund	\$ 2,405,155	\$ -
Special Revenue Fund	-	2,355,299
General Fund	-	49,856
	<u>\$ 2,405,155</u>	<u>\$ 2,405,155</u>

The \$49,856 interfund receivable and payable was created to show the amount due to the Capital Projects Fund for the new RLWD building and garage. This amount will be allocated annually from the General Fund until monies borrowed from the Capital Projects Fund are paid. The \$2,355,299 interfund receivable and payable was created to cover cash shortage created from operations.

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
NOTES TO BASIC FINANCIAL STATEMENTS

NOTE 4. CAPITAL ASSET

Capital assets activity resulting from modified cash basis transactions for the year ended December 31, 2012, was as follows:

	Beginning Balance	Adjustments	Additions	Deletions	Ending Balance
<u>Capital Assets</u>					
Building and Improvements	\$ 762,888	\$ -	\$ -	\$ -	\$ 762,888
Infrastructure improvements	6,235,119	-	1,578,536	-	7,813,655
Engineering equipment	417,302	-	30,747	21,846	426,203
Office equipment	108,588	-	25,543	5,827	128,304
Land & permanent easements	1,567,050	-	200,011	-	1,767,061
Construction in progress	344,864	-	2,626,881	344,864	2,626,881
Total	<u>\$ 9,435,811</u>	<u>\$ -</u>	<u>\$ 4,461,718</u>	<u>\$ 372,537</u>	<u>\$ 13,524,992</u>

	Beginning Balance	Adjustments	Additions	Deletions	Ending Balance
<u>Accumulated Depreciation</u>					
Building and improvements	\$ 139,488	\$ -	\$ 31,691	\$ -	\$ 171,179
Infrastructure improvements	904,078	-	242,273	-	1,146,351
Engineering equipment	280,049	-	47,621	22,048	305,622
Office equipment	61,777	-	14,850	5,709	70,918
Total	<u>1,385,392</u>	<u>-</u>	<u>336,435</u>	<u>27,757</u>	<u>1,694,070</u>
Net Capital Assets	<u>\$ 8,050,419</u>	<u>\$ -</u>	<u>\$ 4,125,283</u>	<u>\$ 344,780</u>	<u>\$ 11,830,922</u>

Depreciation expense of \$336,435 for the year ended December 31, 2012 is included in general and administrative program costs.

NOTE 5. OVERHEAD COST ALLOCATION

Overhead costs are allocated to all projects at 150% of direct salaries charged to projects. Overhead costs represent those costs incurred by the District for administration, employee benefits, engineering, and related operating expenditures, which are not charged directly to the project. The total overhead costs charged to projects in 2012 were \$543,161.

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
NOTES TO BASIC FINANCIAL STATEMENTS

NOTE 7. DEFINED BENEFIT PENSION PLANS - STATEWIDE

A. Plan Description

All full-time and certain part-time employees of the Red Lake Watershed District are covered by a defined benefit pension plan administered by the Public Employees Retirement Association of Minnesota (PERA). PERA administers the General Employees Retirement Fund (GERF) which is a cost-sharing multiple-employer retirement plan. This plan is established and administered in accordance with Minnesota Statutes, Chapter 353 and 356.

GERF members belong to either the Coordinated Plan or the Basic Plan. Coordinated members are covered by Social Security and Basic members are not. All new members must participate in the Coordinated Plan.

PERA provides retirement benefits as well as disability benefits to members, and benefits to survivors upon death of eligible members. Benefits are established by state statute, and vest after three years of credited service. The defined retirement benefits are based on a member's highest average salary for any five successive years of allowable service, age, and years of credit at termination of service.

Two methods are used to compute benefits for PERA's Coordinated and Basic Plan members. The retiring member receives the higher of 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 10 years of service and 2.7 percent for each remaining year. The annuity accrual rate for a Coordinated Plan member is 1.2 percent of average salary for each of the first 10 years and 1.7 percent for each remaining 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 all GERF members hired prior to July 1, 1989 whose annuity is calculated using Method 1, a full annuity is available when age plus years of service equal 90. Normal retirement age is 65 for Basic and Coordinated members hired prior to July 1, 1989. Normal retirement age is the age for unreduced Social Security benefits capped at 66 for Coordinated members hired on or after July 1, 1989. A reduced retirement annuity is also available to eligible members seeking early retirement.

There are different types of annuities available to members upon retirement. A single-life annuity is a lifetime annuity that ceases upon the death of the retiree. No survivor annuity is payable. There are also various types of joint and survivor annuity options available which will reduce the monthly normal annuity amount, because the annuity is payable over joint lives. Members may also leave their contributions in the fund upon termination of public service, in order to qualify for a deferred annuity at retirement age. Refunds of contributions are available at any time to members who leave public service, but before retirement benefits begin.

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

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
NOTES TO BASIC FINANCIAL STATEMENTS

not receiving them yet, are bound by the provisions in effect at the time they last terminated their public service.

PERA issues a publicly available financial report that includes financial statements and required supplementary information for GERP. That report may be obtained on the Internet at [www.mnpera.org](http://www.mnpera.org) or by writing to PERA, 60 Empire Drive #200, St. Paul, Minnesota, 55103-2088 or by calling (651) 296-7460 or 1-800-652-9026.

B. Funding Policy

Minnesota Statutes Chapter 353 sets the rates for employer and employee contributions. These statutes are established and amended by the state legislature. The District makes annual contributions to the pension plans equal to the amount required by state statutes. GERP Basic Plan members and Coordinated Plan members were required to contribute 9.10% and 6.25%, respectively, of their annual covered salary in 2012. The District is required to contribute the following percentages of annual covered payroll: 11.78% for Basic Plan GERP members and 7.25% for Coordinated Plan GERP members. The District's contributions to the Public Employees Retirement Fund for the years ending December 31, 2012, 2011 and 2010 were \$24,935, \$24,177, and \$22,763 respectively. The District's contributions were equal to the contractually required contributions for each year as set by state statute.

NOTE 8. RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters. The District carries commercial insurance coverages on its commercial property and for liability, personal and advertising injury, non-owned auto and a miscellaneous floater. Insurance coverage has not been reduced from the prior year, and settlements have not exceeded insurance coverage in any of the past three years.

NOTE 9. CONTINGENCIES

Grants

The District participates in state and federal grant programs, which are governed by various rules and regulations of the grantor agencies. Costs charged to the respective grant programs are subject to audit and adjustment by the grantor agencies; therefore, to the extent that the District has not complied with the rules and regulations governing the grants, refunds of money received may be required and the collectability of any related receivable at December 31, 2012, may be impaired. The District is not aware of any significant contingent liabilities relating to compliance with the rules and regulations governing the respective grants.

Claims and Litigation

The District is involved in some legal actions relating to projects undertaken or attempted to be undertaken. Although the outcomes cannot be determined, the District believes any potential liability would not have a material impact on the financial condition of the District.

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
NOTES TO BASIC FINANCIAL STATEMENTS

NOTE 10. DEFICIT FUND BALANCE

Special Revenue Fund

A deficit fund balance in the amount of \$2,355,299 exists in the special revenue fund. The deficit is expected to be recovered by future revenues, or if necessary, by transfers from other funds.

NOTE 11. CONSTRUCTION COMMITMENTS

During the year the District had entered into construction projects that had not been completed at year-end.

SUPPLEMENTAL INFORMATION

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
SCHEDULE OF CHANGES IN FUND BALANCES - MODIFIED CASH BASIS  
FOR THE YEAR ENDED DECEMBER 31, 2012

	Fund Balance (Deficit) January 1	Revenues				Expenditures			Transfers	Fund Balance (Deficit) December 31
		Assessments and Other Charges for Services	Operating / Capital Grants and Contributions	Allocated Interest Earned	Taxes	Direct	Allocated Interest Charged	Salary & Overhead Allocation	In (Out)	
GENERAL FUND	\$ 294,705	5,194	-	6,425	180,675	698,343	3,616	(543,161)	-	\$ 328,201
SPECIAL REVENUE FUND JOBS:										
Branch A & 1, J.D. #2	5,115	-	-	47	-	-	-	609	-	4,553
Burnham Creek channel	11,711	9,302	-	88	-	6,325	-	5,472	-	9,304
Clearwater County ditch #1	418	-	-	4	-	-	-	-	-	422
Clearwater County joint ditch #1	(237)	-	-	-	-	-	-	-	237	-
Clearwater County joint ditch #4	1,001	-	-	10	-	-	-	-	-	1,011
Clearwater County joint ditch #5	(8,580)	4,659	-	-	-	193	73	995	-	(5,182)
Clearwater River project	27,659	-	-	267	-	-	-	383	-	27,543
Clearwater/Wild Rice River	9,743	3,877	-	77	-	849	-	6,638	-	6,210
Clifford Arveson ditch	2,488	124	-	22	-	900	-	210	-	1,524
Equality RLWD ditch #1, lat C	170	3,224	-	11	-	360	-	52	-	2,993
Improvement to Penn. Co. Dt. 1	(119,469)	80	84,799	-	-	632,515	4,970	32,999	-	(705,074)
J.D. ditch #72	3,060	3,201	-	-	-	7,907	8	3,703	-	(5,357)
K. Johnson petition	1,769	2,000	-	19	-	315	-	461	-	3,012
Krostue petition	5,775	-	-	50	-	1,080	-	417	-	4,328
Lost River project	18,920	1,858	-	157	-	2,764	-	3,088	-	15,083
Main J.D. #2 and branch B & C	(16,022)	4,548	-	-	-	315	142	901	-	(12,832)
Main J.D. 2C. Eck	485	-	-	-	-	-	5	1,077	-	(597)
Pine Lake maintenance	1,790	4,006	-	19	-	901	-	3,063	-	1,851
Polk Cnty ditch #33 improvement	2,558	-	-	16	-	1,170	-	845	-	559
Polk Cnty ditch #63 improvement	7,055	10,582	-	114	-	900	-	348	-	16,503
Polk Cnty ditch #'s 104, 61, 47, 94	(6,179)	10,862	-	-	-	4,230	33	2,117	-	(1,697)
Red Lake River project	67,223	-	-	653	-	-	-	446	-	67,430
RLWD ditch #1	10,852	-	4,639	72	-	5,422	-	3,228	-	6,913
RLWD ditch #3	(10,353)	3,001	14,036	-	-	8,064	84	1,683	-	(3,147)
RLWD ditch #7	5,087	5,604	18,895	5	-	20,890	-	4,705	-	3,996
RLWD Ditch #8	(16,950)	2,005	-	-	-	360	161	257	-	(15,723)
RLWD Ditch #9	3,625	-	-	34	-	150	-	79	-	3,430
RLWD Ditch #10	(10,577)	7,693	-	-	-	495	79	723	-	(4,181)
RLWD Ditch #11	39,453	-	-	372	-	1,440	-	1,335	-	37,050
RLWD Ditch #12	(31,809)	14,962	-	-	-	4,570	281	1,857	-	(23,555)
RLWD Ditch #13	(1,081)	7,565	-	52	-	415	-	1,477	-	4,644
Scott Baatz petition	1,224	1,000	-	15	-	180	-	-	-	2,059
State ditch #83	(14,280)	34,642	16,000	-	-	81,054	355	11,307	-	(56,354)
TRF drainage ditch (Challenger Ditch)	3,373	3	-	28	-	270	-	867	-	2,267
Thief River Falls Flood Damage Reduction Proj.	(293,587)	5,100	832,158	-	-	2,236,554	9,540	36,915	-	(1,739,338)
Winsor/Hangaard/Clearwater County petition	(7,144)	5,265	-	-	-	1,620	57	1,391	-	(4,947)
Total Special Revenue	(305,714)	145,163	970,527	2,132	-	3,022,208	15,788	129,648	237	(2,355,299)

RED LAKE WATERSHED DISTRICT  
 THIEF RIVER FALLS, MINNESOTA  
 SCHEDULE OF CHANGES IN FUND BALANCES - MODIFIED CASH BASIS

	Revenues					Expenditures			Transfers	Fund Balance (Deficit) December 31
	Fund Balance (Deficit) January 1	Assessments and Other Charges for Services	Operating / Capital Grants and Contributions	Allocated Interest Earned	Taxes	Direct	Allocated Interest Charged	Allocated Salary & Overhead	In (Out)	
CAPITAL PROJECT FUND JOBS:										
Administrative construction	3,627,090	-	98,384	41,376	2,712,430	1,405,407	2	-	(445,685)	4,628,186
Badger Creek / Poplar River	6,596	-	-	64	-	-	-	-	-	6,660
Bench Marks	-	-	-	-	-	-	1	105	106	-
Shirrick Dam	-	-	-	-	-	1,192	3	797	1,992	-
Brandt Channel Ditch	-	-	-	-	-	52,963	181	7,662	-	(60,806)
BWSR flood storage pilot project	-	-	-	-	-	410	1	132	543	-
C. Flage Erosion Cont.	(41)	1,925	-	-	-	141,688	285	2,922	-	(143,011)
Clearbrook Flood Damage Reduction	-	-	-	-	-	-	-	105	105	-
Clearwater public education (River Watch)	-	-	-	-	-	2,515	183	29,177	31,875	-
Clearwater River - TMDL	-	-	-	-	-	-	14	3,367	3,381	-
Clearwater River Dissolved Oxygen TMDL	-	-	-	5	-	(1,353)	-	134	(1,224)	-
Clearbrook Stormwater Pjt.	(13,787)	-	-	-	-	52,041	236	4,163	-	(70,227)
County Ditch 20/State Ditch 83	153,416	720	-	831	-	123,484	-	12,898	-	18,585
Culvert Sizing	-	-	-	-	-	-	26	5,689	5,715	-
Ditch 66 WQ Study	3,586	-	54,207	130	-	40,618	-	2,286	2,155	17,174
Elm Lake	-	-	-	-	-	-	5	948	953	-
Emergency maintenance	106,431	-	-	1,037	-	-	-	-	-	107,468
Erosion control projects	-	-	-	-	-	17,932	74	2,460	20,466	-
G.I.S.	-	-	-	-	-	402	172	37,580	38,154	-
Glacial ridge	3,315	-	-	30	-	-	-	500	470	3,315
Euclid East Impoundment	-	1,721	-	-	-	3,173	19	967	2,438	-
Brandt Channel Restoration	-	3,546	-	20	-	986	-	375	-	2,205
Grand Marais - Restoration	(47,980)	-	138,026	-	-	132,251	473	12,810	-	(55,488)
Grand Marais Cut Channel Stabilization	602,884	120	-	2,337	-	914,213	-	13,057	-	(321,929)
Brandt Impoundment	-	-	-	-	-	1,049	10	1,396	2,455	-
FEMA D-Firm Grant	(26,840)	8,237	68,634	-	-	58,631	181	3,315	3,496	(8,600)
Grand Marais Creek Subwatershed	(2,554)	-	9,708	-	-	14,521	78	4,030	11,475	-
Hydrologic analysis	-	-	-	-	-	110	40	6,337	6,487	-
Lost River impoundment	-	-	-	-	-	-	3	478	481	-
Louisville/Parnell project	-	3,405	-	-	-	7,585	27	3,782	7,989	-
RRWMB - Technical Com	-	-	466	-	-	433	-	-	(33)	-
Maintenance dams	-	-	-	-	-	2,917	23	2,485	5,425	-
Moose River project	-	-	-	-	-	13,379	106	5,421	18,906	-
North Parnell storage site	-	-	-	-	-	360	1	66	427	-
Parnell impoundment	-	2,400	-	-	-	7,949	39	5,057	10,645	-

RED LAKE WATERSHED DISTRICT  
 THIEF RIVER FALLS, MINNESOTA  
 SCHEDULE OF CHANGES IN FUND BALANCES - MODIFIED CASH BASIS

	Revenues					Expenditures			Transfers	Fund Balance (Deficit) December 31
	Fund Balance (Deficit) January 1	Assessments and Other Charges for Services	Operating / Capital Grants and Contributions	Allocated Interest Earned	Taxes	Direct	Allocated Interest Charged	Allocated Salary & Overhead	In (Out)	
CAPITAL PROJECT FUND JOBS (continued)										
Permits	-	4,015	-	-	-	10,257	394	73,678	80,314	-
Project Development	-	-	-	-	-	909	205	41,033	42,147	-
Red Lake Res./Good Lake	-	-	-	-	-	22,296	74	2,922	25,292	-
Red River Basin Long Term Flood Control	-	-	-	-	-	3,355	32	4,545	7,932	-
Red River Corridor	-	-	-	-	-	-	-	-	-	-
Red Lake River Watershed Assessment	(13,077)	-	58,963	-	-	18,067	86	30,322	-	(2,589)
RLRVR Grand Marais Swag	-	-	39,195	-	-	44,566	74	5,359	-	(10,804)
Ring dike program -										
General	(115)	-	432	-	-	12	-	1,682	1,377	-
Radi	(80,140)	3,368	65,805	-	-	-	124	1	11,092	-
Adams	-	-	-	-	-	-	-	-	-	-
Bible Baptist Church	(26)	-	3	-	-	-	-	-	23	-
Stream gauging	-	-	-	-	-	10,570	160	9,075	19,805	-
Ten Year Overall Plan	-	-	-	-	-	-	-	84	84	-
Thief River TMDL	(31,521)	-	70,360	-	-	12,203	177	33,403	-	(6,944)
TR WS Sediment Investigation	-	-	-	-	-	-	-	95	95	-
TR SWAGG	(6,786)	-	16,974	-	-	10,901	39	2,844	-	(3,596)
Water Quality	-	96	4,640	-	-	46,601	265	33,595	75,725	-
Web Page Development	-	-	-	-	-	1,315	18	2,268	3,601	-
Wetland Banking	-	-	-	-	-	965	8	2,106	3,079	-
WS Ditch System Inventory & Mapping	-	-	-	-	-	-	-	-	-	-
Total Capital Projects	4,280,451	29,553	625,797	45,830	2,712,430	3,176,873	3,839	413,513	(237)	4,099,599
Total - All Funds	\$ 4,269,442	179,910	1,596,324	54,387	2,893,105	6,897,424	23,243	-	-	\$ 2,072,501

RED LAKE WATERSHED DISTRICT  
THIEF RIVER FALLS, MINNESOTA  
SCHEDULE OF DIRECT EXPENDITURES BY CLASSIFICATION - MODIFIED CASH BASIS  
GOVERNMENTAL FUNDS  
FOR THE YEARS ENDED DECEMBER 31, 2012 AND 2011

	2012	2011
<u>DIRECT EXPENDITURES:</u>		
Salaries -		
Inspection	\$ 18,472	\$ 10,448
Survey - preliminary	2,940	7,591
Survey - construction	3,533	422
Drafting	15,173	11,706
Engineering	71,391	68,648
Project administration	186,684	197,399
Field work -water programs	12,482	10,669
Other	40,141	27,244
Compensated absences	31,115	33,903
Payroll taxes and benefits	113,816	110,962
Manager's expenses	21,112	22,919
Travel, mileage, meetings and per diems	3,479	4,086
Audit	8,630	8,380
Legal	29,506	24,275
Appraisal and viewers	235	16,746
Other professional fees	177,077	466,630
Office supplies	13,958	15,797
Office equipment	25,543	22,556
Dues & subscriptions	3,760	4,702
Insurance and bonds	34,177	28,826
Rent	-	-
Repairs and maintenance	14,923	11,864
Utilities	6,705	6,215
Telephone	10,907	10,136
Advertising and publications	9,648	8,818
Truck expense	20,253	19,130
Red River Watershed Management Board	1,405,407	1,289,116
Cost share assistance	-	9,338
Land acquisition and easements	200,012	129,271
Construction	3,809,951	356,737
Engineering costs & fees	14,183	6,895
Engineering fees	522,198	428,390
Engineering equipment	30,747	31,538
Glacial Ridge	39,266	238,943
Ring dike reimbursement	-	20,173
	\$ 6,897,424	\$ 3,660,473
Total Expenditures	\$ 6,897,424	\$ 3,660,473

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AUDITORS' REPORT ON LEGAL COMPLIANCE

Board of Managers  
Red Lake Watershed District  
Thief River Falls, Minnesota 56701

We have audited the financial statements of the Red Lake Watershed District, as of and for the year ended December 31, 2012, and have issued our report thereon dated March 7, 2013. The District prepares its financial statements on the modified cash basis, which is a comprehensive basis of accounting other than generally accepted accounting principles.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the comptroller general of the United States and the provisions of the *Minnesota Legal Compliance Audit Guide for Political Subdivisions*, promulgated by the Legal Compliance Task Force pursuant to Minn. Stat. 6.65. Accordingly, the audit included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

The *Minnesota Legal Compliance Audit Guide for Political Subdivisions* covers six main categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, miscellaneous provisions and TIF district. Our study included all of the listed categories, except TIF which was not applicable to the District.

The results of our tests indicate that for the items tested the Red Lake Watershed District complied with the material terms and conditions of applicable legal provisions. Further, for the items not tested, based on our audit and the procedures referred to above, nothing came to our attention to indicate that the Red Lake Watershed District had not complied with such legal provisions.

This report is intended solely for the information and use of the District Board of Managers, management, and the Office of the State Auditor of Minnesota and is not intended to be and should not be used by anyone other than these specified parties.

DREES, RISKEY & VALLAGER, LTD.

Certified Public Accountants

March 7, 2013  
Crookston, Minnesota

**Drees, Risky & Vallager, Ltd.**  
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REPORT ON COMPLIANCE AND 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 Auditors' Report

Board of Managers  
Red Lake Watershed District  
Thief River Falls, Minnesota 56701

We have audited, in accordance with the 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 Red Lake Watershed District, as of and for the year ended December 31, 2012 and the related notes to the financial statements, which collectively comprise District's basic financial statements, and have issued our report thereon dated March 7, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered District's internal control over financial reporting (internal control) 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 District's internal control. Accordingly, we do not express an opinion on the effectiveness of Red Lake Watershed District's internal control.

A *deficiency in internal control* 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 a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance

*Members of Minnesota and North Dakota Society of CPA's  
Members of American Institute of Certified Public Accountants*

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We identified a deficiency in internal control, described in the accompanying schedule of findings and responses that we considered to be a significant deficiency in internal control over financial reporting, 2012-1.

#### Compliance and Other Matters

As part of obtaining reasonable assurance about whether the District'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*.

#### Response to Findings

The Red Lake Watershed District's response to the findings identified in our audit is described in the accompanying schedule of findings and responses. Red Lake Watershed District's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

#### Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

DREES, RISKEY & VALLAGER, LTD.

Certified Public Accountants

March 7, 2013  
Crookston, Minnesota

RED LAKE WATERSHED DISTRICT  
SCHEDULE OF FINDINGS AND RESPONSES  
FOR THE YEAR ENDED DECEMBER 31, 2012

Deficiency 2012-1

Condition: An internal control deficiency over financial reporting may be determined present in the absence of the District's preparation of its financial statements.

Cause: Due to limited personnel as auditors we were requested to draft the financial statements and accompanying notes to the financial statements.

Effect: A material misstatement in the District's financial statements may go undetected.

Recommendation: It is the decision of the board charged with governance to evaluate the degree of risk associated with this condition upon consideration of benefits received and cost associated with making the necessary changes.

Management's Response: We concur with the auditors finding and will continue to evaluate the risks and costs associated with the District's financial statement preparation.